



*Advancing Economic Security
and Community Prosperity*

July 1, 2020

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Chair Jelena McWilliams
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

RE: ***Industrial Loan Corporation (ILC) Regulations***
RIN 3064-AF31

Dear Chair McWilliams:

Woodstock Institute submits these comments in response to the FDIC's Notice of Proposed Rulemaking regarding the ILC charter. Our primary concern pertains to the Community Reinvestment Act (CRA) and the degree to which the ILC is a mechanism for internet companies to exploit a well-known defect in the CRA regulations – that defect being the method for delineating CRA assessment areas based solely on brick-and-mortar locations. The FDIC is under no statutory mandate to grant ILC charters according to any particular schedule or to complete the ILC rulemaking within any specific timeframe. Therefore, the FDIC should wait until the CRA assessment area regulations, which are in a radical state of flux, are modernized before completing the ILC rulemaking and granting any more ILC charters.

About Woodstock Institute

Woodstock Institute's mission is to create a just financial system in which lower-wealth persons and communities and people and communities of color can achieve economic security and community prosperity. Since its foundation in 1973, Woodstock Institute has been a recognized leader in building bridges between low- and moderate-income communities, financial institutions, regulators, and policymakers. We conduct high-quality research on financial products, services, investments, and policies at the local, state, and national levels. Our findings and recommendations inform and influence efforts to build a more equitable financial system.

Assessment Area Modernization Must Come First

In exchange for the privilege of a federal bank charter, including an ILC charter, and the corresponding privilege of federal preemption of state laws, among other privileges, a bank should have a robust plan to lend to, invest in, and serve the communities among which the bank does business, especially underserved low- and moderate-income (LMI) communities. Federal preemption, standing alone, creates a strong incentive for internet companies to become ILCs. For example, internet companies, or "fintechs," are precisely the type of company that was

intended to be covered by California’s SB 1235 (Chapter 11, Statutes of 2018), which requires online small business lenders to disclose the annual percentage rate (APR) of their products. Fintechs that become ILCs gain an exemption from this law.

In the wake of COVID-19’s devastation, LMI communities’ need for reinvestment has become more urgent. The CRA is a tool to help spur reinvestment by banks, but in the case of companies that do substantially all of their business on the internet, the CRA doesn’t work. Delineating an assessment area around a single headquarters, for example, is practically meaningless, especially if the area is like Salt Lake City, which is a desirable location to headquarter due to its labor market but is a CRA “hot spot.”¹ We believe the top priority should be modernizing assessment areas to help steer more bank activity to LMI communities that are struggling to survive the pandemic and the historic civil unrest.

The FDIC and the Office of the Comptroller of the Currency (OCC) recognized the CRA’s assessment area defect when it proposed a modernization framework “to recognize the evolution of modern banking (including the emergence of internet banks).”² The FDIC/OCC proposal, finalized by the OCC on May 20, 2020, would have established deposit-based assessment areas. Woodstock Institute’s official comment on the proposed deposit-based approach said it would “move us in the right direction” given how assessment area reform is “long overdue.”³ Practically anything beyond the current method for delineating assessment areas would be an improvement, but a lending-based approach would make more sense for various reasons, especially in the case of internet lenders seeking to become ILCs. (We support the FDIC’s decision not to join the OCC in finalizing the modernization rulemaking due to other parts of the rule that we believe undermine the CRA’s purpose.)

The Case of Square

The recently approved application of Square Financial Services, Inc. to become an ILC represents a good example of the assessment area defect. Absent regulations requiring Square to develop a CRA plan that actually aligns with the communities it serves – or, put another way, a CRA plan that is not out-of-touch with reality – Square’s CRA plan piles more CRA activity onto Salt Lake City.⁴ Woodstock participated in a coalition of groups led by the California Reinvestment Coalition to try to convince Square to voluntarily adopt a robust plan that included meaningful CRA commitments to the markets it serves.⁵ Square refused. Instead, Square is moving forward – with the FDIC’s blessing – with a plan to invest in Salt Lake City and to provide financial education nationwide focused on small business. In our view, such a plan is wholly inadequate. Granting ILC charters to internet companies that hinge on an out-of-date and ineffectual method of establishing assessment areas is contrary to the purposes of the CRA and is doing a disservice to the communities that do business with these companies, especially LMI communities.

Delay Further Actions that Hinge on Regulations in Flux

The preceding section addressed our substantive concern with the rulemaking as it pertains to LMI communities, but there is also a procedural concern regarding any rulemaking that is conjoined to an unstable regulatory framework. Specifically, the ILC charter is linked to the CRA, and the CRA is in the

¹Susan Wachter, *Modernizing the CRA (While Preserving Its Spirit)*, PennIUR Policy Brief, at 5 (Dec. 2019). https://pennjur.upenn.edu/uploads/media/Modernizing_the_CRA.pdf

²85 FR 1208.

³Brent Adams, Woodstock Institute, Official Comment to FDIC and OCC re: CRA Regulations (Apr. 8, 2020).

⁴Square, Inc., Community Reinvestment Strategic Plan (Draft), Application to FDIC to establish Square Financial Services, Inc. (Dec. 19, 2018). <https://californiareinvestmentcoalition.app.box.com/s/kjxbseizxdkql8r8gb8d776o60txh93>

⁵California Reinvestment Coalition (co-signed by 36 groups), Letter to FDIC Regional Director Kathy Moe: *Community Group Opposition to Square Application for ILC Charter*, Feb. 19, 2019. <http://calreinvest.org/wp-content/uploads/2019/02/Community-groups-opposition-to-Square-ILC-charter-application-2.19.19.pdf>

midst of a seismic transition. The CRA regulations are not merely in the “active discussion” phase. The OCC, by finalizing a CRA modernization rule without the agreement of the FDIC or the Federal Reserve, created, in the words of one commenter, a “regulatory mess.”⁶ This mess extends to ILC charters by virtue of ILCs’ CRA requirement.

The FDIC’s *Interagency Charter and Federal Deposit Insurance Application*⁷ requires applicants to submit their CRA plan to enable the FDIC to assess whether the proposed ILC will serve the “convenience and needs of the community to be served.” Internet companies like Square intend to “serve,” i.e., do business with, a community far more vast than Salt Lake City, and the regulatory meaning of “CRA plan” has been radically altered by the OCC’s CRA Rule. In other words, the “convenience and needs” requirement for an ILC charter is internally inconsistent. The term “community” now has at least three different meanings: (1) what it actually means, (2) the facility-based meaning, and (3) the OCC meaning, which is facility-based and deposit-based. Finalizing the ILC charter rulemaking at this time is analogous to building more structures on a foundation known to be unstable.

We urge you to suspend additional ILC approvals and delay finalizing the ILC rulemaking until the CRA rulemaking is settled. Only then will you have a complete and accurate picture of the regulatory framework to which the ILC framework is linked. Changing the CRA impacts the ILC charter, but changing the ILC charter does not impact the CRA. Therefore, it make sense to finalize the CRA regulations *before* turning to the ILC regulations.

Thank you for the opportunity to provide this comment.

Be well,



Brent E. Adams

About the Author

Brent Adams, Woodstock’s Senior Vice President of Policy & Communication, has 13 years of experience in the financial services area. He has worked as a policy analyst and advocate, drafting and helping to pass the State’s Payday Loan Reform Act of 2005 and major reforms to the State’s check-cashing law in 2018. He has also served as the State’s chief regulatory official from 2009 to 2012 during which he oversaw most licensed professions and the state banking system.

⁶Jesse Van Tohl, NCRC, *OCC Announces Final CRA Rule Changes, Moves Alone, Without FDIC or Federal Reserve* (press release) (May 20, 2020). <https://ncrc.org/occ-announces-final-cra-rule-changes-moves-alone-without-fdic-or-federal-reserve/>
⁷<https://www.fdic.gov/formsdocuments/interagencycharter-insuranceapplication.pdf>