



## Congressman James A. Leach

For Immediate Release

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### **Greenspan Warns Congress on Industrial Loan Corporations**

Washington, Jan. 25 -- In possibly his last communication to the Congress in his role as Fed chairman, Alan Greenspan called today for sweeping reform of industrial loan corporations.

Presenting the views of the Federal Reserve Board, Greenspan endorsed the legislative approach offered by Representative Jim Leach (R-IA), which places ILCs under the supervisory requirements of the Bank Holding Company Act.

Greenspan expressed concern that ILCs, which are FDIC-insured banks chartered in a handful of states, represent a breach in the traditional separation of banking and commerce in United States. Under a special exemption in federal banking law adopted in 1987, ILCs may be acquired by any type of company, including a commercial business or foreign bank. Unlike financial institutions with banking subsidiaries, owners of ILCs are currently not subject to the supervisory requirements of the Bank Holding Company Act.

“The construct of the financial modernization act known as Gramm-Leach-Bliley is that there be no merging of commerce and banking,” Leach said. “The bizarre loophole that allows commercial companies to breach the separation of commerce and banking through a statute limited to a handful of states creates inequities in industry regulation and state authority. It is an anomaly that deserves review by Congress,” Leach added.

Greenspan pointed out in his letter to Leach that the assets held by ILCs have grown by 3,500 percent between 1987 and 2004 to \$140 billion. In Utah alone, the number of ILCs has doubled since 1997 and the aggregate amount of assets controlled by Utah-chartered ILCs now is more than 16 times the total of all the banks, savings associations and credit unions chartered in that state. One ILC now has more than \$58 billion in assets and more than \$50 billion in deposits. Seven other ILCs have more than \$1 billion in deposits each.

“The character, powers and ownership of ILCs have changed materially since Congress first enacted the ILC exemption. These changes are undermining the prudential

framework that Congress has carefully crafted and developed for the corporate owners of other full-service banks,” Greenspan wrote. “Importantly, these changes also threaten to remove Congress’ ability to determine the direction of our nation’s financial system with regard to the mixing of banking and commerce and the appropriate framework of prudential supervision. These are crucial decisions...they should not be made through the expansion and exploitation of a loophole that is available to only one type of institution chartered in a handful of states.”

Greenspan warned that without legislation, ILCs are likely to proliferate. “In 1997, for example,” Greenspan said, “Utah lifted its moratorium on the chartering of new ILCs, allowed ILCs to call themselves ‘banks,’ and permitted ILCs to exercise virtually all of the powers of state-chartered commercial banks. In addition, Utah and certain other grandfathered states have since begun actively to charter new ILCs and promote ILCs as a method for companies to acquire a bank while avoiding the requirements of the BHC Act. As a result, recently there has been a significant change in the number, size and nature of ILCs operation under the exemption.”

Legislation introduced by Leach, H.R. 3882, would subject owners of ILCs to the same prudential constraints -- including consolidated supervisory requirements, bank-level capital, managerial criteria, enforcement mechanism and activity limitations -- as those that apply to financial holding companies. Such an approach, Greenspan wrote, would “address the Board’s concerns and ensure a fair and level playing field for all banking organizations.”

The General Accountability Office, at Leach’s request, also conducted a lengthy investigation to determine whether ILCs and the organizations that own them are adequately regulated under current law. GAO concluded that they are not. Like the Federal Reserve Board, GAO, in a comprehensive report issued in September, urged Congress to fill the regulatory gaps.

“In these perilous economic times, we as a Congress cannot afford to do anything except promote prudential financial oversight,” Leach said. “It cannot be stressed enough that the issue is not Wal-Mart’s application to control an ILC as much as it is the nature of the American economy and whether through a refusal to act Congress precipitates a Japanese, *kereitsu*-like web of financial and commercial cross-ownerships.”

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Greenspan letter and analysis are attached.