

EnerBank - Response to Request for Proposals to Foster Economic Growth

1. Brief description

The Volcker Rule applies to the parent companies of industrial loan companies (“ILCs”), even if they are non-financial (e.g. utility company, motorcycle manufacturer, provider of postal services, etc.). Investors in the non-financial parents of ILCs may also be subject to the rule simply by owning enough stock to be deemed in "control" of the ILC. Generally, "control" is presumed at 10% ownership but could apply to as little as 5%. Large institutional investors will avoid increasing its investment above 10% due to the fear that it might trigger application of the Volcker Rule.

In fact, EnerBank’s parent company, CMS Energy, had a large mutual fund shareholder that wanted to increase its ownership above 10% but was advised against it by its legal counsel due to concerns about application of the Volcker Rule. There is a real concern that many more investors are deterred from increasing their investment without CMS Energy ever having knowledge of the situation. This unintended consequence negatively impacts ILC parent company's ability to access capital and harms its ability to meet Main Street customer demand.

As background, ILCs are state-chartered depository institutions that operate with limited powers under state law and they are companies for which there is a special exemption under the Bank Holding Company Act (“BHCA”). Specifically, the exemption provides that a company that controls an ILC is not subject to the BHCA and supervision by the Federal Reserve and the company is not subject to restrictions on its permissible scope of activities (ILC parent companies are, however, subject to examination and supervision by state banking authorities).. Nevertheless, one section of the BHCA, the Volcker Rule, can be viewed as applying to ILC and their affiliates because of the definition of “banking entities” under the Volcker Rule. The Volcker Rule applies to any “banking entity,” which is defined broadly to include an insured depository institution, including ILCs and all of their affiliates. By incorporating banking law definitions of “affiliate” and “control,” the Volcker Rule applies to the entire company complex to which an insured depository institution belongs--any entity that controls, is controlled by, or is under common control with a banking entity also is a banking entity. Consequently, even though special-purpose banks, such as ILCs, are not “banks” under the BHCA, they and all of their affiliates are banking entities under the Volcker Rule.

Under the BHCA, an investor owning less than 5 percent of the voting stock of a bank or bank holding company is presumed not to “control” the banking entity and an investor owning 25 percent or more of the voting stock of the bank or company is determined conclusively to “control” the bank or company. Individual facts and circumstances determine whether an investor owning between 5 and 25 percent has control. As a result, an investor owning between

5 and 25 percent of a company that owns an industrial loan company or a credit card bank faces uncertainty as to whether it indirectly “controls” the industrial loan company or credit card bank and is, therefore, subject to the Volcker Rule.

We proposed the following narrowly tailored solution to fix this unintended consequence of the Volcker Rule:

1) Amend the definition of “banking entity” under the Volcker Rule to exclude corporate parents of banks that are not predominately engaged in financial activities and not BHCs (*see* section 4 for legislative language).

2. Impact on economic growth/ Impact on the ability of consumer market participants and financial companies to participate in the economy

The demand for ILC banking services requires that parents of ILCs are able to access the capital markets. When their ability to do so is hindered it has the downstream impact of limiting access to the broad array of products and services for consumers nationwide, including some of the most underserved segments of the U.S. economy. For example, ILCs provide financing to the following markets:

- Home improvement contractors offering financing of energy efficient products (e.g. new windows, solar panels, etc.),
- Taxi drivers purchasing medallions,
- Postage buyers,
- Credit cards for small businesses, and
- Financial services to truckers

When these Main Street consumers and business are better able to obtain credit it affords them the opportunity to grow and participate in the economy.

3. Other background material as appropriate

- Appendix A - Letter sent by House Financial Services Committee Chairman Jeb Hensarling and Representative Mia Love to Federal Reserve Chair Janet Yellen regarding ILCs and the Volcker Rule
- Appendix B - Response letter from Federal Reserve Chair Janet Yellen to Representative Mia Love
- Appendix C - Support letter signed by the National Association of Industrial Bankers and Utah Bankers Association
- Appendix D - National Association of Industrial Bankers primer on ILCs

4. Legislative language

SECTION 1. TREATMENT OF CERTAIN NON-FINANCIAL COMPANIES.

Section 13(h)(1) of the Bank Holding Company Act of 1956 (12 U.S.C. 1851(h)(1)) is amended— (1) in subparagraph (D), by redesignating clauses (i) and (ii) as subclauses (I) and (II), respectively, and moving such subclauses 2 ems to the right; (2) by redesignating subparagraphs (A), (B), (C), and (D) as clauses (i), (ii), (iii), and (iv), respectively, and moving such clauses 2 ems to the right; (3) by striking “The term” and inserting the following:

“(A) IN GENERAL.—The term”;

“(B) CERTAIN NON-FINANCIAL COMPANIES.—Notwithstanding subparagraph (A) the term ‘banking entity’ does not include any entity that—

‘(i)(I) is not predominantly engaged in financial activities, as defined under section 102 of the Financial Stability Act of 2010 (12 U.S.C. 5311);

“(II) is not a bank holding company or a nonbank financial company supervised by the Board; and

“(III) is not a direct or indirect subsidiary of a bank holding company or a nonbank financial company supervised by the Board; or “(ii) would be a banking entity solely due to its control of an entity described under clause (i).”.