

SoFi's bid to become an industrial bank pulls FDIC into fintech fray

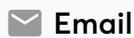
By **Kevin Wack**

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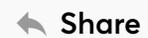
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The Federal Deposit Insurance Corp. has so far managed to stay out of the growing battle over how the U.S. fintech sector should be regulated, but that appears likely to end as one of the nation's largest online lenders announced plans to apply for a specialty banking charter soon.

Social Finance Inc., the San Francisco-based consumer lender known as SoFi, hopes to secure an industrial bank charter. That state-issued charter used to be a popular way to organize a bank, and was commonly used by companies that are not primarily in the financial services industry, but it fell out of political favor when Walmart tried unsuccessfully to obtain a charter over a decade ago.

To obtain the charter, SoFi will need to get FDIC approval, which may be tough, according to industry lawyers. Not a single industrial loan company application has been filed since 2009, a period of time that includes a three-year moratorium imposed by the Dodd-Frank Act.

"The signals from the FDIC still are not conducive," said Frank Pignanelli, a partner at Foxley & Pignanelli in Utah, where many of the remaining industrial banks have charters. "We're hopeful that over time the FDIC does change its perspective."



"This is going to be the biggest challenge with the FDIC, and absolutely something the FDIC has to take into consideration," said SoFi CEO Mike Cagney.

Bloomberg News

In testimony before the House Oversight Committee last July, FDIC Chairman Martin Gruenberg said that the agency welcomes applications for deposit insurance. At the same time, he stated that industrial banks must meet the same standards as any other FDIC-insured bank, including minimum capital standards, the disclosure of insider transactions and financial audit requirements.

The congressional hearing was convened by Rep. Jason Chaffetz, R-Utah, who questioned whether red tape at the FDIC has been discouraging applications. At the time, concerns about the dearth of new industrial banks were largely confined to Utah, which was once home to a thriving industrial bank sector.

But SoFi's plan to apply for a new charter raises the stakes considerably. If the company's application gets approved, other online lenders that are unsatisfied with their existing regulatory options may look to follow SoFi's lead.

"It is time someone in the fintech space bit the bullet, applied to the regulators and forced the issue on the issuance of bank-type charters to fintech companies," said Todd Baker, a senior fellow at Harvard's John F. Kennedy School of Government, in an email.

Today, many U.S. online lenders partner with banks that issue loans on their behalf in an effort to avoid state interest rate caps. But those arrangements have gotten pushback from the courts.

Other online lenders get licensed in every state where they make loans, which can be a costly, duplicative and time-consuming endeavor.

Against that backdrop, the Office of the Comptroller of the Currency has proposed establishing a special charter for fintech firms. But the future of that effort is up in the air following the recent departure of Comptroller Thomas Curry, who championed the new charter.

What's more, the OCC's push to establish a new fintech charter has encountered fierce resistance [from the states](#), which fear encroachment by the federal government. The states have filed two lawsuits against the OCC and [launched their own effort](#) to harmonize registration and supervision across states. Consumer advocates also object to the OCC plan on the grounds that the new federal charter would offer a way for digital lenders to avoid state interest rate caps.

SoFi's application for an industrial bank charter is likely to thrust the FDIC into the middle of this controversy. Ultimately, the decision may fall to a Trump administration appointee. The term for Gruenberg, a former aide to Democratic Sen. Paul Sarbanes who has chaired the agency since 2012, expires in November.

FDIC spokesman David Barr declined to comment for this article.

Meanwhile, SoFi CEO Mike Cagney acknowledged that his firm's application has implications beyond his own company, which raises the stakes for the FDIC.

"I think this is going to be the biggest challenge with the FDIC, and absolutely something the FDIC has to take into consideration," [Cagney told TechCrunch](#), which first reported SoFi's plan to apply for a banking charter.

SoFi was founded in 2011 and has since funded \$18 billion in student loans, personal loans and mortgages. The firm aims to become a full-service financial services provider to its young, well-heeled consumers. To that end, SoFi [recently purchased Zenbanx](#), which offers mobile phone-based deposit accounts.

For SoFi, the decision to apply for an industrial bank charter is a watershed moment. Cagney once famously said that he wants to “kill banks.” But joining their ranks has become more attractive at a time when SoFi is looking to add deposit products and credit cards.

“He simply can’t run his business without a bank long-term,” said Brendan Ross, CEO of Direct Lending Investments, which purchases online loans.

If SoFi’s application for an industrial bank charter gets approved, the privately held firm will be able to collect FDIC-insured deposits. If it gets rejected, SoFi can instead continue a partnership that Zenbanx established with WSFS Bank in Delaware.

For SoFi, securing an industrial bank charter holds certain advantages over other types of banking charters, observers said. Crucially, the firm would not be subject to the Bank Holding Company Act, a law that would impose a raft of new burdens on companies that own stakes in SoFi. The company would also avoid oversight by the Federal Reserve Board.

The OCC is not yet taking applications for its proposed fintech charter. But even if it were, that option would likely be a poor fit for SoFi, since the OCC’s charter will not come with deposit insurance.

SoFi declined to comment for this article.

The industrial bank charter has been a source of controversy in the past. In the mid-2000s, the retail behemoth Walmart applied for the charter but encountered fierce backlash from the banking industry.

Among the banking groups that opposed Walmart’s application was the Independent Community Bankers of America. The ICBA has yet to decide whether it will oppose SoFi’s application, according to Christopher Cole, the group’s senior regulatory counsel.

Cole said there are important differences between SoFi’s application and Walmart’s, including the fact that SoFi is not a retailer. But he added, “We are still concerned about any expansion of the ILC charter.”

Mary Wisniewski contributed to this report.



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