

Statement by Martin J. Gruenberg, Member, FDIC Board of Directors; Deposit Insurance Application: Nelnet Bank (In Organization)

Last Updated: March 18, 2020

The FDIC Board of Directors today is considering an application for deposit insurance for Nelnet Bank (Nelnet Bank or the Bank), which would be a newly-chartered Utah industrial bank headquartered in the Salt Lake City, Utah area, wholly owned by Nelnet, Inc. (Nelnet). While Nelnet's activities are mainly financial in nature, it would not qualify for status as a bank holding company and ownership of a commercial bank because of its non-financial activities. However, the Bank Holding Company Act provides an exception for owning an industrial bank without becoming a bank holding company.¹

Under Section 5(a) of the Federal Deposit Insurance Act, the FDIC Board of Directors is authorized to approve or deny applications for Federal deposit insurance.² Pursuant to a resolution adopted in September 2007, the FDIC Board has reserved the authority to act on applications for Federal deposit insurance from proposed industrial banks and industrial loan companies,³ leading to the Board's consideration today of this application.

For the reasons outlined below, this application meets the statutory requirements, including source of financial strength, for approval of deposit insurance. For that reason, I will vote in favor of this application.

Overview of Nelnet, Inc.⁴

Nelnet, Inc., is a \$24 billion, publicly traded financial and technological services company providing education-related products and services to students, families, schools, and financial institutions. Nelnet, Inc. was founded in 1978 to service federal student loans. In the years following its founding, Nelnet became a leading originator, holder, and servicer of federal student loans. In 2010, however, the federal law was changed to discontinue new loan originations by private firms. That served as an impetus for Nelnet to seek to establish a bank to originate private student loans.

Nelnet seeks to establish an internet-based industrial bank in which it would originate, refinance, and service private student and consumer loans and offer deposit products nationwide.

The proposed Bank would operate from a single location, and plans to market its lending products through various channels, including the internet, direct mail and direct to consumer marketing as well as campus-based marketing, and marketing to families using other Nelnet products and services. The Bank expects to offer deposit products as companion products to lending products and would develop a deposit base through Nelnet's existing client relationships within other lines of business.

Source of Financial Strength

Section 38A of the Federal Deposit Insurance Act includes the following requirement:

"If an insured depository institution is not the subsidiary of a bank holding company..., the appropriate Federal banking agency for the insured depository institution shall require any company that directly or indirectly controls the insured depository institution to serve as a source of financial strength for such institution."⁵

The law also states:

"...the term 'source of financial strength' means the ability of a company that directly or indirectly owns or controls an insured depository institution to provide financial assistance to such insured depository institution in the event of the financial distress of the insured depository institution."⁶

Nelnet, Inc.'s financial statements are publicly reported.⁷ It has recorded a profit every year since its initial public offering in 2003, including during the recession following the financial crisis of 2008.

Nelnet, Inc.'s significant history of performance and profitability support its ability to serve as a source of financial strength for the proposed Bank.

Statutory Factors and FDIC Conditions

In addition to the "source of financial strength" requirement, Section 6 of the Federal Deposit Insurance Act⁸ requires the FDIC to consider seven factors when reviewing an application for deposit insurance:

- (1) the financial history and condition of the depository institution,
- (2) the adequacy of the depository institution's capital structure,
- (3) the future earnings prospects of the depository institution,
- (4) the general character and fitness of its management,
- (5) the risk presented by such depository institution to the Deposit Insurance Fund,
- (6) the convenience and needs of the community to be served by the depository institution,
- (7) whether the depository institution's corporate powers are consistent with the purposes of the FDI Act.

The FDIC's review of the seven statutory factors was favorable. Capital and management were considered satisfactory, future earnings prospects favorable, and no undue risk to the Deposit

Insurance Fund was apparent. Nelnet, Inc. is affiliated with a chain banking organization consisting of six state-chartered banks with combined assets of more than \$6 billion that has had a positive record of performance for over 25 years.

In order to ensure that the proposed Bank maintains sufficient capital and liquidity, approval of the application is conditioned upon the proposed Bank, Nelnet, Inc. and the controlling shareholder of Nelnet, Inc. executing a Capital and Liquidity Maintenance Agreement (CALMA), and a Parent Company Agreement (PCA).

The Capital and Liquidity Maintenance Agreement would require that Nelnet:

- Maintain a 12 percent leverage ratio at all times.
- Contribute sufficient capital to bring the Bank into compliance should the Bank's leverage ratio drop below the required minimum.
- Provide financial support to ensure that the Bank can meet its short-term and long-term liquidity needs.
- Establish and maintain a \$40 million deposit account at the Bank that would be accessible to the Bank in the event Nelnet failed to provide the capital and liquidity support required in the CALMA.

The Parent Company Agreement would require that Nelnet:

- Maintain the Bank's capital and liquidity at such levels reflected in the CALMA.
- Provide an annual listing of its subsidiaries and other reports that the FDIC may request.
- Consent to the FDIC's examination of Nelnet and its subsidiaries.
- Limit its representation on the Bank's board of directors to no more than 25 percent.
- Adopt a contingency plan that describes actions Nelnet would take if it were ultimately unable to serve as a source of strength; and sets forth options for the orderly wind down of the Bank through liquidation, sale, or merger, without entering receivership.

Conclusion

Nelnet's deposit insurance application, subject to certain conditions, appears to demonstrate both that Nelnet, Inc. can meet the source of financial strength requirement for the parent of the proposed Bank, as well as the seven statutory factors the FDIC is required to consider for deposit insurance applications.

It should be noted that the FDIC Board resolution to approve this application would delegate to staff authority to modify or dispose of the conditions, on which approval is contingent, without

review and approval by the Board. This is contrary to the resolution adopted by the FDIC Board in 2007 reserving to the Board approval of ILC applications.

However, since the underlying application appears to meet the statutory requirements, I will vote to approve this application.

¹12 U.S.C. 1841(c)(2)(H).

²12 U.S.C. 1815(a).

³FDIC Board Resolution bearing Seal Number 075095 (Sept. 11, 2007).

⁴See Nelnet Bank Interagency Charter and Federal Deposit Insurance Application Part 1 (Public Information), submitted Nov. 12, 2019 and various public filings with the Securities and Exchange Commission, such as 10-Ks, to be found at www.sec.gov.

⁵12 U.S.C. 1831o-1(b).

⁶12 U.S.C. 1831o-1(e).

⁷Available at <http://www.nelnetinvestors.com/financial-information/sec-filings/default.aspx>.

⁸12 U.S.C. 1816.