Statement by Vice Chairman Travis Hill on the FDIC's Proposed Statement of Policy on Bank Merger Transactions

March 21, 2024

I agree that the FDIC's merger approval process needs to be reevaluated and refreshed. Currently, when we receive certain types of merger applications, our process too often breaks down. It takes far too long, with too many hurdles, and is too unpredictable. The process can be damaging for the institutions involved, as they lose employees and customers, and, if the merger is approved, extended delays can make integration more challenging. If the target institution is in a vulnerable state, lengthy timelines can be dangerous, as the institution's condition may deteriorate while the application is in limbo, and if the merger is ultimately denied, there may be no alternative options left, as no other potential buyers want to risk waiting more than a year just to get an answer.

The proposed Statement of Policy (SOP) under consideration today moves in the wrong direction, potentially making the process longer, more difficult, and less predictable. I appreciate that the FDIC plays an important role in evaluating bank merger applications, including by making sure the acquiring institution has the financial and operational capacity to absorb the target firm. But I will vote against the proposed SOP, for the reasons discussed below.

Competition

The SOP would revise how the FDIC evaluates the competitive effects of a merger[1] and add considerable unpredictability to the analysis. The proposal appears to deemphasize the use of HHI thresholds, which have long served as a predictable proxy for concentrations,[2] and further adds that the FDIC "will consider concentrations beyond those based on deposits" and

[1] The Bank Merger Act prohibits the FDIC from approving a merger that "would result in a monopoly, or which would be in furtherance of any combination or conspiracy to monopolize or to attempt to monopolize the business of banking in any part of the United States" or "whose effect in any section of the country may be substantially to lessen competition, or to tend to create a monopoly, or which in any other manner would be in restraint of trade, unless it finds that the anticompetitive effects of the proposed transaction are clearly outweighed in the public interest by the probable effect of the transaction in meeting the convenience and needs of the community to be served." 12 U.S.C. § 1828(c)(5).

[2] *See, e.g.,* Federal Deposit Insurance Corporation, *Applications Procedures Manual—Section 4: Mergers* (Applications Manual), p. 19 ("The FDIC normally will not deny a proposed merger transaction on competitive grounds (absent objection from the DOJ) when the post-merger HHI in each [Relevant Geographic Market] is 1,800 or less or, if more than 1,800, reflects an increase of less than 200 points from the pre-merger HHI."); Federal Deposit Insurance Corporation, Statement of Policy on Bank Merger Transactions, p. 1 ("The FDIC normally will not find unfavorably on the competitive effects of a proposed merger transaction on antitrust grounds (absent objection from the Department of Justice) if the post-merger HHI in the relevant geographic market(s) is 1,800 points or less or, if it is more than 1,800, it reflects an increase of less than 200 points from the pre-merger HHI. If a proposed merger transaction fails this initial concentration test, the FDIC will consider more closely the various competitive dynamics at work in the market, taking into account a variety of factors that may be especially relevant and important in a particular proposal. . . .").

"may consider concentrations in any specific products or customer segments."[3] The SOP gives little clarity on how the agency will decide what products to look at, how such products might be segmented by customer, and how such analysis would feed into the agency's final conclusions.

Ultimately, when evaluating the competitive effects of a merger, we should remember that banking has changed dramatically since the bank merger framework was first put in place, when banking was generally a much more local business with heavy restrictions on banks' ability to expand geographically.[4] Today, banking and financial services are generally extremely competitive, with a wide range of readily substitutable financial products and services offered on the internet available anywhere in America.[5]

The SOP also notes that the FDIC "may require divestitures of business lines, branches, or portions thereof" prior to the consummation of a merger to mitigate competitive concerns.[6] Requiring divestitures in advance of the merger may add significant delays to the merger process. Meanwhile, failing to successfully divest post-merger is extremely rare, and the FDIC has other supervisory tools to address such a concern.[7] Furthermore, the SOP would generally prohibit non-compete agreements with employees of a divested entity,[8] a policy which seems far outside the FDIC's jurisdiction and expertise.

Financial Resources

The SOP also states, "[g]enerally, the FDIC will not find favorably on the financial resources factor if the merger would result in a weaker IDI from an overall financial perspective."[9] If interpreted literally, this could effectively serve as a prohibition on a broad range of bank mergers. As a general matter, any time an acquiring institution is on stronger financial footing than a target institution, the resulting IDI will initially look worse from a balance sheet perspective. Furthermore, accounting rules generally require an acquiring bank to

---

[3] Federal Deposit Insurance Corporation, Proposed Statement of Policy on Bank Merger Transactions (SOP), p. 88.

[4] As the Supreme Court noted in 1963, "In banking, as in most service industries, convenience of location is essential to effective competition. Individuals and corporations typically confer the bulk of their patronage on banks in their local community; they find it impractical to conduct their banking business at a distance." *U.S. v. Philadelphia Nat'l Bank*, 374 U.S. 321, 358 (1963) (citation omitted).

[5] *See, e.g.,* Travis Hill, *Insights on the FDIC's Agenda* (September 21, 2023) ("While not all banks compete nationwide, all banks in effect compete with those who do.").

[6] SOP, *supra* note 3, at 88.

[7] As the SOP states, "As appropriate, claims and commitments made by the applicant to the FDIC may be included in the Order and Basis for Approval, and the FDIC's ongoing supervisory efforts will evaluate the IDI's adherence to any such claims and commitments." *Id.* at 52.

[8] *See id*. at 88.

[9] *Id*. at 89.

recognize the target's assets and liabilities at fair value, which, in the current environment, often guarantees that the resulting institution will look weaker financially on day one post-merger.[10]

This issue is further exacerbated by the SOP's provision that the FDIC "will not use conditions as a means for favorably resolving any statutory factors that otherwise present material concerns,"[11] which suggests applicants could not, for example, raise outside capital to ensure the resulting institution would be stronger from a financial perspective. More generally, why would the FDIC reject efforts by applicants to address or mitigate concerns that arise during the process?[12]

Financial Stability

Next I'll turn to the financial stability factor.[13] While the analysis in the SOP focuses narrowly on the potential financial stability risks presented by the resulting institution, I think we should consider explicitly focusing on a before-and-after comparison, one that compares the financial stability risks presented by the two stand-alone banks to those presented by the resulting institution. For example, if a large bank acquires a very small bank, it might be the case that the acquisition has no material impact whatsoever on the risk to financial stability presented by the large bank, even if the resulting institution has attributes suggesting an unfavorable finding under the framework described in the SOP.

To give another example, there may be instances in which a strong large bank purchasing a weak large bank would be quite helpful from a financial stability perspective. Last year, if a bank had been willing and able to buy First Republic on an open-bank basis, assuming the acquiring institution had the financial and operational capacity to do so, this would have been an unequivocal positive for financial stability, regardless of how the resulting institution measured

---

[10] *See* Instructions for Preparation of Consolidated Reports of Condition and Income, Glossary, at A-20b (". . . [T]he acquirer in a business combination shall measure the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree at their acquisition-date fair values (with limited exceptions specified in ASC Topic 805) . . . .").

[11] SOP, *supra* note 3, at 84.

[12] By contrast, the proposed Statement of Policy recently released by the OCC suggests that concerns can be "addressed or remediated." *See* Office of the Comptroller of the Currency, Business Combinations Under the Bank Merger Act, 89 Fed. Reg. 10,010, 10,016 (Feb. 13, 2024) ("If certain indicators that raise supervisory or regulatory concerns are present, the OCC is unlikely to find that the statutory factors under the BMA are consistent with approval unless and until the applicant has adequately addressed or remediated the concern."). *See also id.* at 10,017 ("The OCC may impose conditions, enforceable under 12 U.S.C. 1818, to address and mitigate financial stability risk concerns, such as requiring asset divestitures by the resulting institution, imposing higher minimum capital requirements, or imposing other financial stability related conditions.").

[13] The Dodd-Frank Act added to the Bank Merger Act a requirement that the FDIC consider "the risk to the stability of the United States banking or financial system" when evaluating a bank merger. 12 U.S.C. § 1828(c)(5). The SOP describes how the FDIC will evaluate this factor, listing the same five considerations currently enumerated in the FDIC's Application Manual (*see* Applications Manual, *supra* note 2) and described in orders approving mergers of large banks (*see, e.g.,* Federal Deposit Insurance Corporation, Branch Banking and Trust Company Application for Consent to Merge with SunTrust Bank, Order and Basis for Corporation Approval (November 19, 2019)).

up under the SOP. I think the SOP should state explicitly that this would be viewed favorably, even if the target was not yet on the verge of failure.

Our analysis should also balance the various ways a merger can add to and subtract from risks to financial stability. Increasing the size and complexity of an institution may add to potential financial stability risks, while diversification (of business lines and geography) and more sophisticated technology (enabled by additional scale) may reduce potential financial stability risks. For example, in 2022, if a large bank with a stable, diverse deposit franchise and strong risk management and governance had acquired Silicon Valley Bank, with what proved to be an unstable deposit base and relatively unsophisticated risk management, this may have been quite positive for financial stability.

Convenience and Needs

The Bank Merger Act requires the FDIC to "take into consideration … the convenience and needs of the community to be served."[14] The SOP would go much further, imposing an affirmative burden on applicants to "demonstrate how the transaction will benefit the public," and stating that the FDIC "expects that a merger between IDIs will enable the resulting IDI to *better* meet the convenience and the needs of the community to be served than would occur absent the merger."[15] Burden-shifting can make a big difference for a legal regime; for example, there may be examples of mergers in which (1) the merger would benefit the convenience and needs of the community to be served but (2) the applicants are unable to prove that *ex ante* to the satisfaction of the FDIC.

The SOP also suggests the FDIC will closely scrutinize any planned branch closures. While I appreciate the impact the closure of a bank branch can have on a community with limited physical banking options, I think we should avoid presuming that more branch presence is always in the best interest of the community to be served, and we should be mindful of the tradeoffs between benefits such as more in-person service and higher costs that are passed on to customers. Additionally, I am skeptical that it is the FDIC's role to "closely evaluate[]" whom the resulting entity chooses to employ.[16]

Additional Objections

The SOP also notes that, consistent with longstanding practice, applicants may be offered the opportunity to withdraw an application rather than face a public denial. However, the SOP states that the FDIC may still publish a statement describing its concerns with the transaction, which would seem to defeat the purpose of allowing an institution to withdraw. I appreciate the

---

[14] 12 U.S.C. § 1828(c)(5).

[15] SOP, *supra* note 3, at 93 (emphasis in original).

[16] *See id.* at 95 ("Information regarding any proposed or expected closures, including … any job losses or lost job opportunities from branching changes … will be closely evaluated.").

desire to provide more transparency to the public regarding why certain mergers do not get approved, but believe any efforts to do so should avoid imposing reputational damage on applicants.

Finally, the SOP includes "issued and pending enforcement actions" as among the concerns likely to result in unfavorable findings.[17] I think this should be limited to enforcement actions that meet a certain materiality threshold and have some nexus to the statutory factors. For example, other agencies sometimes issue enforcement actions that linger for very long periods of time and may be irrelevant to the statutory factors.

Final Thoughts

Using merger policy to address consolidation in the banking industry reminds me of trying to use price and wage controls to address inflation.[18] In both cases, a combination of deeper economic forces and government policies[19] fuel demand, and imposing restrictions on consolidation or prices without addressing the underlying drivers results in a range of undesirable economic inefficiencies. Meanwhile, if/when restrictions are lifted in the future, a vigorous unleashing of pent up demand quickly undoes the perceived benefits of the prior policy.

We should work to develop a regulatory framework that allows banks of all sizes and various business models to flourish, is not biased in favor of one class of bank over others, and otherwise leaves it up to the market and the American people to determine how banking assets are allocated across the system.

---

[17] *Id*., at 84, 92.

[18] *See, e.g.,* Ben Bernanke, 21st Century Monetary Policy: The Federal Reserve from the Great Inflation to Covid-19, p. 8 ("The [wage and price] controls [that began in August, 1971] were initially popular. They were seen as a sign that the government was finally taking strong action on inflation. But they would ultimately be a costly failure.").

[19] We are currently considering revisions to make bank mergers more challenging at the same time that financial regulators have issued a series of significant rulemakings that create greater incentives for mergers.