December 8, 2022

James P. Sheesley, Assistant Executive Secretary,
Attention: Comments—RIN 3064–ZA31,
Federal Deposit Insurance Corporation,
550 17th Street NW
Washington, D.C. 20429

Re: Request for Comment on Rules, Regulations, Guidance, and Statements of Policy on Bank Merger Transactions (RIN 3064-ZA31)

To Whom It May Concern,

We appreciate the opportunity to submit these comments in response to the Federal Deposit Insurance Corporation's (FDIC) Request for information (RFI) and comment on rules, regulations, guidance, and statement of policy on bank merger transactions.[1]

We are Duke University economics and finance majors. Our coursework and independent research exposed us to the critical importance of maintaining financial stability and the consequences for all Americans when systemic risk in the financial system becomes manifest, as it did in 2008 at the onset of the Global Financial Crisis (GFC). Having been children during the GFC and studying economics and finance in university during the COVID-19 pandemic, we have come of age during times of uncertainty in the banking system. Because of these formative experiences and our own personal interest in bank merger policy, we have decided to submit these comments to help guide the FDIC and the Federal Reserve (Fed) in crafting equitable, sustainable and more fulsome banking merger guidelines.

Background and Position

"[Herfindahl-Hirschman Index] (HHI) is a blunt tool because it is measured at the geographic market level based on deposit activity rather than on a more granular basis, such as based on individual banking products."[2]

In his May 9, 2022, remarks at the Brookings Institution, Acting Comptroller for the Currency Michael Hsu expressed his frustration with much of the current framework for regulating banking mergers. In recent years, there has been growing criticism that the current bank merger

[1] Federal Deposit Insurance Corporation, "Request for Information and Comment on Rules, Regulations, Guidance, and Statements of Policy Regarding Bank Merger Transactions," Federal Register 87 (62) (2022): 18740-18744, https://www.fdic.gov/news/boardmatters/2021/2021-12-06-notational-fr.pdf.
[2] Hsu, Michael. "'Bank Mergers and Industry Resiliency.'" Remarks at Brookings. May 9, 2022. "Bank Mergers and Industry Resiliency." https://www.occ.gov/news-issuances/speeches/2022/pub-speech-2022-49.pdf

review process, overseen by the Fed and FDIC, has failed in protecting consumers and communities from the negative impacts of banking mergers.[3] These critiques pushed the FDIC to conduct a review process. In March 2022, the FDIC issued an RFI seeking information and comments on the effectiveness of current bank merger policies.[4]

The RFI's background section uses empirical evidence to demonstrate considerable consolidation in the banking sector over the last three decades.[5] On the one hand, scholars from the Bank Policy Institute argue against the need to materially change bank merger policies.[6] They contend that the RFI overstates consolidation by not controlling for economic growth and inflation. On the other hand, scholars such as Jeremy Kress insist on the need for more stringent policies that would decrease consolidation.[7] They believe that instead of reducing consumer prices, bank mergers often increase the price of certain financial products, reduce the availability of others, and create financial stability risks for the broader economy.

We have received valuable guidance from this existing literature and acknowledge the merits of these viewpoints. However, we take a different approach. The policies we propose in this letter do not unilaterally push for an increase or decrease in the number of bank mergers. Some of our policies could lead to more merger approvals whereas others could lead to fewer approvals. We are agnostic to the total number of bank mergers that are approved and simply want to ensure that potential flaws in current bank merger policies are effectively addressed. We seek to go beyond the current FDIC policy of primarily looking at the potential benefits of a proposed merger by emphasizing possible harms to consumers, communities, and financial stability.[8] If these harms cannot be sufficiently mitigated, the FDIC should consider denying the proposed merger.

Our recommendations are as follows:

- The Fed and FDIC should measure market concentration using a method that is more accurate than the HHI index in reflecting the competitive effects of nonbank financial institutions and banks serving a market remotely.

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[3] Tarullo, Daniel K. "Regulators Should Rethink the Way They Assess Bank Mergers." Brookings. Brookings, March 16, 2022. https://www.brookings.edu/opinions/regulators-should-rethink-the-way-they-assess-bank-mergers/.
[4] Request for Comment, supra note 1.
[5] Id.
[6] Aibangbee, Yany. "How Has the Size Distribution of Banks Evolved over the Last 30 Years?" Bank Policy Institute, November 22, 2022. https://bpi.com/how-has-the-size-distribution-of-banks-evolved-over-the-last-30-years/.
[7] Jeremy C. Kress, Modernizing Bank Merger Review, 37 YALE J. ON REGUL. 435, 439 n.17 (2020) https://openyls.law.yale.edu/bitstream/handle/20.500.13051/8305/Kress_Article._Publication__1_.pdf?sequence=2&isAllowed=y
[8] Federal Deposit Insurance Corporation, "Application Procedures Manual: Mergers," https://www.fdic.gov/regulations/applications/resources/apps-proc-manual/section04-mergers.pdf (last accessed Dec 2022).

- The Fed and the FDIC should not rely on the HHI's exclusive focus on deposit concentration when measuring the potential anticompetitive effect of a bank merger; instead, they should use a more robust index that individually assesses the change in market concentration of the main lines of products and services offered by the banks.
- The Fed and the FDIC must ensure that the balance of small and large banks in a banking market is not significantly altered by bank mergers to prevent a drastic reduction in small business lending.
- The Fed and the FDIC should use a more holistic approach instead of narrowly focusing on CRA ratings to understand how a bank merger might benefit or harm the surrounding communities.
- The Fed and the FDIC should develop a more analytical and comprehensive framework that specifies which quantitative metrics are used to measure changes in financial stability and clearly explains how the magnitude of those changes should be interpreted.

Analysis

Issue 1: Should the Fed Join the FDIC in Conducting a Review of Bank Merger Guidelines?

We strongly believe that the Fed should join the FDIC in conducting a review of current bank merger guidelines for two reasons.

First, the FDIC has been especially focused on reviewing bank merger guidelines over the past year; it has even released a request for public comment on the issue.[9] If the FDIC is intent on reviewing bank merger guidelines at this time, it would be logical for the Fed to follow suit. This is because both agencies are extremely important in the process of approving bank mergers. Under the Bank Merger Act, banks seeking to merge must receive approval from their primary regulator, which is either the Office of the Comptroller of the Currency (OCC), the FDIC, or the Fed.[10] Additionally, many bank mergers involve a bank holding company and hence, must separately seek approval from the Fed under the Bank Holding Company Act.[11] Consequently, it would be more efficient for the FDIC and the Fed to review and update bank merger guidelines simultaneously and synchronously. It would also provide more transparency about the review process to any banks that are considering a merger in the near future. If the Fed does not join the FDIC and only the latter were to update its bank merger guidelines, there could be confusion about which banks should consider applying for mergers and which mergers might have a chance of being permitted. It could also lead to a situation where the FDIC and the Fed reach a deadlock

[9] "FDIC Request for Information on Bank Merger Act." FDIC. Accessed November 15, 2022. https://www.fdic.gov/news/financial-institution-letters/2022/fil22011.html.
[10] "Bank Mergers and Acquisitions - Congress." Accessed November 15, 2022. https://crsreports.congress.gov/product/pdf/if/if11956.
[11] Tarullo, supra note 3.

on certain regulations, causing even greater confusion for banks that are seeking to merge and require approval from both agencies.

Second, certain macroeconomic factors are putting significant pressure on the Fed to review bank merger guidelines. On the one hand, President Biden has called for a 'whole-of-government' approach to promoting competition in the economy.[12] In the context of bank mergers, this can be interpreted as a rising need for the Fed and the FDIC to work together and determine whether bank merger guidelines are stringent enough. On the other hand, structural and technological changes are shifting the landscape of the banking sector.[13] Nonbank financial institutions are becoming increasingly popular and putting downward pressure on the prices of financial services and products, thereby nudging traditional banks towards mergers.[14] In this rapidly changing environment, the Fed needs to use its specialized knowledge in updating the decades-old bank merger guidelines.

Issue 2: Potential Policy Changes and Reviews

The Fed and FDIC should measure market concentration using a method that is more accurate than the HHI index in reflecting the competitive effects of nonbank financial institutions and banks serving a market remotely.

The process of improving bank merger guidelines begins with an understanding of the technological and structural trends shaping the banking industry. For example, banks are facing increasing competition from nonbank competitors such as fintechs and need the economies of scale provided by mergers to reduce prices for consumers.[15] While we firmly believe that reducing the price of financial products and services should not be the singular emphasis of bank merger guidelines, we still hold that it should be a prime consideration. Hence, existing bank merger guidelines must be updated in a manner that accounts for the aforementioned trends and facilitates the bank mergers necessary for reducing prices, so long as these mergers do not create significant negative consequences (the subsequent recommendations will focus on preventing potential negative consequences).

Under existing guidelines, the Fed and the FDIC use the HHI index to determine potential anticompetitive effects stemming from a bank merger.[16] However, the approximation of each competitor's market shares in the HHI index calculation is based upon the magnitude of deposits

[12] "Executive Order on Promoting Competition in the American Economy." The White House. The United States Government, July 9, 2021. https://www.whitehouse.gov/briefing-room/presidential-actions/2021/07/09/executive-order-on-promoting-competition-in-the-american-economy/.
[13] Tarullo, supra note 3.
[14] Id.
[15] Anton, Austin. "BankThink: To Serve Communities, Banks Need the Ability to Grow." Bank Policy Institute, June 16, 2022. https://bpi.com/bankthink-to-serve-communities-banks-need-the-ability-to-grow/.
[16] Id.

present in the bank branches physically located in that geographic market.[17] We believe that this approach is outdated in the present environment because the rise of the internet has made it possible for banks and nonbank financial institutions to compete in a geographic market without physically maintaining a bank branch in the area.[18]

To keep pace with the competitive realities of the banking industry, we propose that the Fed and the FDIC find a new method of analyzing the actual competition in a market when assessing the concentration in an existing market and the potential anticompetitive effects of a bank merger. This method should acknowledge the significance of competitors that serve a particular market but do not have physical branches located there. It should especially strive to include the relevant online and nonbank competitors. The proposed regulation will thus help facilitate mergers in markets where the concentration is much lower than what is reflected by the HHI index. This will likely help banks achieve more economies of scale, augment technology, and boost innovation.[19] It will also contribute to a decrease in the price of financial products and services and an increase in consumer welfare.[20]

Our recommendation may yield the opposite result in a few situations; the regulation could be used to allow a much greater number of mergers and certain banks might thereafter use the increased scale and market power to raise prices.[21] However, we strongly believe that this risk can be negated by applying the regulation in conjunction with the other regulations proposed in subsequent sections of this letter, many of which aim to curb the anticompetitive effects arising from bank mergers. Additionally, the banking sector's overall dynamics indicate that it will naturally remain competitive in the foreseeable future, even if banks continue to merge at the present rate.[22] This is because nonbank competitors such as fintechs – although not complete substitutes for traditional banks – are providing similar financial products and services.[23] Since nonbank financial institutions do not face the capital and liquidity requirements of traditional banks, they can often offer lower prices to customers, further increasing the overall competitiveness of the banking sector.[24]

The benefit of the proposed regulation is that it could somewhat level the playing field between traditional banks and rising nonbank financial institutions. By recognizing the true competition in a banking market, it could better facilitate mergers that are not actually anticompetitive. This might help several banks achieve the scale they need to reduce prices. These competitive prices

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[17] Id.
[18] Tarullo, supra note 5.
[19] Id.
[20] Anton, supra note 15.
[21] Charles Kahn, George Pennacchi & Ben Sopranzetti, Bank Consolidation and the Dynamics of Consumer Loan Interest Rates, 78 J. BUS. 99, 109 (2005), https://www.jstor.org/stable/10.1086/426521
[22] Tarullo, supra note 5.
[23] Id.
[24] Anton, supra note 15.

will likely incentivize more customers to deposit their money in regulated traditional banks rather than taking the risk of switching to unregulated nonbanks.[25] In the long term, this could prevent too much capital from draining out of the regulated financial system, thereby reducing customers' individual risk as well as systemic risk in the financial system.[26] One could argue that a similar outcome could be achieved by simply imposing stricter regulations on nonbanks instead of amending bank merger guidelines. We acknowledge that if certain nonbanks provide the same services as traditional banks, they pose the same risks to their customers and the financial system and should therefore be subject to the same regulation.[27] However, we do not expect nonbanks to subject to more stringent prudential standards in the near future. This can be surmised by observing the history of shadow banking, which also facilitates credit intermediation outside the banking system and yet remains largely unregulated.[28] It therefore seems more rational to amend bank merger guidelines instead of relying on potential nonbank regulations.

Those who believe that existing bank merger guidelines are not stringent enough and permit too many mergers might argue against the proposed regulation and instead advocate for regulations that restrict bank mergers.[29] As discussed in the subsequent sections, we believe that certain aspects of bank merger guidelines must be made more stringent and certain anticompetitive mergers must not be permitted. However, we also believe in taking a scientific approach, wherein different aspects of bank merger guidelines are tightened and relaxed as necessary and justified, instead of unilaterally moving towards more stringent guidelines.

The Fed and the FDIC should not rely on the HHI's exclusive focus on deposit concentration when measuring the potential anticompetitive effect of a bank merger; instead, they should use a more robust index that individually assesses the change in market concentration of the main lines of products and services offered by the banks.

While bank mergers can help reduce the price of financial products and services, they can occasionally bear the opposite result.[30] Scholars such as Kress argue that bank consolidation has not only "increased the fees that banks charge their customers" but "reduced the interest that banks pay to their depositors."[31] Empirical evidence also suggests that bank mergers frequently

[25] Mark Botti, Nicholas Hill, Sheridan Rogers & Mathis Wagner, Updating Retail Bank Merger Review for the Internet Age, 34 ANTITRUST 44, 46 (2020).
https://www.bateswhite.com/media/publication/185_Botti_Hill_Rogers_Wagner_2020_Updating_retail_bank_merger_review.pdf
[26] Id.
[27] Botti et. al, supra note 25.
[28] Barr, Jackson & Tahyar, Financial Regulation: Law and Policy, Second Edition
[29] Kress, Modernizing Bank Merger Review, supra note 7.
[30] Kahn et. al, supra note 21.
[31] Kress, Jeremy C. "Reviving Bank Antitrust." *SSRN Electronic Journal*, 2022.
https://doi.org/10.2139/ssrn.4039197.

increase the interest rates on specific products such as mortgages or personal loans, even when several other banks operate in the same geographic market.[32]

These observations imply that mergers sometimes equip banks with excessive market power, especially in certain lines of products or services where the merged bank holds a competitive advantage. It can therefore be deduced that the HHI index is not always an effective gauge for the anticompetitive effects of bank mergers. Hence, we propose that a more nuanced approach be employed when determining the anticompetitive effects of a bank merger, one that extends beyond the HHI's exclusive focus on deposit concentration. This metric should individually assess the market concentration of the main lines of products and services – such as personal loans, residential mortgages and digital payment services – that are offered by the banks seeking to merge. If such an analysis indicates that a certain merger will prove significantly anticompetitive for any of the main lines of financial products or services offered by the banks, the merger should not be permitted.

Since the proposed regulation requires the Fed and the FDIC to conduct more case-specific inquiries in comparison to the traditional HHI index approach, it would be expensive to implement. However, it would be a worthwhile effort since it would ensure that the effects of bank mergers are not spread unevenly across consumers of different products and services.
A potential alternative to our proposed regulation is simply lowering the 1800/200 HHI threshold that helps the Fed and the FDIC determine which bank mergers to place under scrutiny.[33] This might help prevent some anticompetitive mergers that could have led to price increases; however, it would still be problematic since it could create a competitive market for certain products and an anticompetitive one for others.

The Fed and the FDIC must ensure that the balance of small and large banks in a banking market is not significantly altered by bank mergers to prevent a drastic reduction in small business lending.

As explained in the previous section, it is possible for bank mergers to negatively affect consumers by granting banks excessive market power over certain financial products or services. One specific product that is frequently affected is small business lending.[34] Empirical studies suggest that small businesses pay higher interest rates, adhere to stricter collateral requirements, and receive smaller loans when a small bank serving a local market is acquired by a larger

[32] Id.
[33] Anton, supra note 15.
[34] Kress, Reviving Bank Antitrust, supra note 31.

bank.[35] We strongly believe it is necessary to individually address the issue surrounding small business lending with effective regulation for three reasons.

First, bank mergers not only affect the price of small business lending but frequently reduce its overall volume.[36] Since smaller businesses tend to have short credit histories, the community banks and other smaller banks that serve them rely on relationship-based lending and soft information.[37] Hence, smaller banks serve as a repository of specialized knowledge on the creditworthiness of local entrepreneurs, farmers, etc.[38] When these banks are acquired by larger banks, this repository often evaporates, thereby reducing the small business lending available to the local community.[39] Larger banks, especially those that did not have a presence in the local market prior to making an acquisition, do not usually adopt the same approach as these community banks.[40] They are likely to place lesser focus on soft information and relationships with local entrepreneurs. More often, they lend to larger businesses with lower or more easily measurable risk profiles.[41] An example that clearly demonstrates this contrast between small and large banks is the government's recent Paycheck Protection Program (PPP). This program was implemented by the Small Business Administration in 2020 and provided small businesses with loans to help pay employees during the pandemic.[42] Community banks clearly outperformed larger banks in their response to the program, issuing about 60% of the total PPP loans.[43] This example also highlights the importance of local relationships in small business lending – 75% of "relationship-borrowers" secured PPP loans in contrast to the 18% of "non-relationship firms".[44]

Second, by impacting the price of small business lending, bank mergers affect not just the consumers of this product – local entrepreneurs – but also the community surrounding them.[45]

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[35] Bernadette A. Minton, Alvaro G. Taboada & Rohan Williamson, Bank Mergers, Acquirer Choice and Small Business Lending: Implications for Community Investment 29 (Nat'l Bureau of Econ. Rsch., Working Paper No. 29284, 2021), https://www.nber.org/papers/ w29284 [https://perma.cc/2BD8-QUW6]
[36] Id.
[37] Paola Sapienza, The Effects of Banking Mergers on Loan Contracts, 68 J. FIN. 329, 364 (2002), https://doi.org/10.1111/1540-6261.00424
[38] Kress, Reviving Bank Antitrust, supra note 31.
[39] Id.
[40] Anton, supra note 15.
[41] Minton et. al, supra note 21.
[42] Li, Lei, and Philip E. Strahan. "Who Supplies PPP Loans (and Does It Matter)? Banks, Relationships, and the COVID Crisis." Journal of Financial and Quantitative Analysis 56, no. 7 (2021): 2411–38. doi:10.1017/S0022109021000405.
[43] Yosif, Noah. "PPP Data Show Community Banks Served Those Most in Need." ICBA. Accessed December 8, 2022. https://www.icba.org/newsroom/blogs/main-street-matters/2021/11/10/paycheck-protection-program-data-show-community-banks-served-those-most-in-need.
[44] Duchin, Ran and Martin, Xiumin and Michaely, Roni and Wang, Hanmeng, Concierge Treatment from Banks: Evidence from the Paycheck Protection Program (October 28, 2021). Journal of Corporate Finance, Forthcoming, https://ssrn.com/abstract=3775276
[45] Nicola Cetorelli, Does Bank Concentration Lead to Concentration in Industrial Sectors? 18 (Fed Reserve Bank of Chicago, Working Paper No. 2001-01, 2001), https://fraser.stlouisfed.org/files/docs/historical/frbchi/workingpapers/frbchi_workingpaper_2001-01.pdf [https://perma.cc/KX45-GVXU]

By potentially impairing credit access for small businesses, bank mergers can stifle their growth. This eventually transpires into negative effects for the local economy. For instance, the growth in jobs or the development of commercial real estate that could have occurred through the rise of a certain small business may no longer be achieved.[46]

Third, since small banks are involved in most bank mergers that occur, the potential reduction in small business lending arising from their acquisition could be magnified throughout the economy and must be mitigated.[47] The FDIC's own research emphasizes this, stating that 91% of bank mergers in recent years involved a community bank.[48] Furthermore, this trend has continued over time – small bank institutions have decreased from 18,000 in the 1980s to less than 5,000 today.[49]

To address this issue surrounding small business lending, we propose that the Fed and the FDIC keep the competitive environment of local banking markets intact by maintaining their 'size diversity'. They should strive to ensure that each banking market continues to have a span of small, medium, and large banks when possible; mergers that significantly disrupt this balance should not be permitted.

The benefit of this regulation is that it could boost the health of local economies. By potentially preventing drastic reductions in small business lending, this regulation will positively influence the employment, median income, development and overall prosperity of a community.[50]

A possible alternative to this regulation is reducing the hefty regulations on de novo banks and encouraging their entry into banking markets. We do not propose this for two reasons. First, the hefty regulations currently imposed on de novo banks are in place for good reason – they ensure that new entrants in the regulated banking system are equipped to safely handle financial deposits. Second, it is likely that reducing these hefty regulations will not sufficiently address the issue surrounding small business lending. While a de novo bank might become a great source of small business lending in the long term, it would require a considerable amount of time to build up soft information and local relationships.[51] If the established community banks in a local market are acquired and the de novo banks have not developed sufficient knowledge on the community members' creditworthiness, a short-term reduction in small business lending would

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[46] "Deposit Insurance Corporations (FDIC) Regulations, Guidance, and ..." Accessed November 15, 2022. https://www.fdic.gov/resources/regulations/federal-register-publications/2022/2022-rfi-rules-regulations-statements-of-policy-regarding-bank-merger-transactions-3064-za31-c-013.pdf.

[47] Bank Mergers and Acquisitions - Congress, supra note 10.

[48] Id.

[49] Chopra, Rohit. "Prepared Remarks of CFPB Director Rohit Chopra in Great Falls ..." Consumer Financial Protection Bureau. June 14, 2022. https://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-of-cfpb-director-rohit-chopra-in-great-falls-montana-on-relationship-banking-and-customer-service/.

[50] Kress, Reviving Bank Antitrust, supra note 31.

[51] Jeremy C. Kress, Solving Banking's "Too Big to Manage" Problem, 104 MINN. L. REV. 171, 212– 30 (2019)

emerge.[52] Such reductions would become a periodic phenomenon in these markets and negatively affect local economies.

The Fed and the FDIC should use a more holistic approach instead of narrowly focusing on CRA ratings to understand how a bank merger might benefit or harm the surrounding communities.

Bank mergers can have a significant impact on the communities the constituent banks operate in, much beyond the reduction in small business lending discussed above.[53] It is therefore necessary for the Fed and the FDIC to consider these impacts when evaluating bank merger applications. Accordingly, the Bank Merger Act states that "in every case, the responsible agency shall take into consideration…the convenience and needs of the community to be served."[54] The Fed and the FDIC currently determine whether a bank merger meets the convenience and needs of a community by checking if the banks seeking to merge have 'Satisfactory' CRA ratings.[55] We strongly believe that this approach is not granular enough to sufficiently ensure the welfare of local communities that could potentially be affected by a bank merger. An objective measure such as the CRA rating cannot accurately measure the plethora of subjective impacts that specific bank mergers have on their local communities.

Consequently, the convenience and needs of a community are often compromised by a bank merger. This is most evident in the form of certain individuals and communities experiencing reduced accessibility to the banking system.[56] When two banks merge, they tend to close multiple branches to reduce costs and increase efficiency, often creating banking deserts. [57]Notably, branch closures are clustered in areas comprising racial minorities and low-to-moderate-income (LMI) communities[58]. This often pushes Hispanic and African American consumers out of the banking system, forcing them to rely on predatory non-bank institutions that charge exorbitantly high fees.[59] According to data found by the National Community Reinvestment Coalition, "one third of the branches closed from 2017 to 2021 were in [LMI] and/or a majority-minority neighborhood."[60] While we do understand that branch closures can

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[52] Chopra, supra note 49.
[53] Kress, Reviving Bank Antitrust, supra note 31.
[54] FDIC, supra note 46.
[55] Id.
[56] Nicola Cetorelli & Philip E. Strahan, Finance as a Barrier to Entry: Bank Competition and Industry Structure in Local U.S. Markets, 61 J. FIN. 437, 437 (2006), https://www.nber.org/papers/w10832
[57] Kress, Reviving Bank Antitrust, supra note 31.
[58] Vitaly M. Bord, Bank Consolidation and Financial Inclusion: The Adverse Effects of Bank Mergers on Depositors 22–25, 30–32 (Dec. 1, 2018) (unpublished manuscript), https://scholar.harvard.edu/files/vbord/files/vbord_-_bank_consolidation_and_financial_inclusion_full.pdf [https://perma.cc/L3P5-A8MG]
[59] Id.
[60] Edlebi, Jad, Bruce Mitchell, and Jason Richardson. "The Great Consolidation of Banks and Acceleration of Branch …" February 2022. https://ncrc.org/the-great-consolidation-of-banks-and-acceleration-of-branch-closures-across-america/

sometimes occur due to a simple profit-loss consideration and the increasing popularity of online banking, we firmly believe that adequate steps must be taken to ensure that certain communities are not exceedingly disadvantaged by them.[61]

The process of addressing this issue begins with revising the FDIC's Statement of Policy, which requires that "in assessing the convenience and needs of the community to be served, the FDIC will consider such elements as the extent to which the proposed merger transaction is likely to benefit the general public."[62] This policy reflects that the FDIC is primarily considering the benefits of a bank merger when deciding whether to permit it. We believe it should be amended such that both the benefits and harms to the community are considered. We recommend that the Fed also adopt a similar standard. In the case that significant harms do arise from a bank merger and the banks involved are unable to propose a solution that truly mitigates these harms, the Fed and the FDIC should not permit the merger.

This acknowledgement not only augments the Fed and the FDIC's focus, but it also drives banks seeking to merge to actively mitigate potential harms to their community. We recommend that banks be required to disclose which of their branches will be closed after the merger. They should also be asked to provide quantifiable estimates that help gauge how their merger will impact the surrounding communities. For example, in the context of small business loans, banks should give an estimate of the expected increase in average interest rate and the expected reduction in loan volume. Banks should also be required to submit Community Benefit Plans (CBPs) alongside their merger applications. CBPs could elaborate on issues such as how the bank plans to incentivize disadvantaged communities to switch to its online banking platform and how it will smoothly facilitate that transition. The Fed and the FDIC could provide their own opinion and encourage members of the local community to give inputs on the feasibility of proposed CBPs. This would help banks further customize their CBPs for the specific communities they are serving. If the merger is permitted thereafter, CBPs should become legally binding to ensure that banks follow through and the negative effects of bank mergers on local communities are potentially mitigated. A prudent example of CBPs can be noticed in the recent acquisition of MUFG Union Bank by U.S. Bancorp.[63] The latter announced a $100 Billion CBP in the form of a "five-year plan focused on supporting equitable access to capital for low-to-moderate-income communities and communities of color."[64] The Fed and the FDIC should strive to make this the standard for all banks seeking to merge. This is not to say that they need to mandate a minimum dollar amount that banks must commit to their community; rather, they

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[61] Anton, Austin. "Do Bank Mergers Create 'Banking Deserts'? The Evidence Indicates No." Bank Policy Institute, September 20, 2022. https://bpi.com/do-bank-mergers-create-banking-deserts-the-evidence-indicates-no/.
[62] FDIC, supra note 46.
[63] "U.S. Bancorp Announces $100 Billion Community Benefits Plan." U.S. Bancorp, May 9, 2022. https://ir.usbank.com/news-releases/news-release-details/us-bancorp-announces-100-billion-community-benefits-plan.
[64] Id.

should encourage banks to create viable CBPs and then evaluate merger proposals based on whether these CBPs could sufficiently mitigate the potential negative effects of a bank merger on the local community.

We also believe that the Fed and the FDIC should take more substantial efforts to gauge the consumer perspective on proposed bank mergers. They should collect community input and feedback through local government meetings and surveys. They should also actively consult the Consumer Financial Protection Bureau (CFPB), which has authority to enforce federal consumer financial laws for banks with over $10B in assets.[65] The CFPB has both the data and the expert opinion to reach a conclusion on consumer compliance and its opinion should therefore influence the Fed and the FDIC's decision on a bank merger application.

The proposed regulations have several important benefits. The first benefit is that these regulations, especially the CBPs, could significantly reduce the negative consequences of a bank merger that are often disproportionately inflicted upon LMI and minority communities. Second, by requiring banks to disclose branch closures and CBPs before the merger, the Fed and the FDIC effectively establish the bank's intended community-related efforts in public view. This will ultimately put greater pressure on the banks to follow through on their commitments in the future and thereby avoid public scrutiny. Third, by placing a greater emphasis on gauging the consumer perspective on a merger, the Fed and the FDIC would be able to add a democratic element to the bank merger approval process.

The Fed and the FDIC should develop a more analytical and comprehensive framework that specifies which quantitative metrics are used to measure changes in financial stability and clearly explains how the magnitude of those changes should be interpreted.

The Dodd Frank Act added a very important factor to bank merger guidelines – the Fed and the FDIC must consider whether bank mergers pose a significant "risk to the financial stability of the United States banking or financial system."[66] The Fed generally performs financial stability analysis using the Global Systemically Important Bank (G-SIB) scores, which are most prominently published by the Basel Committee.[67] These scores reflect the amount of assets, substitutability, interconnectedness, complexity, and cross-jurisdictional activity.[68] The FDIC also performs its own financial stability analysis. Its Application Procedures Manual states that "Case Managers should consider both quantitative and qualitative metrics when evaluating a transaction's impact on financial stability" and gives "a non-exhaustive list of quantitative metrics for Case Managers to consider."[69]

[65] FDIC, supra note 46.
[66] 12 U.S.C. § 1828(c)(5) (2018)
[67] "G-SIB Scores," 2020. https://www.bis.org/bcbs/gsib/.
[68] Id.
[69] Federal Deposit Insurance Corporation, "Application Procedures Manual: Mergers," p. 22,

However, as former Fed Governor Daniel Tarullo explains, the Fed and the FDIC's current efforts do not constitute a "reasonably well-developed and well-explained approach to financial stability analysis in bank mergers."[70] This can be noticed, for instance, in the Fed order approving Morgan Stanley's acquisition of E-Trade.[71] While the Fed order did state that the acquisition would lead to a 2% increase in Morgan Stanley's G-SIB score, it did not explain why this increase was acceptable or how much of an increase would have raised material concerns.[72]

We therefore propose that the Fed and the FDIC develop a more analytical framework to assess whether bank mergers pose a risk to financial stability. This framework should state which quantitative metrics are used to measure changes in financial stability and then clearly explain how the magnitude of different changes in those metrics should be interpreted. It must be noted that our proposal does not promote certain quantitative metrics over others. There are several different metrics that measure financial stability risks, such as the G-SIB score, expected systemic cost of failure (SCF)[73] and conditional value at risk (CVaR).[74] We believe that the Fed and the FDIC should use the set of metrics they deem fit, so long as it is comprehensive. This means that the set of metrics should not be designed to exclusively measure financial stability risks arising from bank mergers involving G-SIBs. It should also account for bank mergers involving other important banks, which might not be G-SIBs but still pose financial stability risks.[75] This is especially important given the rapid growth of national and super-regional banks in recent years. The 2019 merger between BB&T and SunTrust, forming Truist, is just one example of the increasingly important role that super-regional banks play in the American banking system.[76] As of Q2 2022, super-regional banks like US Bancorp, PNC Financial Services, and Truist were all top 10 in the US in total assets, above G-SIBs like Goldman

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https://www.fdic.gov/regulations/applications/resources/apps-proc-manual/section04-mergers.pdf (last accessed Dec 2022).

[70] Tarullo, supra note 3.

[71] Linnane, Ciara. "Morgan Stanley's $13 Billion E-Trade Deal Raises Questions about 'Too Big to Fail'." MarketWatch. MarketWatch, February 22, 2020. https://www.marketwatch.com/story/morgan-stanleys-13-billion-e-trade-deal-raises-questions-about-too-big-to-fail-2020-02-20.

[72] Tarullo, supra note 3.

[73] Aibangbee, Yany. "How to Measure the Change in Financial Stability Risk Resulting from a Merger: Some Technical Considerations." Bank Policy Institute, June 1, 2022. https://bpi.com/how-to-measure-the-change-in-financial-stability-risk-resulting-from-a-merger-some-technical-considerations/.

[74] Uryasev, S., Rockafellar, R.T. (2001). Conditional Value-at-Risk: Optimization Approach. In: Uryasev, S., Pardalos, P.M. (eds) Stochastic Optimization: Algorithms and Applications. Applied Optimization, vol 54. Springer, Boston, MA. https://doi.org/10.1007/978-1-4757-6594-6_17

[75] Gregor N.F. Weiss et al., Systemic Risk and Bank Consolidation: International Evidence, 40 J. BANKING & FIN. 165, 174-77 (2014)

[76] Board of Governors of the Federal Reserve System, "Federal Reserve Board announces approval of application by BB&T Corporation to merge with SunTrust Banks," Press release, Nov. 19, 2019, available at https://www.federalreserve.gov/newsevents/pressreleases/orders20191119a.htm

Sachs.[77] Hence, the proposed framework and its quantitative metrics must account for super-regional banks and other such important banks.

Over time, the use of the proposed framework could help set clear precedents in the bank merger review process, potentially bringing more consistency to the Fed and the FDIC's financial stability analyses. This might help the Fed and the FDIC become even more efficient in preventing mergers that could create 'too big to fail' banks. The proposed framework could also establish greater transparency in the review process. Consequently, banks might better assess whether they should apply for a merger and the public might feel more informed about how certain bank mergers affect financial stability.

Conclusion

In conclusion, we believe that the Fed and FDIC should implement a more accurate market concentration metric than the HHI, ensure a balance between large and small banks, and apply more scrutiny to how bank mergers will affect communities and small business lending. They should also develop a framework that better considers the effects of bank mergers on financial stability. We posit that our proposals will equip the banking system to better serve the American people and be more resilient to potential financial crises.

We thank you again for the opportunity to comment on this topic. Please let us know if we can answer any additional questions.

Sincerely,

Suyash Chandak
Niroop Vallabhaneni
Ben Smith

[77] Goldberg, Matthew. "These Are the 15 Largest Banks in the U.S." Bankrate. Accessed November 15, 2022. https://www.bankrate.com/banking/biggest-banks-in-america/.