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May 31, 2022

By electronic submission to Comments@fdic.gov

The Honorable Martin J. Gruenberg
Acting Chairman
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)

Dear Acting Chairman Gruenberg:

Thank you for the opportunity to comment on the regulatory framework for bank merger transactions. By way of background, I am an assistant professor of business law at the University of Michigan's Stephen M. Ross School of Business and Co-Faculty Director of the University of Michigan's Center on Finance, Law & Policy. Before entering academia, I was an attorney at the Federal Reserve Board of Governors, where I advised the Board on the legal permissibility of bank mergers and acquisitions.

For too long, regulators have treated bank merger oversight as a "check-the-box" exercise. As my research has shown, the federal banking agencies have not denied a merger application in almost 20 years.[1] The banking sector insists that mergers "are almost always approved because banks know what the approval standards are and generally do not apply if a potential merger does not meet them."[2] This view reveals a harmful bias in bank merger regulation: the assumption that a merger will be approved if it satisfies certain minimum standards relating to Herfindahl-Hirschman Index (HHI) thresholds, Community Reinvestment Act (CRA) scores, and confidential management ratings. In essence, the regulatory framework creates an implicit presumption of approval: when a proposed merger complies with the agencies' guidelines, the agencies' analysis typically stops there and the merger is approved.

This permissive approach to bank consolidation is not what Congress intended. The Bank Merger Act instructs the banking agencies to carefully evaluate a proposed merger's effect on the convenience and needs of the community to be served, financial stability, and competition, among

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[1] *See* Jeremy C. Kress, *Modernizing Bank Merger Review*, 37 YALE J. ON REGUL. 435, 439 n.17 (2020) (documenting that the banking agencies last denied a merger application in 2003).

[2] Greg Baer, *It's a Myth That Regulators Rubber-Stamp Bank M&A*, AM. BANKER (Aug. 23, 2021), https://www.americanbanker.com/opinion/its-a-myth-that-regulators-rubber-stamp-bank-m-a.

other factors.[3] As the United States Supreme Court held in 1968, a bank merger "should be judged in terms of its overall effect upon the public interest."[4] The Court characterized the public interest as "the ultimate test imposed."[5] Thus, the bank merger review process is not supposed to be a "check-the-box" exercise; rather, the agencies are required to closely scrutinize the advantages and drawbacks of each proposed merger and authorize only those transactions that advance the public interest.

Regrettably, the agencies' lax oversight of bank mergers has harmed society in numerous ways. My research has documented how lenient bank merger regulation has hurt consumers, small businesses, and the broader financial system. For example, under the banking agencies' prevailing approach, bank mergers have made it harder and more expensive for consumers to obtain credit, increased the fees that banks charge their customers, and reduced the interest rates that banks pay to their depositors.[6] Bank consolidation has likewise impaired local economic development: bank mergers have been associated with lower small business lending, less small business formation, higher unemployment, and wider income inequality.[7] These negative outcomes have proven to be especially acute for consumers in low- and moderate-income (LMI) and minority communities.[8] Meanwhile, the agencies' deferential approach to bank mergers has produced numerous "too big to manage" conglomerates that intensify risks to financial stability.[9]

In this letter, I outline how the FDIC and other banking agencies should strengthen merger oversight. Specifically, I urge the agencies to bolster the regulatory framework for bank merger transactions as follows:

- **Convenience and Needs of the Community:** The agencies should begin reviewing a merger proposal with a presumption that the combination will not produce benefits to the public, consider merger-related branch closures, require that a bank merger applicant have an "outstanding" CRA record, and empower the Consumer Financial Protection Bureau (CFPB) to block a bank merger on public interest grounds.

- **Financial Stability:** The agencies should establish quantitative systemic risk limits for bank mergers using the Basel Committee's G-SIB score or similar systemic risk metric.

- **Competition:** The agencies should reduce the HHI threshold that triggers enhanced scrutiny of bank mergers to 1500/Δ100, deemphasize mitigating factors, evaluate the mix

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[3] 12 U.S.C. § 1828(c)(5).

[4] United States v. Third Nat'l Bank in Nashville, 390 U.S. 171, 185 (1968).

[5] *Id.*

[6] *Modernizing Bank Merger Review*, *supra* note 1, at 459; Jeremy C. Kress, *Reviving Bank Antitrust*, 72 DUKE L.J. (forthcoming 2022), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4039197 (manuscript at 32-34).

[7] *Modernizing Bank Merger Review*, *supra* note 1, at 460; *Reviving Bank Antitrust*, *supra* note 6, at 35-37.

[8] *Modernizing Bank Merger Review*, *supra* note 1, at 459-60; *Reviving Bank Antitrust*, *supra* note 6, at 34-35, 37.

[9] *Modernizing Bank Merger Review*, *supra* note 1, at 461-62; *Reviving Bank Antitrust*, *supra* note 6, at 45-46.

of large and small banks that would remain in a market following a merger, and consider how the "too-big-to-fail" subsidy could distort competition.

To be clear, bank mergers are not inherently objectionable. Indeed, some mergers—particularly among very small community banks—may be beneficial.[10] However, inappropriately lax bank merger oversight creates real risks to consumers, small businesses, and the broader financial system. That is why the banking agencies must fulfill their statutory obligation to closely scrutinize bank merger proposals and prevent consolidations that could harm the public. If enacted, the reforms proposed herein would help ensure that the agencies protect society from the harmful effects of excessive bank consolidation.

1. Convenience and Needs of the Community

Under the Bank Merger Act, the public interest—or the "convenience and needs of the community to be served"—is of paramount importance. Despite this mandate, however, the agencies have not prioritized the public interest in bank merger reviews. To the contrary, the agencies' public interest analyses are typically perfunctory and often focus on advantages to the merging banks—such as projected cost savings—rather than to their consumers.[11] To reinvigorate public interest considerations in bank merger oversight, the agencies should establish a rebuttable presumption that a merger proposal will not produce benefits to the public, consider merger-related branch closures, require that applicants have outstanding CRA records in order to warrant bank merger approval, and empower the CFPB to block a bank merger on consumer compliance grounds.

A. Establish a Rebuttable Presumption That a Merger Proposal Will Not Benefit the Public

As my research has shown, the "convenience and needs of the community" has virtually evaporated as an independent factor in bank merger applications over the past several decades.[12] Today, the agencies barely mention convenience and needs in their merger decisions. When the agencies do refer to convenience and needs, they merely repeat the applicant's "representations" about benefits that will accrue from the merger.[13] The agencies, however, analyze neither the significance of these purported benefits nor the likelihood that they will materialize.[14]

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[10] *See* John H. Boyd & Stanley L. Graham, *Consolidation in U.S. Banking: Implications for Efficiency and Risk*, *in* BANK MERGERS AND ACQUISITIONS 113, 125-33 (Yakov Amihud & Geoffrey Miller eds., 1998) (documenting that mergers resulting in banks with less than $400 million in assets produced efficiency gains); Adel A. Al-Sharkas et al., *The Impact of Mergers and Acquisitions of the US Banking Industry: Further Evidence*, 35 J. BUS. FIN. & ACCT. 50, 62-64 (2008) (documenting that mergers involving small banks result in larger cost efficiency improvements compared to mergers involving larger banks).

[11] *Modernizing Bank Merger Review*, *supra* note 1, at 479.

[12] *See id.* at 476-83.

[13] *See, e.g.*, Fifth Third Bancorp, 105 Fed. Res. Bull. 70, 81-82 (2019) (noting that Fifth Third represented that the proposed merger would expand consumers' access to its retail and commercial banking services); Synovus Bank, 103 Fed. Res. Bull. 67, 77 (2017) (noting that Synovus Bank represented that the proposed merger would increase its deposit base and thereby allow it to provide more loans).

[14] *See* Mehrsa Baradaran, *Banking and the Social Contract*, 89 NOTRE DAME L. REV. 1284, 1338 (2014). ("Despite the public benefit test's salience, in practice no searching inquiry into the actual needs of the public is undertaken.").

To fulfill their statutory mandates, the banking agencies should establish a new paradigm for analyzing the "convenience and needs" standard in bank merger applications. In an optimal framework, the agencies would: (1) begin with a presumption that a proposed merger would *not* benefit the public; (2) insist that the applicant identify concrete, verifiable ways in which the transaction would create better banking services for the community; and (3) quantify these public benefits where possible. Collectively, these reforms would ensure that the agencies satisfy their statutory obligation to assess whether a merger proposal is in the public interest.

First, the agencies should apply a presumption that bank mergers generally do not enhance the public welfare. The agencies, in essence, should flip their current presumption. Whereas recent bank merger approvals have implicitly assumed that consolidation benefits the public, going forward, the agencies should expressly acknowledge the empirical evidence that bank mergers tend to result in detriments to the public. As I have documented in my research, these detriments include increased loan costs, lower deposit rates, less small business lending, and worse customer service.[15] The agencies' presumption against public benefits should be particularly strong for mergers among the United States' largest banks, wherein concerns about market power and systemic risks are most acute and benefits of scale are doubtful, at best.[16]

Second, in order to overcome this presumption, the agencies should require bank merger applicants to identify concrete, verifiable ways in which a proposed transaction will help the community. Mergers could enhance the convenience and needs of the community in a variety of ways. For example, an acquisition might save a troubled bank from potential failure, or it might replace a target's ineffective management. Moreover, there may be some situations in which an acquiring bank offers critical products or services, such as small business loans, that otherwise would be unavailable to the target bank's customers. Rather than merely restating an applicant's "representations" about public benefits, however, the agencies must carefully evaluate the likelihood that the purported benefits will, in fact, occur.[17] The purported benefits should be definite and not "speculative"—a standard to which the agencies previously adhered but have since relaxed considerably.[18]

Finally, the agencies should attempt to quantify the value of public benefits arising from a merger in order to more accurately weigh policy trade-offs inherent in bank consolidation. In the past, the

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[15] *Modernizing Bank Merger Review*, *supra* note 1, at 459-63; *Reviving Bank Antitrust*, *supra* note 6, at 32-37, 41-42.

[16] Professor Jesse Markham has noted the paradox that the agencies consider potential economies of scale in bank merger proposals, but they do not take into account possible diseconomies of scale. *See* Jesse W. Markham, Jr., *Lessons for Competition Law from the Economic Crisis: The Prospect for Antitrust Responses to the "Too Big to Fail" Phenomenon*, 16 FORDHAM J. CORP. & FIN. L. 261, 302 (2011) ("While efficiencies of scale are considered in approving transactions, inefficiencies of scale are not, such that mergers resulting in inefficiently large scale are not disapproved on that particular ground.").

[17] As one federal district court stated, the agency "should specify particularly what [it] finds to be the convenience and needs of the community" and "what [it] considers will be the effect of the merger thereon . . . ." United States v. Crocker-Anglo Nat'l Bank, 263 F. Supp. 125, 138 (N.D. Cal. 1966).

18. *See* N. Star Fin., Inc., 86 Fed. Res. Bull. 609, 610 (2000) (denying proposed acquisition because purported financial and managerial improvements were "speculative").

agencies have not been transparent about how they balance the societal costs of reduced competition and greater systemic risk against purported enhancements to convenience and needs, suggesting a lack of analytical rigor in their review process. Attempting to quantify the value of purported public benefits would help alleviate this concern.

B. Consider Merger-Related Branch Closures

Access to local branches is a critical aspect of the "convenience and needs of the community to be served." Consumers benefit from the convenience of in-person service and familiarity with their bankers.[19] Indeed, the overwhelming majority of consumers still use brick-and-mortar branches despite the proliferation of online banking.[20] As Federal Reserve researchers concluded in 2018, "[B]oth depositors and small businesses continue to value local bank branches."[21] Merger-related branch closures, therefore, hurt customers. To date, however, the agencies have overlooked this aspect of the convenience and needs of the communities affected by bank mergers.

Bank consolidation has triggered merger-related branch closures throughout the country. As merging banks consolidate operations and cut overhead costs, they typically shutter branches in neighboring locations.[22] In fact, Professor Hoai-Luu Nguyen found a twenty-seven percent increase in the likelihood of a branch closure when merging banks operate in the same census tract.[23] In one notable example, BB&T and SunTrust Bank announced plans to close 800 of their 2,887 branches, or nearly twenty-eight percent of their offices, when the banks merged in 2019.[24] Troublingly, branch closures following bank mergers are typically concentrated in LMI areas, further disadvantaging vulnerable populations.[25]

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[19] For many consumers, convenience is so critical that they choose to bank with institutions with nearby branches, even if those institutions offer less favorable product terms. *See* Mary Wisniewski, *Survey: While Checking Fees Vary Wildly By Race and Age, Americans Stay Loyal to Their Banks*, BANKRATE (Jan. 15, 2020), https://www.bankrate.com/banking/best-banks-consumer-survey-2020/.

[20] *See* BD. OF GOVERNORS OF THE FED. RSRV. SYS., CONSUMERS AND MOBILE FINANCIAL SERVICES 2016, at 9 (2016) (noting that 84 percent of survey respondents use bank branches), https://www.federalreserve.gov/econresdata/consumers-and-mobile-financial-services-report-201603.pdf.

[21] Elliot Anenberg et al., *The Branch Puzzle: Why Are There Still Bank Branches?*, FEDS NOTES (Aug. 20, 2018), https://www.federalreserve.gov/econres/notes/feds-notes/why-are-there-still-bank-branches-20180820.htm.

[22] *See* Lydia DePillis, *The Internet Didn't Kill Bank Branches. Bank Mergers Did.*, WASH. POST (July 9, 2013), https://www.washingtonpost.com/news/wonk/wp/2013/07/09/the-internet-didnt-kill-bank-branches-bank-mergers-did.

[23] Hoai-Luu Q. Nguyen, *Are Credit Markets Still Local? Evidence from Bank Branch Closings*, 11 AM. ECON. J.: APPLIED ECON. 1, 15-17 (2019) (analyzing mergers between 1999 and 2012); *see also* Yong Kyu Gam & Yunqi Zhang, Dismembered Giants: Bank Divestitures and Local Lending 19-20, 51 (Nov. 2019) (unpublished manuscript), https://www.aeaweb.org/conference/2020/preliminary/paper/EitrD7zf (evaluating bank mergers between 1999 and 2014 and concluding that merging banks closed significantly more branches than competing banks).

[24] Lauren Seay & Ali Shayan Sikander, *Majority of BB&T, SunTrust Branch Closures Still to Come*, S&P GLOBAL MKT. INTEL. (Oct. 5, 2020), https://www.spglobal.com/marketintelligence/en/news-insights/latest-news- headlines/majority-of-bb-t-suntrust-branch-closures-still-to-come-60511261. Of the closed branches, more than half did not have an active BB&T or SunTrust branch within two miles. *See id.*

[25] *See* GARY A. DYMSKI, THE BANK MERGER WAVE: THE SOCIAL AND ECONOMIC CONSEQUENCES OF FINANCIAL CONSOLIDATION 95 (1999).

Under the current bank merger framework, however, the agencies have failed to consider reductions in branch access as part of their evaluations. Merging banks typically do not disclose planned branch closures during the application process.[26] In response to public commenters' concerns over potential merger-related branch closures, the Federal Reserve frequently asserts that "federal banking law provides a specific mechanism for addressing branch closings."[27] That mechanism, however, simply requires a bank to provide ninety days' notice prior to an upcoming closure.[28] The law expressly prohibits the relevant agency from blocking a proposed branch closure by an interstate bank.[29] By failing to address local branch access as part of the bank merger review framework, therefore, the banking agencies effectively allow a crucial aspect of the "convenience and needs of the community" to escape regulatory review.

To evaluate potential deterioration in branch access, the banking agencies should require merging banks to disclose planned branch closures during the application process instead of waiting until after consummation of the merger.[30] Once disclosed, the relevant agency should assess the extent to which an applicant's proposed branch closures would inconvenience consumers and deprive communities of financial services, with heightened scrutiny of planned branch closures in LMI areas. Meaningful impairments in branch access should weigh heavily against approval of a proposed merger.

C. Require Merger Applicants to Have "Outstanding" CRA Ratings

In addition to considering costs and benefits of a bank merger proposal, the banking agencies must assess merging banks' past performance under the CRA.[31] The CRA imposes an "affirmative obligation" on banks to "help meet the credit needs of [their] communities," with a special emphasis on LMI neighborhoods. The banking agencies periodically examine banks to assess their performance under the CRA,[32] and the main consequence of a poor CRA rating is a potential restriction on the bank's ability to merge.[33] In practice, the agencies have undermined the CRA's objectives by permitting banks with marginal CRA records to merge. The banking agencies should apply more rigorous CRA performance standards in bank merger applications to ensure that only firms genuinely committed to serving LMI communities are permitted to expand.

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[26] *See, e.g.*, Letter from Patricia A. Robinson, Of Counsel, Wachtell, Lipton, Rosen & Katz, to Adam M. Drimer, Assistant Vice President, Fed. Rsrv. Bank of Richmond A-2–A-5 (Apr. 16, 2019), https://www.federalreserve.gov/files/Additional-Information-Response-20190416.pdf (declining to disclose BB&T's and SunTrust's anticipated post-merger branch closures).

[27] *See, e.g.*, BB&T Corp., 106 Fed. Rsrv. Bull. 1, 28 (2020).

[28] *See* 12 U.S.C. § 1831r-1.

[29] *See id.* at § 1831r-1(d)(3).

[30] The relevant agency should prohibit a merging bank from closing any branches not identified as part of the application process for a certain period of time—for example, five years following the merger.

[31] 12 U.S.C. § 2901(a)(3).

[32] *Id.*

[33] *See,* Jonathan R. Macey & Geoffrey P. Miller, *The Community Reinvestment Act: An Economic Analysis*, 79 VA. L. REV. 291, 300 (1993).

The agencies have established lenient standards for merger applicants' CRA performance, to the detriment of LMI communities. The agencies have codified a policy of presumptively approving proposals by firms with at least Satisfactory CRA ratings, as long as other statutory factors are consistent with approval.[34] Banks have responded by "satisficing," or doing the bare minimum to achieve a Satisfactory CRA rating, and no more.[35] As Professor Kenneth Thomas has observed, "there are few if any real incentives for banks to go for CRA gold," so firms "tend to be happy with the middle ground."[36] As a result, more than 90% of banks are currently rated Satisfactory, and few even try for an Outstanding rating.[37] Meanwhile, many LMI areas continue to lack access to traditional banking services.[38]

To address this problem, the agencies should strengthen their standards for the CRA factor in bank merger applications. Specifically, the agencies should insist that an acquirer have received an Outstanding overall rating on two out of its most recent three CRA exams to obtain regulatory approval for a merger. Elevating the CRA threshold from Satisfactory to Outstanding would ensure that the acquirer is permitted to expand only if it is genuinely committed to serving LMI neighborhoods. Moreover, considering the bank's three most CRA exams—instead of only its most recent evaluation, as is current practice[39]—would assess the bank's long-term commitment to LMI areas and counteract the well-known phenomenon whereby a bank strategically increases its lending to LMI populations only when it anticipates filing a merger application.[40]

Although the agencies' recent proposal to modernize their CRA regulations may mitigate "grade inflation" on CRA evaluations, the proposal does not go far enough to encourage banks to strive for an Outstanding rating.[41] Even if the agencies were to establish more stringent standards to achieve a Satisfactory CRA rating, banks will still have little incentive to truly excel in meeting

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[34] *See* BD. OF GOVERNORS OF THE FED. RESERVE SYS., SR 14-2, ENHANCING TRANSPARENCY IN THE FEDERAL RESERVE'S APPLICATIONS PROCESS 3 (2014); FED. DEPOSIT INS. CORP., APPLICATIONS PROCEDURES MANUAL § 1.10 (2019); OFFICE OF THE COMPTROLLER OF THE CURRENCY, PPM 6300-2, POLICIES AND PROCEDURES MANUAL: IMPACT OF CRA RATINGS ON LICENSING APPLICATIONS 1-2 (2017). The agencies have even suggested that a less-than-satisfactory CRA rating may not be a barrier to a merger approval. In 2018, agency officials indicated that they are open to approving merger applications by banks with Needs to Improve or Substantial Noncompliance ratings if the firms demonstrate progress since their last CRA evaluations. *See* Joe Mantone, *Banks Could Get out of M&A Penalty Box Sooner, Regulator Says*, S&P GLOBAL MKT. INTELLIGENCE (Dec. 3, 2018), https://www.spglobal.com/marketintelligence/en/news-insights/trending/0xccl6qtxfgklta1awkpmg2.

[35] Kenneth H. Thomas, *Banks Learn the Price of 'Satisfactory' CRA Grades*, AM. BANKER (Sept. 8, 2016), https://www.americanbanker.com/opinion/banks-learn-the-price-of-satisfactory-cra-grades.

[36] *Id*.

[37] *See id*.

[38] *See, e.g.*, MEHRSA BARADARAN, HOW THE OTHER HALF BANKS 102-37 (2015) (discussing challenges faced by LMI borrowers).

[39] *See, e.g.*, Compass Bank, 102 Fed. Res. Bull. 58, 61 n.18 (2016).

[40] *See* Raphael Bostic et al., *Regulatory Incentives and Consolidation: The Case of Commercial Bank Mergers and the Community Reinvestment Act*, ADVANCES ECON. ANALYSIS & POL'Y, 2005, at 1, 8-11.

[41] *See* Press Release, Fed. Deposit Ins. Corp., Agencies Issue Joint Proposal to Strengthen and Modernize Community Reinvestment Act Regulations (May 5, 2022), https://www.fdic.gov/news/press-releases/2022/pr22039.html.

the credit needs of LMI communities as long as the agencies presumptively approve mergers by banks with Satisfactory ratings. Accordingly, rather than rewarding minimally compliant banks with merger approvals, the agencies should insist that merger applicants demonstrate exceptional records of serving LMI populations under the CRA.

D. Empower the CFPB to Block a Large Bank Merger on Consumer Compliance Grounds

As part of the convenience and needs analysis, the agencies consider the merging banks' records of compliance with fair lending and other consumer protection laws. The agencies have traditionally taken into account the merging banks' compliance records to assess whether the combined institution would have the capacity to implement effective consumer protection systems. Over time, however, the agencies have neglected consumer compliance evaluations in bank merger applications. In order to restore consumer compliance as a central consideration in bank merger oversight, the agencies should empower the CFPB to block a large bank merger proposal if the Bureau determines that the resulting institution would have inadequate consumer compliance systems to protect the public in light of the firm's expanded footprint.

In the wake of the 2008 subprime mortgage crisis, many observers blamed the banking agencies' lax consumer protection policies for the collapse.[42] In response, Congress created the CFPB and gave the CFPB exclusive jurisdiction to supervise banks with more than $10 billion in assets and their affiliates for compliance with most consumer financial protection laws.[43] Thus, the federal banking agencies now play only a minor role in consumer financial protection, especially with respect to the largest banks.

Even though the CFPB now has exclusive supervisory authority over consumer compliance by large banks, it has no independent voice in bank merger applications. Instead, the banking agencies—which lack direct oversight of big banks' consumer compliance—continue to assess bank merger applicants' consumer compliance records. To be sure, the banking agencies consult with the CFPB about bank merger applications on an informal, confidential basis.[44] And the CFPB may share consumer compliance examination reports with the banking agencies.[45] But under current policies, the agencies are not required to accept the CFPB's recommendations on a merger application, and the CFPB lacks a formal mechanism to stop a merger it believes will harm consumers.[46]

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[42] *See, e.g.*, KATHLEEN C. ENGEL & PATRICIA A. MCCOY, THE SUBPRIME VIRUS: RECKLESS CREDIT, REGULATORY FAILURE, AND NEXT STEPS 167-205 (2011).

[43] 12 U.S.C. § 5515(a) (2018); *see also id.* §§ 5481(12), (13) (enumerating relevant consumer financial protection laws).

[44] *Cf.* Fifth Third Bancorp, 105 Fed. Res. Bull. 70, 81 (2019) (noting that the Federal Reserve consulted with the CFPB about Fifth Third's consumer compliance record).

[45] 12 U.S.C. § 5512(c)(6)(C)(i) (2018).

[46] It is insufficient that the Director of the CFPB sits on the FDIC's Board of Directors. Almost all of the largest U.S. banks are chartered as national banks and overseen by the OCC, not the FDIC. As a result, the FDIC, and by extension the CFPB Director, is excluded from merger applications involving the biggest banks—the precise deals on which the CFPB is likely to have supervisory insight. Moreover, even in the rare cases when the FDIC has jurisdiction over a big-bank merger, the FDIC's four other board members—whose primary focus is bank safety and soundness, not

The CFPB's exclusion from the bank merger application process is problematic. The banking agencies have a well-documented history of downplaying banks' consumer compliance problems—indeed, that is why Congress created the CFPB in the first place.[47] Vesting the federal banking agencies with final authority to assess consumer compliance in merger applications therefore increases the risk that banks with deficient compliance systems will be permitted to expand. Furthermore, knowing that the banking agencies deemphasize consumer compliance, prospective merger applicants will have insufficient incentives to maintain strong compliance systems. Excluding the CFPB from bank merger review minimizes the importance of consumer compliance and thereby imperils the public welfare.[48]

For these reasons, the agencies should establish an official role for the CFPB in the bank merger application process. Specifically, the agencies should establish by regulation a process whereby they formally notify and request feedback from the CFPB whenever a bank with more than $10 billion in assets submits a Bank Merger Act application. The agencies should further codify in a regulation that they will not approve any such application without a favorable recommendation by the CFPB Director. Such a recommendation would verify that, based on the Bureau's unique supervisory experience, the combined institution would have sufficiently strong compliance systems to protect consumers.

The CFPB's formal participation in the bank merger process is essential because the banking agencies lack critical information necessary to assess a firm's compliance systems. The supervisors that conduct day-to-day oversight of consumer compliance systems at the largest banks are housed within the CFPB. Although the CFPB may share its examination reports with the banking agencies, the banking agencies may lack the institutional knowledge, context, and experience to interpret these findings. Accordingly, it makes little sense for the banking agencies, which have been stripped of their consumer-focused supervisory authority, to evaluate merger applicants' consumer compliance records while the CFPB is relegated to an informal advisory role. The agencies should therefore formalize the CFPB's participation in bank merger oversight and establish by regulation

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consumer protection—can outvote the CFPB Director. This divergence between bank safety-and-soundness and consumer protection as regulatory objectives is the exact reason why the CFPB was created in the first place. The CFPB Director's representation on the FDIC's Board of Directors is far from sufficient to ensure that consumer compliance is a central consideration in bank merger oversight.

[47] *See, e.g.*, Adam J. Levitin, *The Consumer Financial Protection Bureau: An Introduction*, 32 REV. BANKING & FIN. L. 321, 329-34 (2013).

[48] Mere consultation between the banking agencies and the CFPB as part of the application process is insufficient for two reasons. First, informal consultation provides no mechanism for resolving conflicts when the banking agencies and the CFPB disagree about the merits of a merger proposal. Instead, if the banking agencies and CFPB differ on a merger application, the banking agencies automatically prevail by virtue of their final decision-making authority, leaving the CFPB without recourse to protect consumers. Second, relegating the CFPB to a consultative role reduces its incentive to evaluate bank merger proposals carefully. The CFPB might choose not to devote resources to interagency discussions on bank merger proposals, knowing that it is not accountable for rendering final decisions on merger proposals and that, in any event, the banking agencies might ignore its input. Accordingly, the banking agencies' informal consultation with the CFPB cannot substitute for the Bureau's formal participation in bank merger reviews.

that they will not approve a large bank merger absent a favorable recommendation by the CFPB Director.

2. Financial Stability

The 2008 financial crisis exposed the danger of megamergers that create "too big to fail" financial institutions. In response to the crisis, Congress added a new financial stability factor to the Bank Merger Act that requires the agencies to consider the extent to which a merger proposal poses "risk[s] to the stability of the United States banking or financial system."[49] To date, however, neither the FDIC's regulations nor its Statement of Policy Regarding Bank Mergers address this financial stability provision.

Over the past decade, the agencies' ad hoc application of the financial stability factor in bank merger applications has proven deficient in three critical respects. First, the agencies' financial stability framework lacks clarity and analytical rigor. Although the agencies have identified relevant quantitative metrics—e.g., the resulting firm's share of U.S. financial system assets, or its proportion of outstanding U.S. credit card balances—they have not explained how they evaluate these data. It is unclear, for example, whether the agencies consider certain metrics to be more important than others or how the agencies ultimately decide, based on these data, whether the resulting firm's distress would destabilize financial markets. Second, the agencies have not established an upper limit on financial stability risks in bank merger proposals. In the decade since Congress enacted the financial stability factor, the agencies have not denied a merger on financial stability grounds. Nor have they issued rules or guidance identifying the types of mergers that they would deem impermissible under the financial stability factor. Finally, the agencies have not only failed to establish sensible ex ante systemic risk limits, but they also have demonstrated unreasonably high systemic risk tolerance. Despite the new financial stability factor, the agencies have continued approving mergers among the largest U.S. banks, including BB&T's merger with SunTrust, Morgan Stanley's acquisition of E*Trade, and PNC's acquisition of BBVA's U.S. assets.

The agencies' high tolerance for these recent mergers is in tension with empirical research and historical experience suggesting that such deals can pose a risk to the financial system. Numerous empirical studies have demonstrated that greater consolidation in the financial sector increases systemic risks.[50] One particularly relevant study by Federal Reserve economists showed that the collapse of a single $250 billion bank would be far worse for the economy than if five $50 billion

[49] 12 U.S.C. § 1828(c)(5) (2018).

[50] *See, e.g.*, Gregor N.F. Weiss et al., *Systemic Risk and Bank Consolidation: International Evidence*, 40 J. BANKING & FIN. 165, 174-77 (2014) (finding a significant increase in the post-merger systemic risk of consolidating banks and their competitors); Simone Varotto & Lei Zhao, *Systemic Risk and Bank Size*, 82 J. INT'L MONEY & FIN. 45, 53-54 (2018) (concluding that a bank's size, while not determinative, is the primary driver of its systemic riskiness); *see also* Andre Uhde & Ulrich Heimeshoff, *Consolidation in Banking and Financial Stability in Europe: Empirical Evidence*, 33 J. BANKING & FIN. 1299, 1305-10 (2009) (concluding that national banking market concentration has a negative effect on financial stability).

banks failed separately.[51] Moreover, depository institutions like Washington Mutual, Countrywide, and National City—all similar in size to PNC, BB&T, and SunTrust—proved to be systemically important when they collapsed in 2008.[52] The agencies, however, have not even acknowledged—let alone rebutted—this cautionary evidence in the context of their recent bank merger approvals.

Taken together, these shortcomings suggest that the agencies should adopt a more systematic and stringent approach to their financial stability analyses. The agencies' ill-defined financial stability framework contrasts sharply with their clear-cut approach to competitive considerations in bank merger applications. The agencies rely on the HHI—calculated by summing the squared market shares of each firm in the market—to determine if a proposed merger would substantially lessen competition in a geographic market.[53] The HHI is significantly more systematized than the nebulous financial stability framework. Adopting an analogous index-based framework for systemic risk could significantly enhance the clarity, analytical rigor, and efficacy of the agencies' financial stability analyses.

Conveniently, scholars and policymakers have developed numerous quantitative metrics to assess a financial institution's systemic importance within the past decade. Most significantly, the Basel Committee on Bank Supervision (BCBS) has developed a formula to compute a firm's systemic risk score based on a its size, complexity, interconnectedness, cross-jurisdictional activity, and substitutability.[54] Policymakers already rely on this metric in several contexts. For example, the Federal Reserve uses the BCBS's systemic risk formula to assign risk-based capital requirements to the most systemically important banks.[55] The Federal Reserve proposed in 2018 to further incorporate the BCBS's systemic risk formula in the U.S. regulatory regime by using it to determine a systemically-important bank's leverage capital requirements.[56] Policymakers, in sum,

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[51] Amy G. Lorenc & Jeffrey Y. Zhang, *How Bank Size Relates to the Impact of Bank Stress on the Real Economy*, 62 J. CORP. FIN. 101592 (2020) (concluding that financial stress at large banks has a significantly stronger, negative impact on the real economy compared to smaller banks).

[52] *See* Arthur E. Wilmarth, *Raising SIFI Threshold to $250B Ignores Lessons of Past Crises*, AM. BANKER (Feb. 7, 2018), https://www.americanbanker.com/opinion/raising-sifi-threshold-to-250b-ignores-lessons-of-past-crises.

[53] The agencies follow a clear-cut rule: a merger generally does not pose competitive concerns unless the post-merger HHI is at least 1,800 and merger increases the HHI by more than 200 points. Antitrust Div., *Bank Merger Competitive Review—Introduction and Overview,* U.S. DEP'T JUST. (Sept. 2000) [hereinafter *Bank Merger Guidelines*], https://www.justice.gov/sites/default/files/atr/legacy/2007/08/14/6472.pdf.

[54] *See* Basel Comm. on Banking Supervision, *Global Systemically Important Banks: Updated Assessment Methodology and the Higher Loss Absorbency Requirement,* BANK FOR INT'L SETTLEMENTS 4-11 (2013) [hereinafter *BCBS Assessment Methodology*], https://www.bis.org/publ/bcbs255.pdf. Other systemic risk metrics include SRISK, which measures a firm's expected capital shortfall in a severe market decline, and Conditional Value-at Risk, which quantifies the extent to which distress at a single firm would increase the riskiness of the broader financial system. *See Modernizing Bank Merger Review*, *supra* note 1, at 472.

[55] *See* 12 C.F.R. §§ 217.400-.404 (2020).

[56] *See* Regulatory Capital Rules: Regulatory Capital, Enhanced Supplementary Leverage Ratio Standards for U.S. Global Systemically Important Bank Holding Companies and Certain of Their Subsidiary Insured Depository Institutions; Total Loss-Absorbing Capacity Requirements for U.S. Global Systemically Important Bank Holding Companies, 83 Fed. Reg. 17317 (Apr. 19, 2018) (codified at 12 C.F.R. § 217.11 (2020)).

deem the BCBS systemic risk score sufficiently reliable to use it when making significant regulatory decisions.

Building on this trend, the banking agencies should systematize their bank merger analysis by establishing a quantitative systemic risk limit for bank mergers using the BCBS systemic risk score. The agencies could issue a rule or guidance establishing thresholds beyond which they would presumptively deny a merger on financial stability grounds. For example, the agencies could adopt a presumption against a merger where the resulting firm's BCBS systemic risk score exceeds 50 and the merger increases the score by at least 3 points.[57] These thresholds of course, are merely suggestions, and the agencies should set limits that are informed by econometric analyses and public notice and comment.[58]

A quantitative systemic risk limit based on the BCBS systemic risk score would be a significant improvement over the agencies' current ad hoc approach to the financial stability factor. A systematized methodology would enhance the analytical rigor of the financial stability framework by standardizing how the agencies evaluate systemic risk data. If codified in rulemaking or guidance, an appropriate systemic risk limit could prevent agencies from approving increasingly risky mergers in the future. Furthermore, a quantitative systemic risk limit would add clarity to an otherwise opaque process and thereby reduce confidential pre-merger consultations between banks and their regulators. If banks have greater certainty about how the agencies will evaluate systemic risk, they will have less need to confer confidentially with the agencies before signing a merger agreement.

Finally, in light of financial stability risks posed by large regional banks, the agencies should strongly consider enacting total loss absorbing capacity (TLAC) requirements for such institutions through notice-and-comment rulemaking, as Acting Comptroller of the Currency Michael Hsu recently suggested.[59] The agencies, however, should remain cautious about the extent to which a TLAC requirement would mitigate financial stability risks from a large regional bank merger. The TLAC concept remains untested. Indeed, the FDIC has never attempted to resolve a financial institution that is subject to the TLAC requirement, and the single-point-of-entry resolution strategy has not been tried. Accordingly, although the agencies should create a TLAC requirement for large regional banks, they should not assume that TLAC offsets the financial stability risks of a large regional bank merger.

3. Competition

[57] As a reference point, Citizens Financial Group's most recent publicly available BCBS systemic risk score was 50. *See* OFFICE OF FIN. RESEARCH, *Bank Systemic Risk Monitor*, https://www.financialresearch.gov/bank-systemic-risk-monitor/.

[58] The agencies could retain discretion to approve a merger in excess of the systemic risk limits in an emergency situation, when denial of the merger would jeopardize financial stability. By contrast, the agencies could also retain discretion to deny a merger below the systemic risk limits if other factors indicated that the transaction would increase risks to financial stability.

[59] *See* Michael J. Hsu, Acting Comptroller of the Currency, Financial Stability and Large Bank Resolvability (Apr. 1, 2022), https://www.occ.gov/news-issuances/speeches/2022/pub-speech-2022-33.pdf.

Like the "convenience and needs" and financial stability factors, the agencies' approach to the Bank Merger Act's competition factor has proven inadequate. The Bank Merger Act prohibits the agencies from approving a transaction "which would result in a monopoly … 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."[60] Regrettably, the agencies have neglected the competition factor for the past several decades. Specifically, the agencies have established insufficiently rigorous HHI concentration thresholds and overlooked numerous non-price harms stemming from bank consolidation. As my scholarship has documented, the agencies' lax approach to the competition factor has encouraged excessive consolidation in the banking sector and broader economy, inflicting harm on consumers, small businesses, and LMI communities.[61]

Going forward, the agencies should strengthen and expand the analytical tools used to identify anticompetitive bank consolidation. I propose four specific enhancements: (A) reducing the HHI threshold in the Bank Merger Guidelines, (B) deemphasizing mitigating factors in bank merger reviews, (C) evaluating the mix of large and small institutions in markets experiencing mergers, and (D) considering the distortive effects of the "too-big-to-fail" subsidy.

A. Lower the HHI Threshold

To mitigate competitive harms from bank consolidation, the banking agencies should reduce the HHI threshold that triggers enhanced scrutiny of bank mergers. Under the current Bank Merger Guidelines established by the banking agencies and Department of Justice (DOJ), the agencies are unlikely to deny a proposed merger if the post-merger HHI would be below 1,800 or the merger would cause the HHI to increase by less than 200 points.[62] This 1800/Δ200 threshold has proven insufficient to prevent anticompetitive harms. Indeed, even bank mergers that comply with the 1800/Δ200 threshold are associated with higher cost and lower availability of financial products.[63] Accordingly, the agencies should reduce the HHI threshold for enhanced screening of bank mergers. As one possibility, the agencies could commit to heightened scrutiny of a bank merger that would increase a market's HHI by more than 100 points to a level above 1,500—the same HHI threshold at which nonbanking mergers "potentially raise[s] competitive concerns," according to the DOJ's general merger guidelines.[64]

The banking sector has argued—erroneously—that the 1800/Δ200 threshold is already too stringent compared to the 2500/Δ200 threshold that triggers a presumption of anti-competitiveness

[60] 12 U.S.C. §§ 1828(c)(5). An agency may, however, approve a merger that substantially lessens competition or tends to create a monopoly if it finds that the anticompetitive effects "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." *Id.*

[61] *See Reviving Bank Antitrust*, *supra* note 6, at 32-47.

[62] *See Bank Merger Guidelines*, *supra* note 53.

[63] *See* Robert Mann, Bank Competition, Local Labor Markets, and the Racial Employment Gap 24 (Jan. 27, 2022) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4013042.

[64] U.S. DEP'T OF JUST. & FED. TRADE COMM'N, HORIZONTAL MERGER GUIDELINES 19 (2010), https://www.justice.gov/sites/default/files/atr/legacy/2010/08/19/hmg-2010.pdf.

in other industries under the DOJ's general merger guidelines.[65] The comparison to the general merger guidelines' 2500/Δ200 threshold, however, is inapposite. First, a proposed bank merger that exceeds the Bank Merger Guidelines' HHI threshold merely receives enhanced scrutiny rather than a presumption of anti-competitiveness, as is the case for nonbank mergers that exceed the 2500/Δ200 threshold.[66] In this way, the Bank Merger Guidelines' HHI screen is more akin to the 1500/Δ100 threshold in the general merger guidelines for potentially anticompetitive mergers that "warrant scrutiny."[67] Second, the costs of "false negatives"—or misguided decisions to allow anticompetitive mergers—are higher in banking than in many other industries. Compared to other industries with lower entry barriers, regulation and competitive disadvantages deter de novo banks from forming to counteract the harmful effects of an anticompetitive merger. Moreover, in light of banking's unique and essential role in the economy, anticompetitive bank mergers inflict more extensive and longer-lasting societal harms than anticompetitive mergers in most other industries. As the Supreme Court stated in *Philadelphia National Bank*, "[I]f the costs of banking services and credit are allowed to become excessive by the absence of competitive pressures, virtually all costs, in our credit economy, will be affected…."[68]

As an alternative, or in addition, to lowering the HHI threshold, the agencies could supplement their analyses with other concentration metrics. While widely considered to be a conceptual advancement over the four-firm concentration ratio previously used in bank antitrust, the HHI has nonetheless been subject to criticism.[69] Skeptics contend, for example, that the HHI undervalues smaller firms' competitive significance and is insufficiently sensitive to inequality in firms' market shares.[70] To mitigate the HHI's shortcomings, the agencies could use other measures of concentration, such as the Hall-Tideman Index (HTI) or comprehensive industrial concentration index (CCI), in addition to the HHI.[71] If appropriately calibrated, these alternative metrics could

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[65] *See, e.g.*, *See, e.g.*, Letter from Gregg Rozansky, Senior Vice President, Bank Pol'y Inst., to Makan Delrahim, Assistant Att'y Gen., U.S. Dep't of Just. 2, 11 (Oct. 15, 2020), https://www.justice.gov/atr/page/file/1330306/download; Comments of Wachtell, Lipton, Rosen & Katz to U.S. Dep't of Just., Antitrust Div. 4 (Oct. 15, 2020), https://www.justice.gov/atr/page/file/1330316/download.

[66] *Compare Bank Merger Guidelines*, *supra* note 53, at 3 ("The [DOJ] and the banking agencies are likely to examine a transaction in more detail if it exceeds the 1800/200 threshold…."), *with* HORIZONTAL MERGER GUIDELINES, *supra* note 64, at 19 ("Mergers resulting in highly concentrated markets [with an HHI above 2,500] thatinvolve an increase in the HHI of more than 200 points will be presumed to be likely to enhance market power.").

[67] HORIZONTAL MERGER GUIDELINES, *supra* note 64, at 19.

[68] United States v. Phila. Nat'l Bank, 374 U.S. 321, 372 (1963).

[69] *See, e.g.*, Jay Greenfield, *Beyond Herfindahl: Non-Structural Elements of Merger Analysis*, 53 ANTITRUST L.J. 229, 233 (1984) (discussing shortcomings of the HHI).

[70] *See, e.g.*, Michael O. Finkelstein & Richard M. Friedberg, *The Application of the Entropy Theory of Concentration to the Clayton Act*, 76 YALE L.J. 677, 707 (1967) (criticizing the HHI for understating the role of small competitors); Stephen A. Rhoades, *Market Share Inequality, the HHI, and Other Measures of the Firm-Composition of a Market*, 10 REV. INDUS. ORG. 657, 672-73 (1995) (concluding that the HHI undervalues market share inequality among competitors).

[71] *See* Jacob A. Bikker & Katharina Haaf, *Measures of Competition and Concentration in the Banking Industry: A Review of the Literature*, ECON. & FIN. MODELLING, Summer 2002, at 1, 6-17 (reviewing alternative concentration measures). The HTI resembles the HHI but weights the market shares of individual banks by their rankings within the market, thereby granting more significance to the total number of competitors. *See id.* at 9-10. The CCI "is the sum of the proportional share of the leading bank and the summation of the squares of the proportional sizes of each bank,

augment the traditional HHI analysis and thereby help the agencies identify anticompetitive bank mergers.

B. Deemphasize Mitigating Factors

In addition to reducing the HHI threshold, the banking agencies should stop relying on mitigating factors in bank competition analysis. The banking agencies have frequently cited factors—including branch divestitures and potential market entry—as mitigating the potential anticompetitive effects of a bank merger. In practice, however, these purported mitigants do not significantly alleviate the harmful consequences of bank consolidation. Accordingly, the agencies should place little weight on mitigating factors in future bank merger evaluations.

One of the most common mitigating factors cited in bank antitrust—branch divestitures—appears to be of dubious societal value. When a proposed merger exceeds the 1800/Δ200 HHI threshold, the banking agencies and the DOJ often require the merging banks to sell certain branches and their associated deposits as a condition of approval.[72] In theory, branch divestitures mitigate anticompetitive harms because they reduce the merged banks' presence in the market and bolster the acquirer's competitive position. In reality, however, divestitures have proven ineffective in maintaining the competitiveness of local banking markets. Despite having their accounts transferred to a new bank as part of a divestiture agreement, many customers—especially small businesses—voluntarily choose to remain with their original bank because of existing relationships with loan officers and other bank personnel.[73] As a result, merging banks often maintain their market shares notwithstanding branch divestitures, leading to anticompetitive outcomes.[74] Thus, although policymakers previously assumed that branch divestitures would neutralize the potential anticompetitive effects of a proposed bank merger, divestitures have proven to be an ineffective remedy, and the agencies should therefore deemphasize them as a mitigating factor.

Another commonly-cited mitigating factor—a market's attractiveness for new entry—is equally unproven in alleviating the harms of bank consolidation. Under the Bank Merger Guidelines, the agencies may authorize a merger that exceeds the 1800/Δ200 HHI threshold based on

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weighted by a multiplier reflecting the proportional size of the rest of the industry." *Id.* at 11. The CCI is thus thought to reflect both the market share of a dominant firm and the dispersion of smaller competitors. *See id.*

[72] For example, in 2019, BB&T and SunTrust divested 28 branches and $2.3 billion in deposits as a condition of the banks' merger. *See* Press Release, Dep't of Just., Justice Department Requires Divestitures in Orderfor BB&T and SunTrust to Proceed with Merger (Nov. 8, 2019), https://www.justice.gov/opa/pr/justice-department- requires-divestitures-order-bbt-and-suntrust-proceed-merger.

[73] *See* Gam & Zhang, *supra* note 23, at 4-5 (analyzing bank mergers between 1999 and 2014); Jack Liebersohn, How Effective is Antitrust Intervention? Evidence From Bank Mergers (June 4, 2021), https://www.dropbox.com/s/plvsp4eqz2lmphn/liebersohn_banks_submissionaer.pdf?dl=0 (analyzing bank mergers between 1994 and 2017).

[74] *See* Gam & Zhang, *supra* note 23, at 4 ("[B]ank divestitures do not significantly change the local small business lending activities of either the merging or competing banks.… This finding suggests that antitrust divestitures are ineffective in maintain competitiveness in the small business lending market."); Liebersohn, *supra* note 73, at 37-40 (concluding that branch divestitures have no effect on the small business loan market).

"expectations about potential entry by institutions not now in the market."[75] To evaluate a market's attractiveness for entry, the agencies consider recent de novo entry by out-of-market banks and demographic factors such as population growth rate and per capita income.[76] Attractiveness for entry is now "the most prominent mitigating factor cited when potentially anticompetitive consolidations are allowed."[77] However, Federal Reserve research has cast doubt on the extent to which attractiveness for entry actually mitigates anticompetitive harms. Indeed, Fed economists have found that past entry and demographic variables are generally not correlated with—and thus not predictive of—future entry.[78] Even bank lobbyists acknowledge that attractiveness for entry is unproven as a mitigating factor.[79] In the future, therefore, the agencies should discount a market's attractiveness for entry when evaluating a proposed merger's potential anticompetitive effects.

C. Evaluate Mix of Large and Small Institutions in a Market

As a supplement to the traditional HHI analysis, the banking agencies should expressly consider the mix of large and small institutions that would remain in a market following a merger. The Bank Merger Guidelines' narrow focus on deposit-based HHIs obscures an important determinant of a market's competitive dynamics: the size of the competing banks. Small, locally-rooted community banks and large, multinational megabanks typically serve different customers, specialize in different products, and use different underwriting techniques.[80] Thus, two markets with identical deposit concentration metrics may nonetheless perform differently if one market is dominated by large banks and the other by small banks.[81] The HHI's blindness to competitors' size is part of the reason why large bank acquisitions of small firms often harm customers even when the HHI does not suggest the merger would be anticompetitive. As former Federal Reserve Governor Jeremy Stein and coauthors have asserted, "The key issue might be not so much about banks having market power in the traditional Herfindahl-index sense but rather, the degree to which [customers] have choice over the size of the bank they do business with."[82]

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[75] *Bank Merger Guidelines*, *supra* note 53, at 3.

[76] *See, e.g.*, Centura Banks, Inc., 76 Fed. Rsrv. Bull. 869, 872 (1990).

[77] Robert M. Adams & Dean F. Amel, *The Effects of Past Entry, Market Consolidation, and Expansion by Incumbents on the Probability of Entry in Banking*, 48 REV. INDUS. ORG. 95, 96 (2016).

[78] *See id.* at 117-118 (concluding that demographic variables are correlated with probability of entry only in extreme cases and that past bank entry is uncorrelated with new charter entry in rural markets).

[79] *See* Paul Calem & Gregg Rozansky, *Bank Merger Applications in Law and Practice*, BANK POL'Y INST. 8 (Aug. 19, 2021), https://bpi.com/wp-content/uploads/2021/08/Bank-Merger-Applications-in-Law-and-Practice.pdf ("[W]e are not aware of any study assessing whether the use of th[e attractiveness for entry] criterion as a mitigating factor in merger decisions yielded the intended longer-term outcome.").

[80] *See* Allen N. Berger et al., *Does Function Follow Organizational Form? Evidence from the Lending Practices of Large and Small Banks*, 76 J. FIN. ECON. 237, 240-41 (2005) (documenting that smaller banks lend to smaller firms and use "softer" underwriting criteria than larger banks).

[81] *Cf.* Kwangwoo Park & George Pennacchi, *Harming Depositors and Helping Borrowers: The Disparate Impact of Bank Consolidation*, 22 REV. FIN. STUD. 1, 2 (2009) ("[A] greater presence of [large] banks tends to promote competition in retail loan markets but also tends to harm competition in retail deposit markets.").

[82] Berger et al., *supra* note 80, at 266.

To address this issue, the agencies should affirmatively consider the mix of megabanks, regional banks, and community banks in a market in addition to the HHI and other concentration metrics. The OCC's bank merger framework from the 1960s provides a good model. After Congress adopted the Bank Merger Act, the OCC implemented a "balanced banking structure" approach to bank merger analysis.[83] This approach "stressed the range of bank size," and the OCC sought to ensure that "each market [w]ould have a range of small, medium and large banks."[84] The contemporary banking agencies should implement a similar approach, striving to avoid mergers that would deprive a market of competition among banks of a certain size. This approach would subject transactions like First Citizens BancShares' 2020 acquisition of Entegra Bank to heightened scrutiny.[85] That deal eliminated Entegra—a small, $1.7 billion bank in southwest North Carolina—and left more than ninety-five percent of the deposits in one market controlled by medium and large banks.[86] Even though the relevant market's post-merger HHI was consistent with the 1800/Δ200 threshold when accounting for mitigating factors, the lack of size diversity among the remaining banks threatens to impair competition, particularly for small business loans.[87] Accordingly, a more effective bank antitrust framework would evaluate the mix of large and small institutions in a market in addition to the HHI.

D. Consider Distortive Effects of the "Too-Big-To-Fail" Subsidy

The current bank merger framework overlooks the way in which bank consolidation has exacerbated "too-big-to-fail" subsidies that distort competition and deter new entrants. Market participants generally expect that if a large bank were to experience economic distress, the government would bail out the bank rather than let it collapse.[88] As a result, big banks have traditionally been able to borrow at favorable rates relative to smaller competitors.[89] By one estimate, this implicit subsidy reached more than 600 basis points in the lead-up to the 2008 financial crisis.[90] While the size of the "too-big-to-fail" subsidy has shrunk since the crisis, it still

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[83] Earl W. Kintner & Hugh C. Hansen, *A Review of the Law of Bank Mergers*, 14 B.C. INDUS. & COM. L. REV. 213, 223 (1972).

[84] *Id.*

[85] First Citizens BancShares, Inc., 106 Fed. Rsrv. Bull. 44 (2020).

[86] After the transaction, more than ninety-five percent of the deposits in the Transylvania County banking market were controlled by First Citizens (36 percent), Wells Fargo (22 percent), United Community Bank (19 percent), Fifth Third Bank (11 percent), and PNC Bank (7 percent)—all of which had more than $20 billion in assets and were not headquartered locally. *See id.* at 48-49; Transylvania County, NC Banking Market, FED. RSRV. BANK OF ST. LOUIS CASSIDI (June 30, 2021), https://cassidi.stlouisfed.org/markets/37295/hhi.

[87] *See* First Citizens BancShares, Inc., *supra* note 85, at 48-49 (discussing the Transylvania County banking market's post-merger HHI); Berger et al., *supra* note 80, at 266 (assessing competitive consequences of markets that lack banks of varying sizes).

[88] *See* Saule T. Omarova, *The "Too Big to Fail" Problem*, 103 MINN. L. REV. 2495, 2500 (2019).

[89] *See* Bhanu Balasubramnian & Ken B. Cyree, *Has Market Discipline Improved After the Dodd-Frank Act?*, 41 J. BANKING & FIN. 155, 165 (2014); Viral V. Acharya et al., *The End of Market Discipline? Investor Expectations of Implicit Government Guarantees* 30–33 (Munich Personal RePEc Archive, Working Paper No. 79700, 2016).

[90] *See* U.S. GOV'T ACCOUNTABILITY OFF., GAO-14-621, LARGE BANK HOLDING COMPANIES: EXPECTATIONS OF GOVERNMENT SUPPORT 51 (2014).

persists.[91] When larger banks merge, they obtain the benefit of this funding advantage.[92] The expansion of the "too-big-to-fail" subsidy via bank consolidation distorts the competitive dynamics of the financial sector. Indeed, smaller banks cite the "too-big-to-fail" subsidy as an impediment to fair competition.[93] In addition, megabanks' artificial funding advantages likely deter new banks from forming.[94] Under the prevailing approach, however, the agencies "d[o] not account for … the competitive distortions in creating [too-big-to-fail] firms."[95]

To faithfully effectuate the Bank Merger Act's competition factor, the agencies should consider market distortions created by the "too-big-to-fail" subsidy. Going forward, the agencies should routinely perform econometric analyses to assess whether a bank would accrue a new or expanded "too-big-to-fail" subsidy following a proposed merger. If models suggest that a merger such as BB&T's combination with SunTrust would enlarge the "too-big-to-fail" subsidy, the relevant agency should block the merger to prevent further competitive distortions.

Thank you again for the opportunity to comment on the regulatory framework for bank merger transactions. Please let me know if I can provide any additional information.

Sincerely,

Jeremy C. Kress
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Co-Faculty Director, Center on Finance, Law & Policy

[91] Following the 2008 crisis and ensuing regulatory reforms, typical estimates of the "too-big-to-fail" subsidy have ranged from roughly 20 to 100 basis points. *See* Nicola Cetorelli & James Traina, *Resolving "Too Big to Fail"* 1-2 n.3 (Fed. Rsrv. Bank of N.Y., Staff Rep. No. 859, 2018), https://www.newyorkfed.org/medialibrary/media/research/ staff_reports/sr859.pdf (summarizing various estimates).

[92] A study by Federal Reserve Bank of Philadelphia economists found that banks paid an extra premium for mergers that would qualify them for "too-big-to-fail" status. *See* Elijah Brewer III & Julapa Jagtiani, *How Much Did Banks Pay to Become Too-Big-to-Fail and to Become Systemically Important?*, 43 J. FIN. SERVS. RSCH. 1, 4 (2013).

[93] *See* INDEPENDENT CMTY. BANKERS OF AM., TOO-BIG-TO-FAIL SUBSIDIES THREATEN ECONOMY, COMMUNITY BANKS, AND TAXPAYERS 1-2 (2014), https://www.icba.org/docs/default-source/icba/advocacy-documents/ testimony/113th-congress/test073114.pdf?sfvrsn=2.

[94] *Cf.* David Zaring, *Modernizing the Bank Charter*, 61 WM. & MARY L. REV. 1397, 1441-47 (2020) (documenting decline in de novo bank charters following 2008 financial crisis).

[95] Maurice E. Stucke, *Occupy Wall Street and Antitrust*, 85 S. CAL. L. REV. POSTSCRIPT 33, 49 (2012).