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Agencies Finalize Changes to Bank Merger Review Policies

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Financial Services

On September 17, 2024, two of the three federal banking agencies, the Office of the Comptroller of the Currency ("OCC") and the Federal Deposit Insurance Corporation ("FDIC"), finalized policy statements that change in many ways how these agencies review bank merger proposals under the Bank Merger Act ("BMA"). The final OCC and final FDIC statements of policy mostly adopt the approaches that the agencies proposed earlier this year. Of particular note, the Federal Reserve has not made changes to its merger policies.

Also on September 17, 2024, the United States Department of Justice ("DOJ") withdrew from the 1995 Bank Merger Guidelines that had previously governed its own review of the competitive effects of bank mergers, announcing that it will instead evaluate the bank mergers using its 2023 Merger Guidelines that apply across all industries. Covington summarized the 2023 Merger Guidelines here. The DOJ also released a brief 2024 Banking Addendum to the 2023 Merger Guidelines, though the addendum does not provide much clarity on how the DOJ will review bank mergers. The three federal agencies did not join the 2023 Merger Guidelines or the 2024 Banking Addendum and appear to remain parties to the 1995 Bank Merger Guidelines.

At a high level, the final OCC and FDIC statements of policy and the DOJ's withdrawal from the 1995 Bank Merger Guidelines demonstrate that the current leadership of these agencies is, and has been, adopting a more skeptical view of bank mergers than in the past.

Banks considering M&A in the current environment should consider the following takeaways:

- The most significant impact of the agencies' actions last week could be to the standards the agencies use to review the competitive impact of a merger. In particular, the DOJ's withdrawal from the 1995 Bank Merger Guidelines and its application of the 2023 Guidelines to bank mergers expand the range of mergers that the DOJ may challenge as anticompetitive and create significant uncertainty regarding the DOJ's approach.
  - The 2023 Merger Guidelines set forth more stringent concentration limits than the 1995 Bank Merger Guidelines. The 2023 Merger Guidelines presume a merger to be illegal when there is a change in the Herfindahl–Hirschman index ("HHI") of more than 100 and either the resulting market has an HHI that exceeds 1800 or the resulting institution has a market share that exceeds 30 percent. Under the 1995 Bank Merger Guidelines, a transaction requires further analysis when it causes a change in the HHI of more than 200 and the resulting market has an HHI of more than 1800.

- Further, the 2023 Merger Guidelines provide additional, largely qualitative grounds on which the DOJ could object to a transaction beyond traditional local market concentration.
- Lack of clarity in how the DOJ will apply the 2023 Guidelines may chill merger activity unless the DOJ provides more specificity. Uncertainty around the DOJ's approach increases the risk that an acquirer will need to make unplanned divestitures to secure regulatory approval, undermining an acquirer's ability to know with certainty what assets and liabilities it will own following a transaction.

- The OCC's and FDIC's final statements of policy are largely the same as the proposals the agencies released earlier this year, though the agencies made a few substantive changes.
  - Of particular note, the OCC amended language that described attributes of "applications that are consistent with approval," to clarify that these are attributes of applications that "tend to withstand scrutiny more easily and are more likely to be approved expeditiously" and that the OCC can still approve an application that lacks one or more of these attributes.
  - Also of note, the FDIC omitted proposed language that had suggested that the FDIC will not approve a merger that would result in a "weaker" bank. New language states instead that the FDIC will make a favorable finding on financial resources factor only when merger results in an bank that presents "less financial risk than the financial risk posed by the institutions on a standalone basis."
- Through their new guidance, the OCC, FDIC, and DOJ appear to be raising the bar for the types of mergers that they will approve. These agencies may deny merger applications and/or impose burdensome conditions in their approval orders more frequently than in the past.
- More than ever, regulators want acquirers to make an affirmative showing that management can capably operate the combined institution safely and soundly and in a compliant manner and deliver benefits to a broader range of constituencies. Parties to a merger should expect to do more upfront integration planning and to provide more information to regulators as part of the application process. The cost of reaching every milestone in a transaction – signing, filing of regulatory applications, receipt of regulatory approvals, and closing – will increase, and we expect the pre-signing upfront costs will increase the most because of the extra work acquirers will need to do in order to achieve more certainty around regulatory approval. So too will the parties' sunk costs if the regulators ultimately deny their applications.
- The new approach in Washington heightens the need for acquirers to discuss potential transactions with their supervisory teams well in advance of signing, to be thoughtful about structuring transactions and integration plans, and to consider what commitments they could make – or what conditions might be imposed on them – to secure regulatory approval.
- In terms of comparing the final OCC and FDIC statements of policy, they share several themes and features, as both statements indicate that these agencies have grown concerned with size, rapid growth, integration and risk-management issues, branch closures and related job losses, and other reductions in service, and are considering holding public hearings on a broader range of transactions. Acting Comptroller Hsu

called the two statements "broadly consistent" with each other. At the same time, there are key differences between the final OCC and FDIC statements of policy.

- Federal Reserve Vice Chair for Supervision Michael Barr stated earlier this year that the Federal Reserve has no plans to release its own new bank merger policy. However, the Federal Reserve released revised instructions to its Form FR Y-3, which is required for applications for mergers of bank holding companies, in August 2024. Among other changes, the revised instructions now request information regarding an institution's integration planning, reflecting a common theme across the three federal banking agencies.

Differences in the OCC and FDIC policy statements, the fact that the Federal Reserve has not issued its own statement of policy, and the DOJ's withdrawal from the 1995 Bank Merger Guidelines all indicate that the federal agencies responsible for reviewing bank mergers appear to be taking divergent approaches to evaluating merger applications. Of course, it remains to be seen how these policy developments will be impacted by whichever presidential administration occupies the White House come next year.

To highlight the similarities and differences in the OCC's and FDIC's statements of policy, we have prepared the following chart that compares their notable provisions, grouped by subject matter.

OCC Statement	FDIC Statement
Competition/Antitrust Analysis	
No comparable provisions: does not address how the OCC will evaluate the competitive impact of a transaction	***More Holistic But Less Clear Standards.*** Provides for a more nuanced review of the competitive effects of a transaction, but in the process, will eliminate the clarity that the current system provides (even if it is imperfect), and create significant uncertainty. Vice Chairman of the FDIC Board Hill criticized the deemphasis of HHI thresholds in the final rule, referring to them as a predictable proxy for concentrations, and stating that this change along with the consideration of "concentrations in any specific products or customer segments" (*see below*) will lead to unpredictability.
	Broader Sources of Competition. On the positive side, considers competition from non-banks lenders in the antitrust analysis (and, as with the prior FDIC Statement of Policy, the FDIC will continue also to consider non-local lenders as appropriate).

OCC Statement	FDIC Statement
	Additional Competition Analyses. Goes beyond the focus on local deposits by more clearly considering concentrations in other products and services. The statement also expands to regional and national markets and makes clearer the potential consideration of pricing data – but without explaining how these other factors will be considered.
	Consideration of Management and Board Deliberations. Provides that the "narrative describing the analysis and evaluation of the transaction should be supported by studies, surveys, analyses and reports, including those prepared by or for officers, directors, or deal team leads."
	Requirements for Divestitures. Requires antitrust-related divestitures to be completed before the merger can close, and sets out a "general[] expect[ation]" that the parties will not enter into or enforce non-compete agreements with employees of divested entities.
Managerial and Financial Resources	
Specific Expectations for Target Supervisory Status. Provides that applications that that "tend to withstand scrutiny more easily and are more likely to be approved expeditiously" will involve an acquiring institution and target with traits such as CAMELS composite and consumer compliance ratings of 1 or 2 and Community Reinvestment Act ("CRA") ratings of "Satisfactory." However, the preamble to the final OCC statement clarifies that "the OCC has approved many transactions where the target is not an eligible depository institution and the	***General Consideration of Target Supervisory Status.*** Considers the managerial resources, including supervisory history and ratings, of both parties to the merger, but would not set forth specific minimum requirements for target entities' supervisory status. While less defined than the OCC approach, the FDIC approach appears to be closer to the agencies' historical practice, which is to consider the target's status only insofar as it affects the prospects of the resulting institution.

OCC Statement	FDIC Statement
acquirer brings the appropriate financial and managerial resources to bear to mitigate deficiencies at the target."	
Concerns with Rapid Growth. Provides that the OCC is less likely to approve a transaction when the acquirer has experienced "rapid growth" or has engaged in multiple acquisitions with overlapping integration periods.	***Concerns with Rapid Growth.*** Similar to the OCC, considers "recent rapid growth" and the record of management in overseeing and controlling risks associated with such growth.
Concerns Over Integration. Considers IT systems compatibility and integration issues and provides that such issues could be a basis for conditions to be imposed or the transaction to be denied. This focus may require significant upfront work (and cost) by both institutions, even prior to signing a definitive agreement, and acquiring banks may want to preview their integration plans with their supervisory team.	***Specific Integration Planning Expectations.*** Sets forth an expectation for integration plans to cover "human capital; products and services; operating systems, policies, and procedures; internal controls and audit coverage; physical locations; information technology; and risk management programs." Provides for the FDIC to conduct a "comprehensive evaluation" of each entity's program to combat money laundering (Anti-Money Laundering or "AML") and counter the financing of terrorism ("CFT") and consider whether the resulting bank has developed an appropriate plan for the integration of the combined operations into a single AML/CFT program. Compared to the OCC, the FDIC approach could require even more upfront work by both institutions – particularly in light of the substantial operational AML/CFT analyses required for the application.

OCC Statement	FDIC Statement
No comparable provision.	***Combined Institution Must Present "Less Financial Risk" than the Merging Parties on a Standalone Basis.*** Provides that the FDIC will generally find favorably on the financial resources factor only if "the merger results in a combined IDI that presents less financial risk than the financial risk posed by the institutions on a standalone basis." The preamble acknowledges that the combined institution may "look weaker financially on day one, post-merger" as a result of purchase accounting, but the FDIC will "broadly consider[] the long-term financial impacts over the near-term implications of a merger."
No comparable provision that separately considers each member of management or the performance of affiliates.	***Review of Management Team and Affiliates.*** Considers the background and experience of each member of management relative to the size, complexity, and risk profile of the resulting bank, including the managerial performance and supervisory record of affiliates and subsidiaries. This requirement, coupled with the FDIC's concerns over rapid growth, could slow an acquirer's ability to engage in multiple acquisitions in a short period of time.
No comparable provision.	***Review of Insider Payments.*** Considers the reasonableness of fees, expenses, and other payments made to insiders.
No comparable provision beyond a general review of the applicant's liquidity and liquidity risk management.	***Review of Specific Liquidity Factors.*** Specifically considers the extent of the resulting bank's projected reliance on uninsured deposits (under the Risk to the Stability of the United States Banking or Financial System factor) and its funding strategies.

OCC Statement	FDIC Statement
Convenience and Needs of the Community	
Plans to Maintain, Reduce, or Improve Credit Availability Throughout the Community. Provides that the OCC will consider whether the resulting institution has plans to "maintain, reduce, or *improve*" credit availability.	***Improved Ability to Serve Community.*** Provides that a transaction should enable the resulting bank to "*better*" meet the convenience and needs of its communities than would occur absent the merger. Many acquirers already make this showing, but the statement of policy's lack of objective standards will give the FDIC discretion to deny or impose conditions on more transactions.
General Consideration of Branch Closures. As is the case historically, considers any plans to close, consolidate, limit, or expand branches or branching services, including in low- or moderate-income ("LMI") areas.	***Specific Branch Closure Plans.*** Requires applications to include at least three years of information regarding projected branch expansions, closings, or consolidations.
New Focus on Job Losses. Considers any job losses or reduced job opportunities from branch staffing changes, including branch closures or consolidations. Consideration of job losses and branch closings without any specific standards will create uncertainty as to how many job losses or closings are too many for the OCC to grant approval.	***New Focus on Job Losses.*** Considers any job losses or lost job opportunities from branching changes.
Financial Stability and Other Size Issues	
Heightened Review at $50 Billion in Assets. Provides that applications "that tend to withstand scrutiny more easily and are more likely to be approved expeditiously" will involve a resulting institution with total assets of less than $50 billion, thereby enhancing scrutiny on transactions involving larger institutions.	***Added Scrutiny at $100 Billion in Assets.*** Provides that transactions that result in a bank with $100 billion or more in assets will be subject to added scrutiny.

OCC Statement	FDIC Statement
Presumption Against G-SIB Acquisitions. Provides that an application raises supervisory or regulatory concerns where the acquirer is a global systemically important banking organization ("G-SIB") or subsidiary thereof.	*No comparable provision.*
Public Comment Process	
Public Hearings Based on Size or Public Interest. Sets forth a number of factors that would determine whether the OCC will hold a public hearing on an application, including (1) "the significance of the transaction to the banking industry," which "may include the asset sizes of the institutions involved (e.g., resulting institution will have $50 billion or more in total assets)," and (2) the extent of public interest in the proposed transaction.	***Public Hearings Based on Size or Significance of Protests.*** Provides that the FDIC generally expects to hold a hearing for any application (1) resulting in a bank with more than $50 billion in assets or (2) for which "significant" CRA protests are received. Like the OCC, the FDIC is signaling that a bank crossing $50 billion in assets should be prepared for a public hearing to be held.
Application Procedures	
Standardize Processing Tracks. Eliminates the OCC's expedited processing track and streamlined application form for eligible mergers. In practice, these streamlined procedures have not provided significant relief to eligible institutions, so we do not expect a substantial practical effect from this change.	***Expedited Processing Not Amended.*** The FDIC has not amended its regulations governing expedited processing, codified at 12 C.F.R. § 303.11.
No comparable provision.	***Agency Statements on Withdrawn Applications.*** Provides that if an applicant withdraws its filing, the FDIC may release a statement regarding the concerns with the transaction if such a statement is "considered to be in the public interest for purposes of creating transparency for the public and future applicants." The FDIC had included identical language in the preamble to the recently proposed rule governing industrial bank deposit insurance applications.

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	Director Chopra stated that he believes it is generally "quite inappropriate" for applicants to be permitted to withdraw their BMA applications instead of receiving a denial. The possibility of such a public statement could have a significant chilling effect on mergers, even when two banks are otherwise eligible for approval. It could also incentivize applicants facing a denial to receive a denial order, which can be challenged in court, rather than withdraw their application.
Other Issues	
Heightened Review of Mergers of Equals. Provides that applications "that tend to withstand scrutiny more easily and are more likely to be approved expeditiously" will involve a target that has total assets that are less than or equal to the acquirer's total assets, thereby creating more scrutiny for mergers of equals. However, the preamble to the final statement states: "The indicator is not intended to discourage mergers of equals. It was included because, in the OCC's supervisory experience, mergers between institutions of similar sizes are likely to require more review than transactions where the target is much smaller than the acquirer." We expect that parties to a merger of equals will likely need to provide additional information to satisfy the OCC that the resulting institution has the managerial resources to complete a successful integration and operate a larger institution.	*No comparable provision.*
Heightened Review of Larger Party Merging into Smaller Party. Provides that a transaction is less likely to be approved where the acquirer is "functionally the target."	*No comparable provision.*

OCC Statement	FDIC Statement
No comparable provision. However, OCC regulations separately require an application for certain substantial changes in a bank's business, which could include some transactions that would be subject to the FDIC's review under the BMA.	***Expanded Jurisdiction to Review Transactions Under the BMA.*** The statement potentially expands the circumstances in which the FDIC would assert its authority to review a transaction under the BMA, including to cover: (1) purchase and assumption transactions or other transactions that are "mergers in substance," where the "target would no longer compete in the market, regardless of whether the target plans to liquidate immediately after consummating the transaction," (2) an FDIC-supervised bank's assumption of a deposit from another bank, or any bank's assumption of a deposit from a non-insured entity, even in the absence of an express agreement for a direct assumption and (3) a transfer of deposits from any IDI to a non-insured entity. While the lines the FDIC is drawing are not entirely clear, the FDIC may be expanding the situations in which it expects banks that work with fintech companies in Banking-as-a-Service ("BaaS") and other arrangements to submit a BMA application to establish new relationships.
No comparable provision.	***Scrutiny of Non-Traditional Business Models.*** Provides that the FDIC's Washington Office or Board of Directors reserves authority to act on certain merger applications that do not involve "traditional community banks." The preamble to the proposed statement of policy had stated that a bank that is not a "traditional community bank" generally: (1) focuses on products, services, activities, market segments, funding, or delivery channels other than local lending and deposit taking; (2) pursues a broad geographic footprint (such as operating nationwide from a limited number of offices); (3) pursues a monoline, limited, or specialty business model; or (4) operates within an organizational structure that involves significant affiliate or other third-party

OCC Statement	FDIC Statement
	relationships (other than common relationships such as audit, human resources, or core information technology processing services). Banks with non-traditional business models, including those that provide BaaS to fintech companies, should be prepared for significantly heightened scrutiny of their merger applications.

Covington's Financial Services Group has deep experience helping financial institutions secure regulatory approval of mergers and acquisitions. For additional information, please do not hesitate to contact the following lawyers:

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