



Federal Reserve Provides Guidance on Bank M&A

Posted by Edward D. Herlihy, Wachtell, Lipton, Rosen & Katz , on Friday, July 10, 2015

Editor's Note: [Edward D. Herlihy](#) is a partner and co-chairman of the Executive Committee at Wachtell, Lipton, Rosen & Katz. The following post is based on a Wachtell Lipton memorandum by Mr. Herlihy, [Richard K. Kim](#), and [Matthew M. Guest](#).

The Federal Reserve Board approved BB&T's application to acquire Susquehanna Bancshares earlier this week and set the stage for an August 1 closing— just over eight months from the date of announcement. The BB&T/Susquehanna transaction will be the largest U.S. bank merger in recent years to close within this timeframe. This acquisition follows closely after the timely approval of two other smaller acquisitions by BB&T, of Bank of Kentucky in June and of former Citibank branches in Texas in February. The series of promptly completed transactions reflects well on BB&T's M&A and regulatory approach and continues its long history of successful deal-making.

Also very recently, another successful and acquisitive bank, Sterling Bancorp, completed its acquisition of Hudson Valley Holding Corp. This transaction was transformative in taking Sterling above \$10 billion in assets— an important threshold for regulatory purposes which triggers requirements for annual stress tests, caps on debit card interchange fees and other new requirements. Again, the transaction was completed within 8 months of announcement and in line with market expectations, despite protests by community groups pursuant to the Community Reinvestment Act ("CRA").

Given the spate of bank mergers which have been subject to elongated approval processes, the timeliness of these recent approvals is a reassuring sign to the market that properly structured transactions by experienced acquirers can receive approval on a reasonable and predictable timeline. Just as importantly, these recent Federal Reserve orders contain new language that reflects a changing view of bank mergers. As reflected in the detailed analyses in the orders regarding CRA and consumer compliance, prospective bank holding company acquirers should generally expect more detailed probing in these areas by the Federal Reserve with less deference paid to findings by the subsidiary bank's primary regulators. The heightened focus on CRA means that community group protests are accorded a higher degree of scrutiny and can result in long delays. This underscores the advisability of maintaining cordial working relationships with community groups and putting in place a strong CRA program on an ongoing basis.

The approval orders also reflect an evolving approach to analyzing the impact of a bank merger on financial stability. In prior orders, the Federal Reserve had focused on five criteria: size, substitutability, interconnectedness, complexity and cross-border activity. While these factors are still relevant, the Federal Reserve now focuses on the "systemic footprint" of the combined

organization and the incremental effect of the transaction on that footprint and also looks at other quantitative and qualitative factors, such as the “opaqueness and complexity of an organization’s internal structure.” The Federal Reserve cited as positive factors in the BB&T/Susquehanna order that both parties are “predominately engaged in retail commercial banking activities” as well as the relatively minimal level of cross-border activities, critical services and interconnectedness, which sets a positive precedent for similar transactions by other large retail banks.

Beyond the language of the approval orders, the manner by which the Federal Reserve now processes bank merger applications has changed even more significantly. The Federal Reserve now expects highly detailed analyses of due diligence findings, including any identified weaknesses and plans for remediation. Also carefully considered during the application process are integration plans and post-merger compliance and risk management systems and programs. Federal Reserve staff also reviews and comments on the terms of the merger agreement, including the restrictiveness of the negative covenants. For bank holding companies over \$50 billion in assets or that would cross that level by virtue of an acquisition, the Federal Reserve will look carefully at the timing and implications of the annual CCAR stress tests.