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The Likely Impact of the Executive Order on Bank M&A

Last Friday, the White House issued an Executive Order and an accompanying Fact Sheet on "Promoting Competition in the American Economy" calling for 72 actions aimed at a broad swath of industries, including the banking industry. The Executive Order differs in substantive ways from the Fact Sheet, but because the Fact Sheet was released first, it has received more attention. The Fact Sheet notes that:

- Over the past four decades, the U.S. has lost 70% of its banks – many as a result of mergers and acquisitions;
- Communities of color are disproportionately affected by these closures;
- The federal agencies have not formally denied a bank merger application in more than 15 years;
- Excessive consolidation raises costs for consumers, restricts credit to small businesses and harms low-income communities;
- Branch closures can reduce small business lending and lead to higher interest rates; and
- Customers cannot easily take their financial transaction history data to a new bank, further impeding competition.

The Fact Sheet "encourages" the Department of Justice, Federal Reserve, Federal Deposit Insurance Corporation and Office of the Comptroller of the Currency to "update guidelines on banking mergers to provide more robust scrutiny of mergers." The Fact Sheet also encourages the Consumer Financial Protection Bureau to "issue rules allowing customers to download their banking data and take it with them."

The Executive Order is more muted and nuanced than the Fact Sheet. It notes at the outset that "consumers pay steep and often hidden fees because of industry consolidation." In order to "guard against excessive market power", the Attorney General in consultation with the banking agencies is "encouraged" to review "current practices" and adopt a plan not later than 180 days after the date of the order "for the revitalization of merger oversight under the Bank Merger Act and the Bank Holding Company Act of 1956." The Executive Order also encourages the Director of the CFPB to complete a rulemaking to "facilitate the portability of consumer financial transaction data so consumers can more easily switch financial institutions and use new, innovative financial products" and enforce existing legal prohibitions on “unfair, deceptive, or abusive acts or practices in consumer financial products or services.” Importantly, the Executive Order also notes that the review must be in accordance with the factors enumerated by existing law – the statutory standards remain unchanged.

Because the banking agencies are independent agencies, the Administration can only encourage and not compel them to take specific actions. Tellingly, the Department of Justice issued a statement also on Friday that it would “immediately begin implementing the interagency collaborations called for in the Executive Order”, while the banking agencies did not comment. It is too early to tell how impactful the Executive Order will be on bank M&A. Interagency collaborations tend to span many months and occasionally years. Once the DOJ and the banking agencies agree to and adopt a plan, if the agencies elect to issue new regulations, they must then undergo a lengthy process of publishing proposed regulations for public comment, considering the comments and then issuing final regulations. In doing so, they must square them with recent prior statements, such as Federal Reserve Governor Michelle Bowman’s public statement made just five months ago, that are inconsistent with the Executive Order. In her comments, she notes that the banking industry is growing more – not less competitive – as a result of technology and fintech companies and that the Federal Reserve’s antitrust framework at least as applied to community banks should be loosened:

> The Board's framework for banking antitrust analysis hasn't changed substantially over the past couple of decades. I believe we should consider revisions to that framework that would better reflect the competition that smaller banks face in an industry quickly being transformed by technology and non-bank financial companies. As part of this effort, we have engaged in conversations and received feedback from community banks about the Board’s competitive analysis framework and its impact on their business strategies and long-term growth plans. We are in the process of reviewing our approach, and we are specifically considering the unique market dynamics faced by small community banks in rural and underserved areas.

More recently, the Federal Reserve Board unanimously approved Huntington Bancshares’ merger with TCF Financial in May, the most recent large bank merger with antitrust-mandated divestitures. In its approval order, the Federal Reserve employed its traditional method of antitrust analysis. Notably, the transaction was also approved by Federal Reserve Board Governor Lael Brainard, a Democratic appointee who has abstained or voted against a number of recent large bank mergers.

The Federal Reserve will also have to justify imposing a more rigorous mode of antitrust analysis on an industry that has grown increasingly competitive and remains remarkably unconcentrated. In the U.S. banking industry, there are still over 5000 banks. Only three banks hold over 10% of nationwide deposits (with the highest at 11.5%) and all of them are barred by a statutory federal deposit cap from further bank acquisitions. Moreover, large fintech companies like Paypal, Square, Global Payments and Stripe all threaten to disintermediate banks as never before.

Given all of these procedural hurdles, an overhaul of the antitrust framework as applied to bank M&A is unlikely to be completed this year. At the same time, a change in tone at the regulatory agencies can be highly impactful even with no change in regulation. The Federal Reserve's extended review of M&T's acquisition of Hudson City Bancorp spanned three years – from 2012 to 2015. Now widely viewed as a flawed process, the extended timeframe had a chilling effect on bank M&A for a considerable amount of time.

Also of more immediate concern is the impact of the Executive Order on the DOJ. While the Executive Order calls for the DOJ to collaborate with the banking agencies, the DOJ acting alone can block a bank merger. While the DOJ does not have the authority to approve or deny a bank merger, in our experience, the banking agencies will not approve a transaction unless and until the DOJ is signed off. As we previously noted, in the Huntington/TCF transaction, the DOJ made several changes to its approach in reviewing the transaction. The net effect was to seemingly expand the DOJ's focus from antitrust to assessing the broader community impact of the transaction.

Accordingly, in our view, the competitive standards relating to bank mergers are not likely to change in the near-term and the regulatory approval process remains favorable at this time. However, there is a risk of arbitrary action by the DOJ or, less likely, by the banking agencies to send a message to the banking industry. We believe that this effectively raises the bar on the quality and thoroughness of the pre-signing regulatory consultations and the regulatory applications filed in connection with bank merger transactions.

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