EBBING THE TIDE OF LOCAL BANK CONCENTRATION: GRANTING SOLE AUTHORITY TO THE DEPARTMENT OF JUSTICE TO REVIEW THE COMPETITIVE EFFECTS OF BANK MERGERS

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The [G]reat [M]onopoly in this country is the money monopoly . . . . A great individual nation is controlled by its system of credit. Our system of credit is concentrated. The growth of the nation . . . and all our activities are in the hands of a few men . . . who, necessarily, . . . chill and check and destroy genuine economic freedom. This is the greatest question of all . . . .[1]

CONTENTS

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1. Woodrow Wilson, riding the populist wave championing monetary reform, spoke these words during his 1912 presidential campaign. *See* RICHARD SCOTT CARNELL ET AL., THE LAW OF BANKING AND FINANCIAL INSTITUTIONS 13 (4th ed. 2009).

INTRODUCTION

Take a trip back: the year is 1991, and First Hawaiian, Inc., Honolulu, Hawaii ("Applicant") has applied for Federal Reserve Board ("Fed") approval to acquire First Interstate of Hawaii, Inc., Honolulu, Hawaii, ("FIH") which owns a bank as one of its subsidiaries.[2] The Fed, instructed by statute to determine whether a particular transaction is likely to lessen competition, notes first that the Applicant is the second largest commercial banking organization in Hawaii, and that FIH is the fourth largest commercial banking organization in Hawaii.[3] Further, after consummation of the transaction, the Applicant would control 37.3% of the total deposits in commercial banking organizations in Hawaii.[4] Upon first blush, one would assume that the Fed would be hesitant to approve the transaction, given that the Applicant would occupy an even more dominant position in the Hawaiian commercial banking market. But the Fed, much to the chagrin of the United States Department of Justice's Antitrust Division ("DOJ"), approves the transaction, concluding that the proposed acquisition would not have "a substantially anticompetitive effect in any relevant market."[5]

Now flash forward to the present day. The United States has suffered through an economic collapse that required multiple bank bailouts, including $700 billion under the Troubled Assets Relief Program (TARP).[6] All told, the Fed lent $2 trillion to shore up banks,[7] with much of the money going towards bailing out America's largest banks, such as Bank of America[8] and Citigroup.[9] Although the causes of the crisis are numerous,[10] there is no denying that regulators

2. *See* First Hawaiian, Inc., Honolulu, Hawaii, 77 Fed. Res. Bull. 52, 52 (1991).

3. *Id.* at 54.

4. *Id.*

5. *Id.* at 57.

6. *See* Alex Johnson, *Bush Signs $700 Billion Financial Bailout Bill*, MSNBC.COM (Oct. 3, 2008), http://www.msnbc.msn.com/id/26987291/.

7. *See* Alan Feuer, *Battle Over the Bailout*, N.Y. TIMES, Feb. 14, 2010, at MB1.

8. Bank of America received a $20 billion bailout and a government guarantee for almost $100 billion of potential losses on toxic assets through an individual rescue plan, in addition to the $25 billion it received under TARP. *See* Patrick Rucker & Jonathan Stempel, *Bank of America Gets Big Government Bailouts*, REUTERS.COM (Jan. 16, 2009), http://www.reuters.com/article/idUSTRE50F1Q720090116.

9. Citigroup received guarantees on losses of its pool of approximately $306 billion in troubled assets, along with $45 billion in capital. *See* David Enrich et al., *U.S. Agrees to Rescue Struggling Citigroup*, WALL STREET J., Nov. 24, 2008, at A1.

10. For an overview of the causes of the financial crisis, *see generally* Kenneth E. Scott, *The Financial Crisis: Causes and Lessons*, 22 J. APPLIED CORP. FIN. 8 (Dec. 10, 2009), *available at* http://ssrn.com/abstract=1521610; *see also* Sheila C. Bair, Chairman, FDIC, Causes and Current State of the Financial Crisis Before the Financial Crisis Inquiry

"pumped tens of billions of dollars into the nation's leading financial institutions because the banks were so big that officials feared their failure would ruin the entire financial system."[11] After the financial collapse, the public and policymakers alike heaped much scorn upon banks that had become "too big to fail." But another pressing concern rose from the ashes of the fallout of the financial crisis: increasing levels of bank concentration in small, local markets and the dangers such concentration presents.

Banks in localized, small markets have sought out consolidation with equal vigor as the titans of the industry, and for good reason. Empirical analysis demonstrates that as concentration among local markets increases, the banks operating in those markets have increased profit rates, can pay lower interest rates on deposits, and can charge higher interest rates on loans.[12] This has a particularly potent effect on small businesses that rely primarily on local banks for their credit needs.[13] Yet under the current banking regulators' antitrust analysis, lending to small- and medium-sized businesses as a distinct submarket is ignored, which presents opportunities for local banks, such as those involved in First Hawaiian, to exploit their increased market power, or, at the very minimum, to continue to seek consolidation in hopes of obtaining a monopoly over local markets.

This Article argues that the DOJ, rather than the banking regulators, such as the Fed, the Office of the Comptroller of the Currency (OCC), and the Federal Deposit Insurance Corporation (FDIC), should be given the sole power to review the competitive effects of bank mergers to minimize the dangers of continued local bank concentration. Although we will never know the extent to which bank consolidation could have been prevented, it is clear that mergers such as First Hawaiian Inc., Honolulu, Hawaii would have come out differently under DOJ review. Section I of this Article explores America's long storied fear—shared by the public and policymakers alike—of concentration among industries, particularly that of the banking

Commission (Jan. 14, 2010), *available at* http://www.fdic.gov/news/news/speeches/spjan1410.html.

11. *See* David Cho, *Banks 'Too Big to Fail' Have Grown Even Bigger*, WASH. POST, Aug. 28, 2009, at A01.

12. *See generally* R. ALTON GILBERT & ADAM M. ZARETSKY, THE FEDERAL RESERVE BANK OF ST. LOUIS, BANKING ANTITRUST: ARE THE ASSUMPTIONS STILL VALID? (2003), *available at* http://research.stlouisfed.org/publications/review/03/11/gilbert.pdf.

13. *See generally* Robert DeYoung et al., *Youth, Adolescence, and Maturity of Banks: Credit Availability to Small Business in an Era of Banking Consolidation*, 23 J. BANKING & FIN. 463 (1999), *available at* http://research.stlouisfed.org/publications/review/03/11/gilbert.pdf.

industry. Section II describes the laws governing bank mergers that grew out of this fear of concentration, and details the reemergence of concentration in the banking industry. Section III begins with a look at how the bank merger process works and then proceeds to explain why the DOJ should be the agency responsible for reviewing the competitive effects of bank mergers. Finally, Section IV contemplates and responds to potential counterarguments.

I. A LOOK INTO THE PAST: WHY BANK MERGERS ARE "UNIQUE"

Before delving into the history of America's fascination with and trepidation of bank concentration, whether by merger or otherwise, it is important to note that fears about concentration have long lingered in the American consciousness. Indeed, much of American antitrust law is rooted in the conviction that the concentration of economic power and resources among fewer and fewer businesses is an evil that requires strong government intervention. Part A of this Section briefly explores this conviction that gave birth to a variety of antitrust measures designed to reign in the evils of concentration. Part B details historical American attitudes toward bank concentration to demonstrate why the laws governing bank mergers differ from general antitrust legislation.

A. Concentration as Conflagration: General Historical Perspective

The Sherman Antitrust Act of 1890 ("Sherman Act"),[14] America's first foray into the field of antitrust legislation, was in part a response to the rapid rise of big business. Justice Harlan in his concurrence in *Standard Oil Co. v. United States*[15] described the state of mind of the American people at the time:

> [T]here was everywhere, among the people generally, a deep feeling of unrest. The nation had been rid of human slavery—fortunately, as all now feel,—but the conviction was universal that the country was in real danger from another kind of slavery sought to be fastened on the American people; namely, the slavery that would result from aggregations of capital in the hands of a few individuals and

14. Sherman Antitrust Act of 1890, 15 U.S.C §§ 1-7 (2006). The Sherman Act, however, was ill-equipped to deal with corporate mergers, a fact not lost on the sponsors of the Clayton Bill designed to address that very problem. *See* Scott A. Sher, *Closed But Not Forgotten: Government Review of Consummated Mergers Under Section 7 of the Clayton Act*, 45 SANTA CLARA L. REV. 41, 46-47 (2004) (quoting Senator Barkley, a primary proponent of the Clayton Act, as to the need for its passage) ("[N]otwithstanding that law (the Sherman Act) has been in force for 24 years, combinations, trusts, and monopolies have increased at a marvelous rate and have grown so enormous in size as almost to stagger with bewilderment and confusion the mind that undertakes to contemplate or unravel them.").

15. 221 U.S. 1 (1911).

> corporations controlling, for their own profit and advantage exclusively, the entire business of the country, including the production and sale of the necessaries of life. Such a danger was thought to be then imminent, and all felt that it must be met firmly and by such statutory regulations as would adequately protect the people against oppression and wrong. Congress therefore took up the matter and gave the whole subject the fullest consideration . . . . Its authority to regulate such commerce [among the several states] was and is paramount, due force being given to other provisions of the fundamental law, devised by the fathers for the safety of the government and for the protection and security of the essential rights inhering in life, liberty, and property.[16]

Later legislation would continue to echo these sentiments in attempting to decelerate concentration among American businesses. For example, the 1950 amendments to the Clayton Act[17] were grounded in the "fear of what was considered to be a rising tide of economic concentration" and bolstered by statistics that demonstrated the "danger to the American economy [of] unchecked corporate expansions through mergers."[18]

Those supporting such legislation were fearful that increasing concentration had "corrupted the American way of life."[19] Senator Thompson, a primary sponsor of the Clayton Act, summarized the severity of the problem:

> Neither at birth, in life, nor at death are we free from trusts. We are welcomed into the world by the Milk Trust and rocked in a cradle built by the Furniture Trust. As we proceed through life we find practically everything we eat and everything we wear furnished by a trust and nearly every business in which we may wish to engage completely monopolized; and at last, as we approach death, we are brought face to face with the Coffin Trust, by which we are finally conveyed to our last resting place.[20]

Given that concentration in general raised such fervor, it is unsurprising

16. *Id.* at 83-84 (Harlan, J., concurring in part and dissenting in part); *see also* United States v. Aluminum Co. of Am., 148 F.2d 416, 428 (2d Cir. 1945) ("In the debates in Congress Senator Sherman himself . . . showed that among the purposes of Congress in 1890 was a desire to put an end to great aggregations of capital because of the helplessness of the individual before them.").

17. Celler-Kefauver Amendments, Pub. L. No. 81-899, 64 Stat. 1125 (1950) (current version at 15 U.S.C. § 18 (2006)).

18. *See* Brown Shoe Co. v. United States, 370 U.S. 294, 315 (1962).

19. *See* Sher, *supra* note 14, at 47.

20. 51 CONG. REC. 14200, 14222 (daily ed. Aug. 25, 1914) (statement of Sen. William Howard Thompson).

that concentration in the banking industry took on extra significance. Since America's inception, politicians have waged a "war" against bank concentration and designed special rules above and beyond that of general antitrust legislation, all in an effort to prevent the development of bank trusts that would have a stranglehold on credit.

B. Historical Attitudes Toward Bank Concentration

Americans have long been wary of what has been described as the "Wall Street 'Money Trust,'" the concentration of credit among private financiers and bankers.[21] The seeds of this fear were sown shortly after American Independence when the first incorporated bank in the United States—the Bank of North America—had its charter repealed over claims that its exclusive banking privileges "would confer 'enormous wealth' on BNA's stockholders and 'produce a degree of influence and power which [cannot] be entrusted in the hands of any set of men whatsoever without endangering the public safety.'"[22]

This distrust manifested itself throughout the country's early years. The creation of the First Bank of the United States met with heavy resistance from Thomas Jefferson and James Madison, who argued that the First Bank would create a dangerous financial monopoly.[23] Similar arguments were made against establishment of the Second Bank of the United States, with President Jackson exclaiming that the Second Bank was "'dangerous to the liberties of the people,' because it made possible 'a concentration of power in the hands of a few men irresponsible to the people.'"[24]

As the United States grew out of its infancy, there were more and more clashes between banks seeking to expand their reach and those who fought in opposition. Each time the legislature was called upon to vote on a proposal that might increase concentration, it would be met with hostility by the banking regulators and congressmen catering to their constituents.[25] The constant tug-of-war was fueled in large part by the belief that the banking system and its unique attributes merit additional regulation because:

> The banking system is affected with the public interest to a much

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21. *See* CARNELL ET AL., *supra* note 1, at 12.

22. *See* Arthur E. Wilmarth, Jr., *Too Big to Fail, Too Few to Serve? The Potential Risks of Nationwide Banks*, 77 IOWA L. REV. 957, 969 (1992).

23. *Id.* at 970.

24. *Id.* at 971.

25. *See* J. Alfred Broaddus, Jr., *The Bank Merger Wave: Causes and Consequences*, 84 ECON. Q. 1, 2-3 (1998).

> greater extent than most industries. On the national level, the banking system is an important influence upon the money supply, and sharp fluctuations in the money supply can have serious adverse effects on the economy. On the local level, the individual bank has a much more important role than the individual firm in most other industries. Failure of a bank . . . may have a serious impact on the entire economy of its trade area if the bank is of significant size.[26]

Although the United States has changed greatly from its yesteryears, the same fears of financial industry concentration still linger. The financial crisis has reinvigorated the debate of how best to control bank concentration and renewed scrutiny of the laws and agencies responsible for preventing such concentration before it becomes a problem.

II. THE RISING TIDE OF CONCENTRATION

Congress has passed a variety of statutes to combat concentration among American industries, and it has given a number of different agencies the power to enforce them. Although an in-depth review of those statutes and the accompanying regulators is beyond the scope of this Article, it is instructive to provide a general outline of the laws that govern bank mergers. Part A of this Section sketches an overview of the relevant statutes that apply to bank mergers. Part B presents relevant statistics regarding the effectiveness of these laws, in order to demonstrate the need for regulatory overhaul.

A. Antitrust Statutes

"[There] can be no single, consistent sketch of the developments in banking law . . . . Only the perspective that comes when time provides the proper spacing will reveal whether the storm or the quiet was the theme of the picture, or whether it was all just a happening."[27]

The Sherman Act "forbids mergers effecting an unreasonable restraint of trade."[28] The Sherman Act, however, did little to counteract the explosion of trusts through mergers,[29] leading Congress to pass the Clayton Act in 1914. The Clayton Act "prohibited the acquisition by one corporation of the stock of another corporation when such acquisition would result in a substantial lessening of competition

26. *See* Tynan Smith & Nathaniel Greenspun, *Structural Limitations on Bank Competition*, 32 LAW & CONTEMP. PROBS. 40, 40 (1967).

27. John J. Brennan, *Developments in Banking Law—1964-1965*, 83 BANKING L.J. 189, 190 (1966).

28. United States v. Phila. Nat'l Bank, 374 U.S. 321, 354 (1963).

29. *See* Sher, *supra* note 14, at 47.

between the acquiring and the acquired companies, or tend to create a monopoly in any line of commerce."[30]

It too, though, had its deficiencies as it failed to reach acquisitions by one corporation of another's assets. Thus, in 1950, the Cellar-Kefauver Act amended and broadened the Clayton Act, removing the "artificial distinction between acquisitions of assets and acquisitions of stock."[31] Its purpose was to remove the perception that there was a "rising tide of economic concentration in the American economy [and] . . . that increased economic concentration might threaten other fundamental values of a non-economic nature."[32] Yet even after promulgation of the Cellar-Kefauver Act, banking concentration remained a problem. Congress felt that the Sherman Act had "little practical effect in the banking field."[33] The Clayton Act was similarly ineffective because banks rarely effectuated mergers through the purchase of shares, and the language of the Clayton Act relating to acquisitions of assets was inapplicable to banks (as understood at the time).[34] Therefore, in response to the "apparently accelerating trend

30. Brown Shoe Co. v. United States, 370 U.S. 294, 312-13 (1962). The Clayton Act stated:

> No person shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no person subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of one or more persons engaged in commerce or in any activity affecting commerce, where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition, of such stocks or assets, or of the use of such stock by the voting or granting of proxies or otherwise, may be substantially to lessen competition, or to tend to create a monopoly.

15 U.S.C. § 18 (2006).

31. Thomas B. Leary, *The Essential Stability of Merger Policy in the United States*, 70 ANTITRUST L.J. 105, 107 (2002).

32. *See* Edward Pekarek & Michela Huth, *Bank Merger Reform Takes An Extended Philadelphia National Bank Holiday*, 13 FORDHAM J. CORP. & FIN. L. 595, 612 (2008).

33. *See* Carl W. Funk, *Antitrust Legislation Affecting Bank Mergers*, 75 BANKING L.J. 369, 370 (1958). The Sherman Act was considered to be of limited use for a number of reasons:

> It is generally considered necessary, in order to show that the Sherman Act has been violated, to prove that a merger has actually had or will actually have the effect of restraining competition or creating a monopoly. The practical difficulties of undoing a consummated bank merger are in themselves sufficiently great so that it seems unlikely that the Sherman Act will be invoked.

Id.

34. *Id.* at 370-71. At the time, banks were thought to be not subject to the Clayton Act's limitations on acquisitions of assets for the following reason:

> The remainder of each sentence, relating to the acquisition of assets, is limited to corporations subject to the jurisdiction of the Federal Trade Commission. Under section 11 of the Clayton Act, 15 U.S.C. 21, banks are subject to the jurisdiction of the Board of Governors of the Federal Reserve System, and banks are likewise expressly excepted from sections 5 and 6 of the Federal Trade Commission Act, 15 U.S.C. 45, 46. Hence, this

toward concentration in the commercial banking system . . . a trend which existing laws were evidently ill-suited to control,"[35] Congress passed the Bank Merger Act of 1960 ("Bank Merger Act").[36]

At their heart, the Bank Merger Act and the Clayton Act do not differ much because both prohibit a merger or acquisition that "would result in a monopoly . . . or whose effect . . . may be to substantially . . . lessen competition."[37] The Bank Merger Act, however, has a few additional wrinkles. The banking regulators, before giving approval to a transaction, are to assess a variety of fact-specific factors, including:

> The financial history and condition of each of the banks involved, the adequacy of its capital structure, its future earnings prospects, the general character of its management, the convenience and needs of the community to be served, whether the bank's corporate powers are consistent with the purposes of the Federal Deposit Insurance Act, and the effect of the transaction on competition (including any tendency toward monopoly).[38]

Ultimately, the banking regulator may only approve a transaction if its "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."[39] This public interest exception is entirely unique to the bank merger context and has no counterpart in the general antitrust laws.

B. What's the Big Deal? Concentration Run Amok

The banking industry has undergone a dramatic transformation over the past three decades, with the number of banks dwindling each year. The statistics are staggering: for example, "[b]etween 1985 and

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prohibition does not apply to them.

Id. at 371. This apparent loophole in the statute was later closed by the ruling in *United States v. Philadelphia National Bank*, which brought bank mergers within the reach of Section 7 of the Clayton Act.

35. United States v. Phila. Nat'l Bank, 374 U.S. 321, 373 (1963) (Harlan, J., dissenting) (internal citations omitted).

36. 12 U.S.C. § 1828 (2006).

37. Terry Calvani, *Antitrust Analysis of Bank Mergers: A Survey of Recent Developments*, FINDLAW.COM, http://library.findlaw.com/1996/Dec/1/129882.html (last visited Feb. 2, 2012). This clause of the Bank Merger Act is known as the maintaining competition rule. The Bank Merger Act contains an additional substantive antitrust rule that may rightfully be called the anti-monopolization rule because it "proscribes any transaction that would 'result in a monopoly' or further 'any combination or conspiracy to monopolize or to attempt to monopolize the business of banking in any part of the United States.'" *See* CARNELL ET AL., *supra* note 1, at 205.

38. H.R. REP. NO. 86-1416 (1960), *reprinted in* 1960 U.S.C.C.A.N. 1995.

39. *See* CARNELL ET AL., *supra* note 1, at 205.

1991, more than 4000 mergers occurred among U.S. commercial banks, a rate of consolidation more than four times greater than in previous decades."[40] In this six-year period alone, "consolidation transferred control of more than $350 billion in financial assets from small acquired banking institutions to the 100 largest U.S. depository institutions."[41] This six-year stretch was no mere anomaly: during the period between 1980 and 2003, the number of banks went from 16,000 to approximately 8000.[42] The number of bank mergers increased rapidly as the 1990s saw an average of over 500 bank mergers annually, up from approximately 345 per year during the 1980s.[43]

Smaller banking institutions have been particularly susceptible to merger activity; "nearly all of the decline [in the number of banking and thrift organizations] occurred in the community bank sector (organizations with less than $1 billion in assets in 2002 dollars), and especially among the smallest size group (less than $100 million in assets in 2002 dollars)."[44] That is not to say that bank concentration levels, whether measured on a national or local scale, have reached the point "where monopolistic behavior might manifest itself."[45] Rather, it indicates that, "although MSA (metropolitan statistical area) market concentration remains fairly low on average, it has nonetheless increased substantially since 1984."[46] The question then becomes how to prevent concentration levels, especially those in small, local markets, from reaching the point where monopolies begin to surface, and the answer involves shifting the responsibility for analyzing the anticompetitive effects of bank mergers to the DOJ.

III. THE SOLUTION: A LITTLE CHANGE GOES A LONG WAY

It is necessary to understand the current dynamic between the DOJ and the banking regulators in reviewing bank mergers to establish what needs to be changed. Part A of this Section describes the procedural aspects of the bank merger process and the Bank Merger Guidelines that govern the current analysis. Part B discusses how the agencies differ in their analysis and delineates a proposal for reform.

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40. *See* Sherrill Shaffer, *Bank Competition in Concentrated Markets*, BUS. REV., at 3 (1994).

41. *Id.*

42. *See* Pekarek & Huth, *supra* note 32, at 604.

43. *Id.*

44. *See* Kenneth D. Jones & Tim Critchfield, *Consolidation in the U.S. Banking Industry: Is the "Long, Strange Trip" About to End?*, 17 FDIC BANKING REV.31, 36 (2005).

45. *Id.*

46. *Id.*

A. An Unhealthy Accord

The process involved in approving a bank merger differs from that of mergers in other contexts because the DOJ shares jurisdiction with the banking regulators.[47] When a bank seeks consolidation through merger, it must first file for approval with the appropriate banking regulator: "for national banks—the OCC; for state member banks and holding company transactions—the [Fed]; and for nonmember insured banks—the FDIC."[48] Upon receiving the application, the regulator forwards it to the DOJ and both the regulator involved and the DOJ analyze the competitive effects of the proposed transaction concurrently.[49]

The two agencies, however, utilize different statutory standards, as the DOJ applies the standards set forth under Section 7 of the Clayton Act while the banking regulator is guided by the Bank Merger Act.[50] Normally, the banking regulator will wait until the DOJ has submitted a report with its findings regarding the likely competitive effects of a transaction before the banking regulator makes its decision whether to grant approval for the merger.[51]

As the starting point for the analysis, both agencies look to the Bank Merger Guidelines, which were developed by the DOJ, the Fed, and the OCC.[52] The Bank Merger Guidelines were an effort by the relevant authorities to provide a framework to allow the merging parties to assess the information needed to support their application for approval of their merger.[53] Section 1 of the Bank Merger Guidelines contain a list of quantitative information that the agencies will consider, along with two separate screens for analyzing the transaction, Screens A and B.[54] Section 2 lists types of qualitative information that "may be

47. Jonathan M. Rich & Thomas G. Scriven, *Bank Consolidation Caused By The Financial Crisis: How Should the Antitrust Division Review "Shotgun Marriages"?*, ANTITRUSTSOURCE.COM 1 (Dec. 2008), http://www.americanbar.org/content/dam/aba/publishing/antitrust_source/Dec08_Rich12_22f.authcheckdam.pdf.

48. Calvani, *supra* note 37.

49. Rich & Scriven, *supra* note 47, at 2. This represents a drastic change from the past, when the Fed might very well have made a formal decision without waiting for the DOJ's input. *See* Calvani, *supra* note 37.

50. As discussed in Part II.A *supra*, the Bank Merger Act and Section 7 of the Clayton Act both ask whether the merger or acquisition will substantially lessen competition, yet the Bank Merger Act requires the regulator to also consider additional factors, such as the public interest and the future prospects of the institution, before approving the transaction.

51. Rich & Scriven, *supra* note 47, at 2.

52. *Id.*

53. *See* CARNELL ET AL., *supra* note 1, at 238.

54. Calvani, *supra* note 37.

relevant to the banking agencies and DOJ when the quantitative results from Screen A and/or B signal potential antitrust concerns."[55]

Upon filing for approval, the merging party must complete a Screen A Herfindahl-Hirschman Index (HHI)[56] calculation chart for three separate geographic markets: the FED Board ("FRB") market,[57] the Ranally Metro Area (RMA) market,[58] and the county market.[59] Both the banking regulator and the DOJ employ what is known as the 1800/200 test for Screen A, but differ in how they proceed after using it. The banking regulator applies the test to deposits, "if, with respect to deposits, a transaction does not cause the [HHI] to exceed 1800 and to increase more than 200 points in any relevant banking market, the Fed is unlikely to challenge the transaction."[60] Further, under Screen A, fifty percent of all thrifts' deposits are included when calculating the HHI.[61] Regardless of whether or not the potential merger raises red flags under Screen A, the banking regulator will not use Screen B.[62] Instead, the banking regulator will proceed to analyze the transaction under Section 2 of the Bank Merger Guidelines, focusing on the qualitative factors listed in that Section.[63] This may seem strange if one believes that the Bank Merger Guidelines represent "an accord on the substance of antitrust analysis."[64] Yet the Bank Merger Guidelines were merely designed to provide transparency to the merger parties and were not meant to unify the antitrust analysis of the DOJ and banking

55. *Id.*

56. The index is a commonly accepted measure of market concentration, calculated by squaring the market share of each firm competing in a market and then summing the result numbers. *See The Herfindahl-Hirschman Index*, DEP'T OF JUST., http://www.justice.gov/atr/public/testimony/hhi.htm (last visited Feb. 2, 2012).

57. The general definition of an FRB market is difficult, if not impossible, to articulate due in large part to the fact that each Federal Reserve Bank defines an FRB market differently. For more information on how each Federal Reserve Bank defines its respective FRB market, *see generally* James V. Disalvo, *Federal Reserve Geographic Banking Market Definitions*, FED. RESERVE BANK OF PHILA. (1999), *available at* http://www.philadelphiafed.org/research-and-data/banking/third-district-markets/banking-market-definitions.pdf

58. RMAs are defined by the Rand McNally Corporation "using commuting and population density data at the subcounty level." *Id.* at 3. Three criteria must be met before a market is designated as an RMA: "1) an urbanized area with a population of approximately 50,000, 2) a population density of at least 70 per square mile, and 3) commutation of at least 20 percent of the labor force to the central urban area." *Id.*

59. Calvani, *supra* note 37.

60. Rich & Scriven, *supra* note 47, at 2.

61. Calvani, *supra* note 37.

62. *See id.*

63. *See id.*

64. *See* CARNELL ET AL., *supra* note 1, at 238.

regulators.[65]

The DOJ uses Screen A only as a starting point for the analysis and will often times utilize Screen B as a secondary means of analysis.[66] First, if the transaction exceeds the 1800/200 threshold of Screen A, the DOJ encourages the applicant to "consider submitting the calculations set forth in Screen B."[67] Screen B has alternative definitions of the geographic market that differ from the banking regulators and "looks only to offices that make commercial loans in the relevant market."[68]

Even if the proposed transaction does not exceed the Screen A threshold, the DOJ may choose to further scrutinize the transaction under Screen B. This occurs most often "when Screen A does not reflect fully the competitive effects of the transaction in all relevant markets, in particular lending to small and medium sized businesses."[69] For example, the DOJ is "more likely to review a transaction if the predefined market in which the applicants compete is significantly larger than the area in which small business lending competition may exist."[70]

As demonstrated, the DOJ and banking regulators' antitrust analysis differs quite drastically because of the DOJ's use of Screen B under the Bank Merger Guidelines. Screen B analyzes the product and geographic markets in an entirely different way from that of the banking regulators. This difference lies at the root of what may be a relevant factor in the increased concentration in local markets and is the impetus for overhauling the current system.

B. Revamping the Bank Merger Review Hierarchy

The DOJ's analysis of the geographic and product markets in a banking merger represents a more nuanced understanding of competition in the banking industry, yet it does not receive due attention in the overall analysis because of the DOJ's status as a "junior partner in the government's bank merger review process."[71] The solution is to turn the system on its head and make the DOJ the agency responsible for performing the competitive analysis of bank mergers.

Under the new system, the DOJ and the banking regulatory would

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65. *Id.* at 237-38.
66. *Id.* at 237.
67. *Id.*
68. *Id.*
69. *See* CARNELL ET AL., *supra* note 1, at 237.
70. *Id.*
71. *See* Leiv Blad & Jon Roellke, *Antitrust Mistrust*, THE DEAL MAG., (Jan. 22, 2010) http://www.thedeal.com/magazine/2010/01/antitrust_mistrust/print/.

still maintain "dual, independent authority to review [bank] mergers."[72] The DOJ would review the merger utilizing the statutory standards under the Clayton Act and the more detailed provisions it currently employs under the Bank Merger Guidelines.[73] Meanwhile, the banking regulator would review the merger solely under the public interest standard of the Bank Merger Act.[74] Most importantly, the DOJ's conclusions as to the competition issues would bind the banking regulators, "with preclusive effect on the economic competition portion of the [banking regulator's] public interest determination."[75] The result would be that the banking regulator could prohibit, allow, or impose conditions on a merger based on public interest considerations, but it "would have to articulate clearly and with sufficient basis why those public interest considerations outweigh the antitrust agency's conclusion regarding competitive effects."[76] This solution may seem slight in its breadth, but its effects are far-reaching.

Currently, the banking regulators rely on outdated definitions of the product and geographic markets. The Fed utilizes a traditional approach, otherwise known as the cluster method, that defines the relevant product market as the "cluster of products (various kinds of credit) and services (such as checking accounts and trust administration) denoted by the term 'commercial banking.'"[77] The FDIC takes an even broader view:

> The FDIC will view the relevant product market as consisting of those particular banking services offered by the merging institutions or to be offered by the combined institution and the functional equivalent of such services offered by other types of competitors, including, . . . other depository institutions securities firms, finance companies, etc. For example, . . . [NOW] accounts offered by savings institutions are in many respects the functional equivalent of demand deposit checking accounts. Similarly, captive finance companies of automobile manufacturers may compete directly with banks for automobile loans and mortgage bankers may compete directly for real

72. This solution is modeled after a proposal by the Antitrust Modernization Commission in a memo titled Supplemental Regulated Industries Discussion Memorandum—Merger Review in Regulated Industries 2 (July 21, 2006), *available at* http://govinfo.library.unt.edu/amc/pdf/meetings/Intl-FTAIASuppMemo060721circ.pdf .

73. *Id.* at 5.

74. *Id.* at 3.

75. *Id.*at 2-3.

76. *Id.*

77. *See* CARNELL ET AL., *supra* note 1, at 221. This approach stems from the decision in *United States v. Philadelphia National Bank*, 374 U.S. 321 (1963), defining the market as such.

estate loans.[78]

The banking regulators take an equally liberal approach towards defining the geographic market,[79] with the result being that they "might overlook significant concentrations in particular product lines and particular geographic areas."[80]

In comparison, the DOJ has "adopted [an] enlightened analytical model, one which is attuned to contemporary market variables, instead of a monolithic adherence to half-century old doctrine."[81] It uses a submarket or product-oriented approach when analyzing the product market and focuses on "transaction accounts and commercial lending to small and medium-sized business," which "increases the odds of finding some of those markets overly concentrated or in danger of becoming overly concentrated."[82] Further, the use of the submarket approach alters the analysis of the geographic market, confining it to the boundaries of the submarket.

Commentators have advocated for the DOJ's approach because it is supported both by theory and empirical evidence. As one commentator wrote: "[t]he cluster market method of product market definition obfuscates the partial, submarket nature of partial providers' competition with commercial banks" which "may mask significant concentrations in bank-dominated product markets by conflating them

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78. Federal Deposit Insurance Corporation, Notices, Statement of Policy; Bank Merger Transactions, 54 Fed. Reg. 39,043 (Sept. 22, 1989).

79. For example, the FDIC takes the following stance on the geographic market:

> The FDIC will view the relevant geographic market as consisting of those areas in which offices of the merging institutions are located and from which the institutions derive the predominant portion of their loan, deposit or other business and where existing and potential customers of the merging and resulting institutions may reasonably be expected to find alternative sources of banking services. Where practical, the geographic market will be defined in terms of political subdivisions to facilitate statistical analysis.

Id.

80. Tim McCarthy, *Refining Product Market Definition in the Antitrust Analysis of Bank Mergers*, 46 DUKE L.J. 865, 888 (1997).

81. Pekarek & Huth, *supra* note 32, at 646.

82. *See* CARNELL ET AL., *supra* note 1, at 227. Some have suggested that the market be broken down into even smaller "customer" segments, including: (1) the household segment, including markets for real estate loans, other secured loans, unsecured consumer credit, transaction accounts, non-negotiable deposits, and investment services; (2) the local business segment, involving long-term credit, short-term credit, transaction accounts, and long-term investments; (3) the regional business segment, involving these same basic business services plus short-term investment services for idle cash; and (4) the national business segment, involving the same basic services as the regional business segment minus short-term investment services which might be performed internally instead. *See generally* Note, *The Line of Commerce for Commercial Bank Mergers: A Product-Oriented Redefinition*, 96 HARV. L. REV. 907 (1983).

with relatively diluted concentrations in product markets in which non-depository partial providers are significant competitors."[83] The empirical evidence demonstrates that small business lending is primarily a local market as compared to other markets for banking services because "small businesses generally rely almost exclusively on local commercial banks for working capital, and use fewer financial institutions in general."[84]

All told, reforming the system and placing the responsibility for analyzing the competitive effects of bank mergers with the DOJ would allow for the DOJ's modernized and empirically-tested approach to rule the day. The proposal has significant backers: the Antitrust Modernization Commission recommended that "[f]or mergers in regulated industries, the relevant antitrust agency should perform the competition analysis" and "[t]he relevant regulatory authority should not re-do the competition analysis of the antitrust agency."[85] The banking regulators would still have a significant role in the process—they would still be responsible for approval of the parties' merger application, but their role in the merger analysis would be appropriately confined to public interest considerations. At the very least, heightened attention would be paid to localized markets, which would likely contribute towards preventing further concentration in those markets. Take, for instance, the First Hawaiian merger mentioned previously. The DOJ filed a report with the Fed that defined the relevant product market as commercial lending to small and medium-sized business[es], and relevant geographic market as the state of Hawaii.[86] Using these market definitions, the DOJ concluded that the HHI would increase 440 points to 2925 after consummation of the transaction and flagged the merger as anticompetitive.[87] Yet the Fed disregarded the DOJ's report and approved the transaction anyway. Under the new system, the transaction would not have been approved

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83. McCarthy, *supra* note 80, at 887-88.

84. *Id.* at 889. McCarthy goes on to note that:

> Competition from non-bank and non-depository institutions is much weaker in the small business lending submarket, especially with regard to unsecured small business credit, and debt securitization is not a viable option for small firms as it is for large ones. Thus, consumers of small business loans demand that product from a very limited geographic market, . . . even as they turn to institutions in a wider geographic area for other products and services, such as credit cards and equipment financing.

Id. at 889-90.

85. ANTITRUST MODERNIZATION COMMISSION, REPORT AND RECOMMENDATIONS 23 (Apr. 2007).

86. *See* CARNELL ET AL., *supra* note 1, at 241.

87. *Id.*

without more significant divestitures, thus preserving competition in what the DOJ felt would otherwise be a concentrated market.[88]

Although the new system would have its critics, it represents a step towards ensuring that concentration in the banking industry does not continue at the rate seen over the past few decades.

IV. COUNTERARGUMENTS

There are an abundant number of potential arguments against placing the competitive analysis of bank mergers solely in the hands of the DOJ, ranging from worries over regulatory capture to concerns about a lack of available resources. Although such reservations deserve independent review, this Section concentrates on three of the more persuasive arguments against changing the status quo, including: (1) the current system is functioning effectively; (2) bank mergers are no longer a pressing concern; and (3) the DOJ lacks the proper expertise to effectively review bank mergers.

A. If It Ain't Broke, Don't Fix It

Perhaps the strongest argument against giving the DOJ the sole authority to review the competitive effects of bank mergers is the idea that the system is not malfunctioning as it currently operates, thus there is nothing to fix. Proponents of this argument would point to the fact that domestic banks in the United States are still relatively small compared to their overseas competitors. Indeed, only one of the twenty largest banking companies is headquartered in the United States.[89] From this perspective, the bank mergers of the past three decades were merely a reaction by domestic banks to the size of their overseas brethren and were a market necessity. As explained by a former FTC commissioner, the acquisition trend could be explained by "[d]eregulation, competition, the desire to improve bank capital ratios, the S&L crisis, [and] a growing perception that we have too many

88. First Hawaiian is not the only instance where the DOJ has disagreed with a banking regulator's approval of a merger. Sometimes the DOJ is successful in exacting more divestitures than the banking regulator required. *See, e.g.*, United States v. Society Corp., No. 1:92CV 0525, 1992 WL 191096 (N.D. Ohio June 4, 1992); United States v. Fleet/Norstar Fin. Group, Inc., Civ. No. 91-0221-P, 1991 WL 299117 (D. Me. Dec. 3, 1991). Often times, however, the DOJ is unsuccessful in its attempt to block a banking regulator-approved merger or otherwise garner additional relief. *See, e.g.*, United States v. Cent. State Bank, 817 F.2d 22 (6th Cir. 1987), *aff'd* United States v. Cent. State Bank, 621 F. Supp. 1276 (W.D. Mich. 1985); United States v. First Nat'l State Bancorporation., 499 F. Supp. 793 (D.N.J. 1980); *see also* Rich & Scriven, *supra* note 47, at 3-4 ("The [DOJ] . . . has lost most of the merger cases that have gone to trial.").

89. Pekarek & Huth, *supra* note 32, at 605.

banks . . . ."[90]

Furthermore, supporters of this viewpoint stress that antitrust regulators in general do not (and did not) have the proper tools to combat the too big to fail phenomenon. In a hearing dedicated to the topic, Albert A. Foer, President of the American Antitrust Institute, testified that there exists no "workable antitrust mechanism for stopping large conglomerate mergers that create giant corporations without reducing competition in specific markets."[91] Further, antitrust legislation is too narrowly defined to "stop mergers on the basis of either the absolute size of the resulting institution or a calculation of the systemic consequences of their eventual failure."[92]

This perspective, however, ignores the reality that bank concentration is not limited strictly to America's largest banks, but rather has occurred with increasing frequency in local markets. As Mr. Foer himself notes, antitrust "has done a poor job of dealing with what might be called the 'lemming effect' where a particular merger can be predicted to set off a chain reaction of industry consolidation . . . ."[93] This consolidation certainly takes place at the periphery, where smaller banks—stricken by the "fear on the part of management of being acquired by a larger and/or more aggressive bank or becoming 'a bit player' in a field of giants"—merge with other banks with similar worries.[94]

In addition, statistics comparing the relative sizes of U.S. banks to their overseas counterparts fail to account for traditional domestic views towards bank concentration. It is one thing to say that U.S. banks are on average much smaller than foreign banks, but it is quite another to view bank concentration as a positive when much of the U.S. history is littered with statements and laws condemning such concentration.[95] Further, statistics show that bank concentration in local markets concerning local banks that do not compete internationally has increased.[96] It would be difficult to explain to local businesses, which

90. Calvani, *supra* note 37, at 2.

91. *'Too Big to Fail'?: The Role of Antitrust Law in Government-Funded Consolidation in the Banking Industry: Hearing Before the Subcomm. On Courts and Competition Policy of the H. Comm. on the Judiciary*, 111th Cong. 11 (2009) (statement of Albert A. Foer, President of the American Antitrust Institute).

92. *Id.*

93. *Id.*

94. John C. Soper, *What's Next for Consolidation in Banking?*, BUS. ECON., Apr. 2001, at 40.

95. *See supra* Part I.B.

96. *See supra* Part II.B.

predominantly take out loans from local markets,[97] that concentration (and reduced competition) in such markets is a necessity. The reality is that antitrust law is designed to preserve competition and promoting the DOJ to senior partner in bank merger competitive analysis would best serve the purpose behind the antitrust laws.

B. Bank Mergers: A Creature of the Past?

"The days of big bank mergers are gone. And it may be a long time before they ever come back."[98]

Another argument against upsetting the status quo rests on an entirely different premise: that bank merger activity is likely to be slow in the foreseeable future. There is evidence indicating that bank merger activity is currently at depressed levels and well off the highs set during the boom period of the 1990s and early 2000s. For example, as of late 2009, there was only approximately $56 billion in deals, down $16 billion from the previous year and over $63 billion from the highs set in 2000.[99]

The reasons behind the depressed merger levels, however, suggest that bank merger activity will accelerate just as quickly as it slowed. Banks have been leery about mergers because they "remain reluctant to trust what is on each other's books."[100] As one commentator put it: "[t]here is a significant hesitancy about buying something that is so beat up it infects the acquirer."[101] Yet bank merger activity is dependent upon the industry's health, and there are already signs that banks are on the mend. Bank earnings for the fiscal year 2009 exceeded that of the previous year by a healthy margin, with some banks recording record earnings.[102] Although there is disagreement as to how lasting the recovery will be,[103] it is clear that sustained earnings will lead to increased merger activity, thereby presenting the same merger issues as seen previously.

Moreover, there are those who believe that the financial crisis will ultimately increase merger activity, not because of an economic

97. *See supra* Part III.B.

98. David Ellis, *Big Banks in No Rush to Pair Up*, CNNMONEY.COM (Nov. 13, 2009, 3:40 AM), http://money.cnn.com/2009/11/13/news/companies/bank_deals/.

99. *Id.*

100. *Id.*

101. *Id.*

102. Douglas Mcintyre, *Bank Earnings Look Good, But Not For Long*, DAILYFINANCE.COM (Feb. 17, 2010), http://www.dailyfinance.com/story/bank-earnings-look-good-but-not-for-long/19361407/.

103. *Id.*

recovery, but rather because banks will need to "reorganize . . . for more capital, long-term financing, and access to goods, which generally occurs after a crisis—not during the crisis."[104] Industry insiders such as Jamie Dimon, Chairman and CEO of JPMorgan Chase, "expect[] the current market turmoil to unleash a wave of bank mergers" and that these mergers will be "big."[105] Dimon's claim is bolstered by the recent development of a cottage industry "that performs 'early triage' on behalf of prospective bank merger participants in order to improve the approval chances of related merger applications."[106]

The fact remains that bank merger activity, even if temporarily stunted, will likely hasten in the future, and that the accelerated pace may return sooner than expected. The problem of banking industry concentration seen over the past few decades will rear its head once again, necessitating a need for a change in the current banking merger regulatory hierarchy.

C. Does the DOJ Have the "Right Stuff" to Analyze Bank Mergers?

There are those who believe that giving the DOJ any additional authority in reviewing bank mergers would do more harm than good because the DOJ lacks the "expertise to properly analyze bank mergers."[107] Critics point to the fact that the DOJ in its antitrust analysis of bank mergers asks only whether the merged bank will have a dominant market share in deposits and lending within a particular geographic area.[108] This methodology, the argument goes, has "almost nothing to do with the too-big-to-fail problem" because "[i]t was not the size of a financial institution that cause the government to intervene, but its investments in particular credit instruments."[109]

Nonetheless, it is equally likely that banking regulators are ill-equipped to properly analyze whether a potential merger will have a substantial effect on competition. It has been argued that because banking regulators "have made market intervention a habit" and "place greatest value on soundness, the spirit of competition may be absent from their hearts, or may grow there in a distorted shape."[110]

This criticism also fails to account for the fact that although the

104. *See* Pekarek & Huth, *supra* note 32, at 605.
105. *Id.*
106. *Id.* at 610-11.
107. *See* Blad & Roellke, *supra* note 71.
108. *Id.*
109. *Id.*
110. Robert Charles Clark, *The Regulation of Financial Holding Companies*, 92 HARV. L. REV. 787, 837 (1979).

banking regulators may be more properly situated for preventing banks from becoming too big to fail, the proper tools for doing so lie outside of antitrust law.[111] Thus, the question is more accurately framed as which agency should have chief authority over the *competitive* analysis of banking mergers, and the DOJ has a much stronger claim based on its empirically-tested methodology.

CONCLUSION

Although much of the debate has emphasized banks that have grown too big to fail, far less attention has been paid to concerns about more localized bank concentration. Given our country's long distrust of concentration in the financial industry, it is surprising that banking regulators have become somewhat complacent towards bank mergers. Yet the statistics speak for themselves, as the last three decades have brought a wave of concentration unlike any seen previously in the banking industry. Something has to give, and the most palatable solution is to give the DOJ the responsibility for reviewing the competitive effects of a bank merger. As one commentator put it: "the best way of ensuring that ordinary antitrust rules and policies are applied to financial conglomerates is to let antitrust review of their actions be handled, as it ordinarily would be, by the [DOJ]."[112] It is time to return the banking regulators to their rightful position in the merger review hierarchy, where "they may function better if they specialize in their main job, insuring soundness."[113]

111. *See supra* Part IV.A.
112. Clark, *supra* note 110, at 837.
113. *Id.*