

UPDATES

U.S. Office of the Comptroller of the Currency Begins to Revamp Bank Merger Review Process

January 30, 2024

On January 29, the U.S. Office of the Comptroller of the Currency (OCC) proposed changes to its regulations for evaluating transactions under the Bank Merger Act (BMA) and adoption of a policy statement that outlines the principles and factors the OCC considers in reviewing applications for approval of transactions subject to the BMA (together, the Proposal). The Proposal was released in conjunction with a speech by Acting Comptroller Michael Hsu that makes valuable contributions to a discussion of the macro environment for the banking system in the United States and how bank merger-and-acquisition (M&A) activity and the associated regulatory process should relate to this broader context.

The Proposal follows a 2021 executive order regarding economic competition as well as a series of subsequent regulatory symposia, speeches, and requests for information regarding the BMA (and bank M&A more specifically). It is a critical early step in a larger interagency process to revisit the framework for evaluating bank M&A transactions, which is likely to have a meaningful impact on the bank M&A environment in the coming years.

The Proposal is open for comment for 60 days from the date it is published in the *Federal Register*.

Regulatory Changes

The Proposal includes two main changes to the OCC regulations implementing the BMA. First, it eliminates expedited review of certain applications, a procedure under which such applications are deemed approved 15 days after the end of the associated comment period (if the review period is not otherwise extended). The Proposal indicates that expedited review is inappropriate given the significance of the types of transactions reviewable under the BMA and that all such transactions should be adjudicated by the OCC rather than approved based on the passage of time. Second, the Proposal also eliminates the OCC's streamlined version of the BMA application, usable in certain specified transactions. The Proposal suggests this is being done for similar reasons — that the presence of a complete application would provide a fuller record for the OCC to review and adjudicate significant transactions and that the OCC could tailor the required information in its discretion if appropriate.

Policy Statement

The policy statement included in the Proposal is meant to provide greater clarity to financial institutions and the public regarding how the OCC will evaluate transactions subject to the BMA. Transactions subject to the BMA include bank mergers as well as certain kinds of asset purchases, such as the acquisition of substantially all of the assets and liabilities of another bank or the assumption of any deposit liabilities of another bank. Issues addressed by the policy statement include the general principles that the OCC will follow in reviewing BMA applications as well as how the OCC will analyze specific factors it is required by statute to address when reviewing an application. A number of these key issues addressed in the policy statement are outlined below.

- *General Principles of OCC Review:* The policy statement sets out 13 factors generally consistent with approvals of the corresponding transactions and six factors that would raise supervisory or regulatory concerns (and thus are inconsistent with approvals). No single factor is necessarily dispositive, although institutions should carefully evaluate each of these factors in considering potential transactions. The factors consistent with approvals are the following:

1. The acquirer is and the postmerger resulting institution will be well capitalized.
2. The resulting institution will have total assets less than \$50 billion.
3. The acquirer has a Community Reinvestment Act (CRA) rating of outstanding or satisfactory.
4. The acquirer has composite and management ratings of 1 or 2 under the Uniform Financial Institution Ratings System (UFIRS) or ROCA rating system.
5. The acquirer has a consumer compliance rating of 1 or 2 under the Uniform Interagency Consumer Compliance Rating System, if applicable.
6. The acquirer has no open formal or informal enforcement actions.
7. The acquirer has no open or pending fair lending actions, including referrals or notifications to other agencies.
8. The acquirer is effective in combatting money laundering activities.
9. The target's combined total assets are less than or equal to 50% of acquirer's total assets.
10. The target is an eligible depository institution (as defined by OCC regulation).
11. The proposed transaction clearly would not have a significant adverse effect on competition.
12. The OCC has not identified a significant legal or policy issue.
13. No adverse comment letter from the public has raised a significant CRA or consumer compliance concern.

The factors inconsistent with approvals are the following:

1. The acquirer has a CRA rating of "needs to improve" or substantial noncompliance;
2. the acquirer has a consumer compliance rating of 3 or worse;
3. the acquirer has UFIRS or ROCA composite or management ratings of 3 or worse, or the

most recent report of examination otherwise indicates that the acquirer is not financially sound or well managed;

4. the acquirer is a global systemically important banking organization (GSIB) or subsidiary thereof;
 5. the acquirer has open or pending Bank Secrecy Act/anti-money-laundering enforcement or fair lending actions, including referrals or notifications to other agencies; or
 6. the acquirer has failed to adopt, implement, and adhere to all the corrective actions required by a formal enforcement action in a timely manner, or multiple enforcement actions have been executed or are outstanding against the acquirer during a three-year period.
- *Financial Stability:* The BMA requires the OCC to consider the risk to the stability of the United States banking or financial system when reviewing an application. In doing so, the OCC will apply a balancing test, weighing different factors as well as the risk posed by both the approval or disapproval of the proposed transaction. Factors to be considered include the size of the resulting institution, the availability of alternatives following the transaction, the complexity of the resulting institution, the contagion risks posed by the resulting institution, and whether the resulting institution can be readily resolved in the event of distress.
 - *Financial and Managerial Resources and Future Prospects:* The BMA requires the OCC to consider the managerial resources, financial resources, and future prospects of the combining and the resulting institutions when reviewing an application. The OCC will consider relevant factors both independently as well as in concert, given their interrelation. These factors include the size, complexity, and risk profile of the combining and resulting institutions; the supervisory record of the acquirer; the adequacy of the resulting institution's capital, liquidity, management, and earnings prospects; and pertinent regulatory exam ratings and findings.
 - *Convenience and Needs:* The OCC considers the probable effects of a transaction subject to the BMA on the community to be served by the resulting institution. This includes looking at plans to close or consolidate branches or otherwise limit services, credit availability for different types of community needs (home loans, farm loans, etc.), changes in the institution's workforce, and community investment initiatives.
 - *Public Comments and Meetings:* Transactions subject to the BMA generally require a 30-day comment period following publication of the notice of the proposed transaction. While the BMA does not require the OCC to hold meetings or hearings, the OCC may elect to do so based on weighing the public's interest in the transaction with the value or harm of a public meeting to the decision-making process.

Three Key Takeaways

First, if adopted as proposed, the Proposal seems to make the environment for M&A involving nationally chartered banks and savings associations generally more favorable for community banks and smaller regional banks (under \$50 billion in total assets) but more challenging for GSIBs and their subsidiaries. Moreover, the Proposal could introduce greater complexity to the review of mergers of equals as compared to the acquisition by a larger institution of a clearly smaller one. However, under the Proposal,

no single factor (such as size) is necessarily dispositive. As such, all banks will still want to carefully evaluate each potential transaction before determining whether to proceed.

Second, Acting Comptroller Hsu's speech seems to divide potential transactions subject to BMA review into three general categories. The first category is those that are easy to approve because the depository institutions involved are model banks and the transaction has clear benefits. This means that the parties and the transaction tend to satisfy most or all of the 13 factors consistent with approvals and avoid the six factors that are inconsistent with approvals. The second category is those that seem to be especially challenging for a relatively clear reason or reasons, which are likely to result in greater scrutiny and a greater likelihood of disapproval. The third category is those banks that fall in neither of the prior two and thus are in the middle. Knowing which category a proposed transaction is likely to fit into will be essential to assessing both the likelihood and, importantly, the timing of needed regulatory approvals.

Third, the Proposal is an important step forward in greater transparency in the bank M&A environment. However, there is still a great deal of work to be done by the banking agencies and other government agencies with regard to the interagency review of the evaluation of bank M&A more generally. Given the OCC's jurisdiction, the Proposal cannot address either state-chartered banks or any bank holding companies. That said, the Proposal is still a significant step in amending the BMA framework and a hint of what is to come.

CONTACTS

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