FedFin Client Report

Wednesday, October 19, 2022

USB/MUFG Orders Point to New Merger, Regulatory Policy

Client Report: MERGER11

Executive Summary

As promised, this analysis focuses on the OCC and FRB approvals of the acquisition by U.S. Bancorp of MUFG's Union Bank in California. Derided in a tweet from Sen. Warren (D-MA) as another "rubber-stamp" approval, both the nature of the transaction – which included massive commitments to community support – and the approvals themselves suggest otherwise. We shall continue to evaluate agency action on larger transactions and shortly provide clients with an analysis of the FDIC/FRB advance notice of proposed rulemaking on new resolution standards approved for public comment by the FDIC (see *Client Report* **DEPOSITINSURANCE115**). However, while policy and politics formulate new standards, pending transactions are directly and immediately affected by the new approach epitomized in these orders. We thus note the financial-stability and resolvability conditions applied to this transaction, which clearly signal those – i.e., "severability" – for near-term deals as well as for future standards. Still, the Fed's findings paint a different picture of at least one super-regional saying noting that the combined bank "would not exhibit an organizational structure, complex interrelationships, or unique characteristics that would complicate resolution of the institution in the event of financial distress." We note also the consultations between both the Fed and OCC with the CFPB, suggesting that, at least with regard to consumer compliance, this agency plays some role in merger review despite Director Chopra's harsh words about the current "lax and opaque" process.

Analysis

Both the FRB and OCC orders had an extensive discussion of CRA. While critical to approval, it does not set new policy ground.

FRB

Key aspects of the FRB's approval that are not transaction-specific include:

- The company commits to be governed by Category II rules (see FSM Report **SIFI34**) by the earlier of when it crosses the $700 billion threshold or December 31, 2024 if the

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Board has told it by January 1 of that year to prepare it to do so. The Board expects to send this notice unless the combined bank persuades the Fed that its risk profile has or will shortly be reduced by, for example, a "material" asset-size reduction.

- Representations that Union Bank's parent company continue to do business with Russia were not deemed germane to any U.S. operations and thus to this approval.
- Representations that the merger would increase climate risk were rejected.
- The combined bank's activities do not create financial-stability risk by virtue of the largely-traditional composition (i.e., little short-term wholesale lending). Similarly, complexity is not found to be problematic, nor is the combined bank likely to be highly inter-connected.

OCC

Key aspects of the OCC's conditional approval include:

- The importance accorded to testimony at the merger hearing was emphasized in both the approval and statement releasing it.
- The approval also emphasizes the importance to the OCC of findings that mortgage-lending decisions do not correlate with key demographics, but the agency was persuaded by the bank's record and its decision associated with the acquisition to offer new products such as down payment assistance.
- The OCC accepts USB's defense of its overdraft-fee practices despite the CFPB's likely objection to them.
- For the first time of which we are aware at the OCC and despite the Fed's finding, a regional-bank transaction is found to threaten financial stability. The OCC nonetheless conditionally approves it because of the combined bank's size and resulting resolvability challenges. The OCC is particularly concerned with what it calls "optionality" – i.e., the lack of an acquiring institution other than an even larger banking organization forcing either greater consolidation or a costly FDIC intervention. Ex ante resolution planning limits this risk as does the new requirement that USB "quickly" develop a list of business activities and portfolios that could be quickly divested along with a "data ring" that could be quickly populated to ready divestiture under stress. This plan must be provided to the OCC within six months of consummation and then be granted a ruling of no supervisory objection.
- "Countervailing" financial-stability benefits are noted by virtue of USB's stronger governance framework and technology in comparison to Union. USB's ability to increase West Coast competition with GSIBs is also noted.

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