THE BANK FAILURE CRISIS: CHALLENGES IN ENFORCING ANTITRUST REGULATION

I. INTRODUCTION

On March 16, 2008, JP Morgan Chase agreed to purchase the quickly collapsing Bear Stearns Companies, then the fifth largest securities firm on Wall Street and an eighty-five-year-old pillar of investment banking, for ten percent of the firm's value one week earlier.[1] This triggered a wave of consolidation in the banking market unlike any before.[2] One by one, commercial and investment banks began to merge[3] as banks could no longer mitigate their losses from mortgage-backed securities.[4] The banking landscape changed dramatically by the end of

1. Andrew Ross Sorkin, *JP Morgan Pays $2 a Share for Bear Stearns*, N.Y. TIMES, Mar. 17, 2008, *available at* http://www.nytimes.com (accessed from homepage by entering keywords "JP Morgan Pays") (last visited Nov. 9, 2009) ("Reflecting Bear's dire straits, JP Morgan agreed to pay only about [two hundred and seventy] million in stock for the firm, which had run up big losses on investments linked to mortgages . . . JP Morgan is buying Bear . . . for a third the price at which the smaller firm went public in 1985.").

2. Louise Story & Edmund L. Andrews, *A Sense That Wall St.'s Boom Times Are Over*, N.Y. TIMES, Sept. 15, 2008, *available at* http://www.nytimes.com (accessed from homepage by searching the phrase "Wall St's Boom Times") (last visited Nov. 9, 2009) ("[A]s investors tried to comprehend the abrupt downfall of two of Wall Street's mightiest firms — Lehman Brothers, which spiraled into bankruptcy, and Merrill Lynch, which rushed into the arms of Bank of America — even optimists said the immediate future would be difficult."). Story and Andrews also discuss the government's role, stating that "[t]reasury Secretary Henry M. Paulson Jr. and the Federal Reserve are paving the way for the few strong survivors to lead an industry turnaround, while letting the weaker ones fail or be subsumed by larger rivals." *Id.*

3. *See* Mark Anderson, *Big Changes Ahead for Region's Five Largest Banks*, SACRAMENTO BUS. J., Nov. 7, 2008, *available at* http://www.bizjournals.com (accessed from homepage by searching the phrase "Big Changes Ahead for Region") (last visited Nov. 9, 2009).

4. *See generally* E. Scott Reckard & Tiffany Hsu, *Feds Seize, Sell WaMu in Biggest U.S. Bank Failure*, Sept. 26, 2008, *available at* http://articles.latimes.com (accessed from homepage by searching the phrase "Feds Seize, Sell Wamu" and selecting "Wash. Mutual News in Sept. 2008") (last visited Nov. 9, 2009) (discussing federal regulators' seizure and subsequent sale of Washington Mutual Bank to JP Morgan Chase bank). Many banks and lenders, including most of the banks threatening to fail, invested heavily in mortgage-backed securities. These securities were created by banks and home lenders, such as Fannie May and Freddie Mac, and consisted of mortgages that were packaged together and sold. Initially, these securities were a big hit among the banking market. They were presented as fairly low risk, highly liquid securities. As these securities gained popularity, banks began packaging groups of less secure loans with higher home loan interest rates. These loans were known as "subprime mortgages" because borrowers did

2008, with only a few conglomerate banks dominating the canvas. Bank of America purchased Merrill Lynch and Countrywide Financial, JP Morgan Chase added Washington Mutual to its list of takeovers, and Wells Fargo took ownership of Wachovia.[5]

Responding to the potential failures of these large banks, the Federal Reserve and the Department of Justice began readily approving these "weekend bank mergers"[6] and disregarding antitrust regulations.[7] The effect has been a patch-job on an old, leaking tire. Part I of this Note discusses the roots of antitrust regulation as it applies to the banking market, first through the Clayton Act, the government's primary tool for preventing anticompetitive markets, and then through more bank-specific acts of Congress like the Bank Merger Act of 1960. It then explains the courts' interpretation and application of the Clayton Act to bank mergers since the Supreme Court's decision in *United States v. Philadelphia National Bank*,[8] and the current process that the federal government uses to review the legality of bank mergers.

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not meet ideal home lending guidelines (poor credit, little or no down payment, high debt-to-income ratio, etc.). Banks all over the world were participating in the buying and selling of mortgage-backed securities, full of subprime mortgages. Simply put, eventually more homeowners began defaulting on their subprime mortgages than anticipated, and the mortgage-backed securities became highly overvalued. Soon, banks were stuck with billions of dollars of mortgage-backed securities that they could no longer sell and on which they were no longer receiving returns. These assets are often referred to as the "toxic assets" that banks are unable to rid from their books. It is these "toxic assets" that led to the failure of a number of banks that invested heavily in them. *See generally* Chairman Ben S. Bernanke, Four Questions About the Financial Crisis at the Morehouse College, Atlanta, Georgia (Apr. 14, 2009), *available at* http://www.federalreserve.gov/newsevents/speech/bernanke20091414a.htm (last visisted Nov. 9, 2009); Mortgage-Backed Securities, SEC, June 25, 2007, *available at* http://www.sec.gov/answers/mortgagesecurities.htm (last visited Nov. 9, 2009).

5. Albert A. Foer, *Preserving Competition After the Banking Meltdown*, GCP: THE ONLINE MAGAZINE FOR GLOBAL COMPETITION POLICY, (Dec. 16, 2008), *available at* http://www.antitrustinstitute.org (accessed from homepage by entering keywords "Preserving Competition") (last visited Nov. 9, 2009).

6. *Id.*

7. *See generally* Len Boselovic, *Fed Approves PNC-National City Deal*, PITTSBURGH POST GAZETTE, Dec. 16, 2008, *available at* http://www.post-gazette.com (accessed from homepage by entering keywords "Fed Approves PNC Deal") (last visited Nov. 9, 2009); *Justice Department Approves BofA Deal for Merrill*, Oct. 17, 2008, http://www.bizjournals.com/sacramento.bizjournals.com (accessed from homepage by entering keywords "Deal for Merrill") (last visited Nov. 9, 2009) ("Charlotte, N.C.-based BofA agreed Sept. 15 to buy Merrill Lynch for about [fifty] billion. A Justice spokeswoman said . . . the deal has cleared antitrust review by the Federal Trade Commission.").

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

Part II analyzes the impact of bank consolidations on market-share concentrations and some of the effects of the government's failure to enforce antitrust regulations. This includes an analysis of potential anticompetitive concerns and the creation of banks that are "too big to fail." Part III of this Note suggests how federal regulators should respond to the current consolidated banking market through more permanent solutions such as statutory changes to antitrust laws and through additional governmental oversight committees. Finally, Part IV concludes that stricter application of antitrust laws should be applied to the current banking market in order to prevent future bank failures and bailouts, as well as to prevent potentially increased fees and loan rates.

II. BACKGROUND

A. The Clayton Act

Along with the Sherman Act,[9] section 7 of the Clayton Act[10] serves as the general federal antitrust statute targeting mergers that may lessen competition, not only in the financial sector, but for all major industries unless Congress has decided otherwise.[11] Section 7 of the Clayton Act is different from the Sherman Act in that it "is not intended to prohibit current anticompetitive behavior but instead is designed to preserve and promote market structures conducive to future competition by enabling judges to arrest monopoly or oligopoly in its incipiency."[12] Therefore, regulators must promote competition by assessing and preventing particular mergers before any anticompetitive violations actually occur.[13] This requires regulators to analyze possible future market-shares, rather than current market statistics: "[T]hus even mergers involving firms with relatively modest market shares have been enjoined when part of a growing trend toward concentration."[14] The relevant portion of the statute, codified in 15 U.S.C. § 18, states:

> No person engaged in commerce or in any activity affecting commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no person subject to

9. The Sherman Antitrust Act, 15 U.S.C. §§ 1-7 (West 2009) [hereinafter Sherman Act].

10. The Clayton Act, 15 U.S.C. § 18 (West 1996) [hereinafter Clayton Act].

11. Dan W. Schneider, *Evolving Proof Standards Under Section 7 and Mergers in Transitional Markets: The Securities Industry Example*, 1981 WIS. L. REV. 1, 6 (1981).

12. *Id.* at 6-7.

13. *Id.* at 7.

14. *Id.*

> the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another person engaged also 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 may be substantially to lessen competition, or to tend to create a monopoly.[15]

Determining the statute's application to the financial services industry, the Supreme Court in *United States v. Philadelphia National Bank*, discussed *infra*, explained that "[t]he statutory test is whether the effect of the merger may be substantially to lessen competition in any line of commerce in any section of the country."[16]

B. The Bank Merger Act of 1960

In addition to section 7 of the Clayton Act, Congress passed the Bank Merger Act of 1960.[17] The Bank Merger Act, which included a number of bank merger regulations, expressed similar goals as the Clayton Act, but was particular to the mergers of banks.[18] The Bank Merger Act explicitly prohibits regulators from approving any bank merger transaction that would result in a monopoly, further a conspiracy to monopolize, or that would substantially lessen competition.[19]

C. United States v. Philadelphia National Bank *(Application of Clayton Act)*

The foremost Supreme Court case regarding the mergers and acquisitions of banks is *United States v. Philadelphia National Bank.*[20] In that case, the Supreme Court analyzed the legality of a proposed merger between Philadelphia National Bank and the Girard Trust Corn Exchange Bank.[21] In this case, the Court applied section 7 of the Clayton Act, dismissing an argument that section 7 does not include bank mergers in its stock-acquisition provision.[22] The Court stated:

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15. 15 U.S.C.A. § 18.
16. *Phila. Nat'l Bank*, 374 U.S. at 355 (internal quotations omitted).
17. 12 U.S.C. § 1828 (West 2008) [hereinafter Bank Merger Act of 1960].
18. *Id.*
19. *Id.*
20. Gregory J. Werden, *Perceptions of the Future of Bank Merger Antitrust: Local Areas Will Remain Relevant Markets*, 13 FORDHAM J. CORP. & FIN. L. 581, 584 (2008).
21. *Phila. Nat'l Bank*, 374 U.S. at 323.
22. *Id.* at 343.

> Any other construction would be illogical and disrespectful of the plain congressional purpose in amending [section] 7, because it would create a larger loophole in a statute designed to close a loophole. It is unquestioned that the stock-acquisition provision of [section] 7 embraces every corporation engaged in commerce, including banks.[23]

The Court also emphasized that the stock-acquisition provision encompasses all methods of direct and indirect acquisitions, included mergers and consolidations, and that the Federal Trade Commission had jurisdiction of such acquisitions.[24]

Before delving into its section 7 analysis, the Court clarified that the Bank Merger Act in no way precludes the application of section 7 to bank mergers, and that the Court's application of the Clayton Act did not diminish the power of the Bank Merger Act.[25] Rather than having to apply one statute over the other, the Court explained that the Banker Merger Act and the Clayton Act are complimentary to one another.[26] Justice Brennan stated, "[i]f, in addition, bank mergers are subject to [section] 7, we do not see how the objectives of the 1960 Act are thereby thwarted."[27]

In applying section 7 of the Clayton Act, the Court had to examine the relevant market of the banks at issue in order to determine if there was a competitive overlap and if this overlap had an effect on competition in the region.[28] In the case at issue, the relevant market was a four-county region of the Philadelphia area.[29] In its analysis, the Court explained that the examination of the anti-competitive effects of a merger "requires not merely an appraisal of the immediate impact of the merger upon competition, but a prediction of its impact upon competitive

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23. *Id.* at 342-43. The Court explained that the section 7 stock-acquisition provision is broad enough to cover acquisitions of assets, and therefore mergers, stating that "Congress contemplated that the 1950 amendment would give [section] 7 a reach which would bring the entire range of corporate amalgamations, from pure stock-acquisitions to pure asset-acquisitions, within the scope of [section] 7." *Id.* at 342.

24. *Id.* at 346-48.

25. *Id.* at 354.

26. *Phila. Nat'l Bank*, 374 U.S. at 354-55 ("[C]ongress did not intend the 1960 Act to extinguish other sources of federal restraint of bank acquisitions having anticompetitive effects . . . Congress certainly knew that bank mergers would continue subject to the Sherman Act . . . as well as that pure stock acquisitions by banks would continue subject to [section] 7 of the Clayton Act.").

27. *Id.*

28. *Id.* at 357.

29. *Id.* at 361.

conditions in the future; this is what is meant when it is said that the amended section 7 was intended to arrest anticompetitive tendencies in their 'incipiency'."[30]

The Court explained that a merger should be enjoined if the resulting firm controls an "undue percentage share of the relevant market, and results in a significant increase in the concentration of firms in that market [such that it] is . . . inherently likely to lessen competition substantially."[31] The Court held that the merger between Philadelphia National Bank and Girard Trust Corn Exchange Bank, which would have controlled thirty percent of the relevant market after the merger (the top two banks would control fifty-nine percent of the market), was a sufficient threat to the described standard.[32]

D. The Bank Merger Review Process

Bank merger proposals, like mergers in any other industry, are submitted to relevant agencies, usually the Federal Trade Commission or the Federal Reserve, and the Antitrust Division of the Department of Justice ("agencies").[33] The agencies and the Department of Justice both utilize a screening process which allows them to categorize particular mergers as either those needing further scrutiny or those not requiring inquiry into anticompetitive effects.[34] Just as the Court did in

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30. *Id.* at 362.

31. *Id.* at 363. Seven years prior to the decision in *Philadelphia National Bank*, Chairman Martin of the Board of Governors of the Federal Reserve suggested a slightly different standard for reviewing bank mergers and their impact on competition. The Chairman stated: "The Board believes that, at least in the field of banking, the test should be whether or not a merger would result in 'undue' rather than a 'substantial' lessening of competition." *Statement on Bank Merger Bills: Statement Before the Subcomm. on Antitrust and Monopoly of the Comm. on the Judiciary of the S.*, 84th Cong. (1956) (statement of Chairman Martin, Board of Governors of the Federal Reserve System), *available at* http://fraser.stlouisfed.org (accessed from homepage by searching the phrase "Statement on Bank Merger Bills") (last visited Nov. 9, 2009).

32. *Phila. Nat'l Bank*, 374 U.S. at 364-65.

33. U.S. DEPT. OF JUSTICE, ANTITRUST DIV., BANK MERGER COMPETITIVE REVIEW: INTRODUCTION AND OVERVIEW, *available at* http://www.justice.gov/atrlpublic-/guidelines/6472.htm (last visited Nov. 9, 2009).

34. *Id.* Additional and further scrutiny consists of information such as:

> [E]vidence that the merging parties do not significantly compete with one another; evidence that rapid economic change has resulted in an outdated geographic market definition, and that an alternate market is more appropriate; evidence that market shares are not an adequate indicator of the extent of competition in the market . . . evidence concerning entry conditions, including evidence of entry by institutions within the last two years and the growth of those institutions that have entered; evidence of likely entry within the next two years, such as pending branch applications; and expectations about potential

Philadelphia National Bank, the agencies employ a system that recognizes and analyzes relevant geographical market areas, usually consisting of a group of counties.[35]

After the agencies determine a relevant market, the remaining analysis can be dissected into five steps.[36] First, the agencies "determine whether or not a proposed merger would significantly increase concentration in the relevant market and result in a high level of concentration in that market."[37] Second, the agencies determine whether

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> entry by institutions not now in the market area and the reasons for such expectations, including legal requirements for entry.

Id. Information not included in the Screen B worksheet may be helpful in determining if there is competition from other sources. This information includes:

> [E]vidence that a thrift institution is actively engaged in providing services to commercial customers, particularly loans for business startup or working capital purposes and cash management services; evidence that a credit union has such membership restrictions, or lack of restrictions, and offers such services to commercial customers that it should be considered to be in the market; evidence of actual competition by out-of-market institutions for commercial customers, particularly competition for loans for business startup or working capital purposes; evidence of actual competition by non-bank institutions for commercial customers, particularly competition for loans for business startup or working capital purposes.

Id.

35. *Id. See* Tim McCarthy, *Refining Product Market Definition in the Antitrust Analysis of Bank Mergers*, 46 DUKE L.J. 865, 867-68 (1997):

> The relevant geographic market is defined as the area in which a hypothetical monopolist could impose an increase in the price of its products without fear that competition would force the monopolist to abandon its attempt to increase prices. The relevant product market similarly is defined as the product or products whose prices the hypothetical monopolist could raise without fear that competition would force it to lower its prices. In the context of commercial bank mergers, the traditional method of defining the relevant product market has been to include in that market all the products and services traditionally provided by commercial banks, including products such as loans and services such as acceptance of savings and checking deposits and provision of trust services. This method is still used by the Federal Reserve. In recent years, however, the Antitrust Division has abandoned this 'cluster market' method of product market definition. It has instead adopted a method of disaggregation of the traditional cluster of bank products and services into several submarkets, with particular emphasis on the market for commercial lending to small and medium-sized businesses. Because the Division's method is intended to determine whether any of these several submarkets may be susceptible to anticompetitive effects, its scrutiny is now widely regarded as more stringent than that of the Fed.

36. *Id.* at 871.

37. *Id.* The agencies use a two-tiered calculation system for determining market concentrations for banks. Pre- and post-merger market concentrations in the relevant markets are calculated by using a system called the Herfindahl-Hirschman Index (HHI). This index uses a bank's total deposits in a relevant geographical market to determine its

the increase in market concentration, if any, creates possible anticompetitive effects.[38] Third, the agencies analyze whether other banks are able to enter the market and compete with the merged bank to counteract any anticompetitive effects the merger may have caused.[39] Fourth, the agencies "assess any efficiency gains that might result from the merger."[40] Last, the agencies consider whether facilitating the merger would be "necessary to prevent the failure of one of the merging banks."[41]

E. The Glass-Steagall Act and the Gramm-Leach-Bliley Act

The Glass-Steagall Act of 1933 was important to bank merger activity and bank failures, not only because it established the Federal Deposit Insurance Corporation (FDIC), but also because it separated commercial and investment banking, limiting commercial banks' ability to trade in securities.[42] One of the original reasons for creating this distinction in the market was the idea that the power of commercial banks should "be limited to ensure soundness and competition in the market for funds, whether loans or investments."[43] This market distinction promoted the theory that banks' inherent power should be restricted in their investments to limit the risk of deposits.[44] Essentially, the Act's effect was to limit the impact of a bank failure by preventing a bank's ability to enter other monetary markets. In 1999, however, Congress repealed the Glass-Steagall Act by passing the Gramm-Leach-Bliley Act,[45] which allowed holding banks to participate in securities trading.[46] The Gramm-Leach-Bliley Act "was passed for the purpose of

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strength. The first tier is called Screen A, and the second tier is called Screen B. A merger proposal fails Screen A if post-merger HHI value exceeds 1800 points and has increased by 200 index points from its pre-merger value. Screen B is a more stringent calculation to pass because it excludes thrift deposits from the total deposit base. *Id.* at 884-85.

38. *Id.* at 871.

39. *Id.*

40. McCarthy, *supra* note 35.

41. *Id.*

42. Banking Act of 1933, 48 Stat. 162 (1933) (repealed 1999).

43. WILLIAM D. JACKSON, CONG. RESEARCH SERV., ECON. DIV., GLASS-STEAGALL ACT: COMMERCIAL VS. INVESTMENT BANKING 3 (1987), *available at* http://digital.library.unt.edu/govdocs/crs/permalink/meta-crs-9065:1 (last visited Nov. 9, 2009).

44. *Id.*

45. Gramm-Leach-Bliley Financial Modernization Act of 1999, Pub. L. No. 106-102, 113 Stat. 1338 (1999).

46. Jonathan R. Macy, *The Business of Banking: Before and After Gramm-Leach-Bliley*, 25 J. CORP. L. 691, 709 (2000).

facilitating mergers and acquisitions" among banks and financial institutions.[47] The passage of the Gramm-Leach-Bliley Act, and the sanctioning of banks' ability to trade in securities and other investments, was essential to the current conception that banks have become "too big to fail" and the notion that they are too intertwined into the nation's economy, discussed *infra*.

III. ANALYSIS

A. Market Share Concentrations

Since *Philadelphia National Bank*, merger enforcement has varied slightly, but has generally led to an increasing trend of softer enforcement, especially within the last decade.[48] With the recent financial crisis, and in light of the multiple bank mergers of 2008, many experts have shown concern for the anticompetitive effects of this lenient enforcement.[49] The outcome of these bank mergers is a continuously consolidating market.[50]

To help maintain a competitive market in the banking industry, Congress passed the Riegle-Neal Interstate Banking and Branching Efficiency Act in 1994.[51] The Act stated that banks were limited to

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47. *Id.*

48. For an interesting study on the decline of antitrust enforcement since the 1960s, *see generally* Jonathan B. Baker & Carl Shapiro, REINVIGORATING HORIZONTAL MERGER ENFORCEMENT (2007), *available at* http://faculty.naas.berkeley.edu/SHAPIRO/-mergerpolicy.pdf (last visited Nov. 9, 2009) Baker and Shapiro explain in the Article's abstract that "[t]he past forty years have witnessed a remarkable transformation in horizontal merger enforcement in the United States. With no change in the underlying statute, the Clayton Act, the weight given to market concentration by the federal courts and by the federal antitrust agencies has declined dramatically." *Id.*

49. Press Release, American Antitrust Institute, AAI Calls for Government Review of Emergency Mergers to Include Competition Concerns (Oct. 21, 2008) [hereinafter Press Release], *available at* http://www.antitrustinstitute.org (accessed from homepage by searching phrase "AII Calls for Governmental Review") (last visited Nov. 9, 2009). The press release stated that "[t]he American Antitrust Institute (AAI) has called on regulators to carefully monitor the competitive effects of the deluge of emergency merger and acquisition transactions within the financial services sector." *Id.* AAI President Albert Foer suggested that "government agencies should carefully review the transactions as part of a larger investigation into how the sector should be restructured and regulated once order has been restored to the U.S. financial markets." *Id.*

50. *Id.*

51. *See* Laurie Kulikowski, *Bank M&A May Hinge on Deposit Cap Rule*, Nov. 6, 2008, *available at* http://www.thestreet.com (accessed from homepage by entering keywords "Bank M&A May Hinge") (last visited Nov. 9, 2009).

holding no more than ten percent of the total of nationwide deposits.[52] Regulators, however, have been efficiently working their way around the Act.[53] Wells Fargo's acquisition of Wachovia Bank is a prime example. It was reported that after the deal, Wells Fargo would hold just over ten percent of the sum of nationwide deposits.[54] Despite this fact, "the Fed argued that the purchase would not violate the federal law barring any company from controlling more than [ten percent] of the nation's deposits, because industry deposits have swelled as investors have fled money market funds."[55] Similarly, when Bank of America (which was already on the edge of the deposit cap)[56] acquired Countrywide Financial and Merrill Lynch in 2008, the "Fed" explained that the newly acquired deposits from the two acquisitions would not count toward the cap because "Countrywide's deposits are housed in the firm's thrift subsidiary, while Merrill Lynch's . . . deposits . . . were in both thrift and industrial loan company units," both of which are considered exceptions to the deposit cap rule.[57]

These individual deposit market shares turned this once heavily regulated market into one that is becoming increasingly consolidated.[58] After the series of mergers, Bank of America, JP Morgan Chase, and Wells Fargo will have roughly one-third of the nation's bank deposits.[59]

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52. 12 U.S.C. § 1831u (West 2009). Section (b)(2)(A), titled "Nationwide Concentration Limits," states: "The responsible agency may not approve an application for an interstate merger transaction if the resulting bank . . . upon consummation of the transaction, would control more than [ten] percent of the total amount of deposits of insured depository institutions in the United States." *Id.*

53. *See* Joe Adler, *For Fed, Deposit Cap is No Barrier for Wells Deal*, AM. BANKER, Oct. 23, 2008, at 3.

54. *Id.*

55. *Id.* (emphasis added).

56. Cybil White, *Riegle-Neal's 10% Nationwide Deposit Cap: Arbitrary and Unnecessary*, 9 N.C. BANKING INST. 347, 347 (2005) ("In 2004 Bank of America bought FleetBoston in a $49.3 billion all-stock transaction, giving it 9.9% of all federally-insured deposits in the United States.").

57. Kulikowski, *supra* note 51.

58. Robin Sidel & Damian Paletta, Abstracts, *Industry is Remade in a Wave of Mergers*, WALL ST. J., Sept. 30, 2008, at A1.

59. *See* David Lazarus, *Moral Hazards Rise When Banks Get Too Big to Fail*, L.A. TIMES, Oct. 1, 2008, at A2, *available at* http://articles.latimes.com/2008-/Oct/01/business/fi-lazarus1 (last visited Nov. 9, 2009) (listing the three banks with one-third of the nation's deposit shares as Bank of America, JP Morgan Chase, and Citigroup). The numbers in Lazarus' article prematurely reflected that Citigroup acquired Wachovia Bank. On October 3, 2008 Wells Fargo announced that it, instead of Citigroup, would acquire Wachovia Bank. The Wells Fargo merger created a similarly-sized entity as a Citigroup-Wachovia merger would have created. *See* Rick Rothacker & Christina Rexrode, *Legal Battle Brewing Over Wachovia-Wells Fargo Merger*, THE CHARLOTTE OBSERVER, Oct. 3, 2008.

In addition to increasing national market shares, regional markets (federal regulators generally use regions to determine the extent of banking antitrust violations)[60] are often much more consolidated.[61]

Moreover, this wave of consolidations has not only affected the market for bank holding companies, but also the market for investment banks.[62] After JP Morgan Chase acquired Bear Stearns, Lehman Brothers filed for bankruptcy, and Bank of America acquired Merrill Lynch, Goldman Sachs and Morgan Stanley became the "last big independent investment banks."[63]

These deposit cap breaches and extremely rapid market consolidations, although by no means dispositive of antitrust activity,[64] are examples of regulators turning their backs to antitrust regulation because of the financial crisis.

B. The Consequences of Relaxed Antitrust Regulation

1. The Lessening of Competition

One of the major concerns of the "extraordinary rate of mergers and acquisitions activity among the nation's largest financial institutions"[65] is that small- and medium-sized banks will feel pressure from the federal

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60. McCarthy, *supra* note 35, at 866-68. McCarthy notes that the Antitrust Division of the Department of Justice and the federal banking agencies, like the Federal Reserve, often differ on the relevant geographic market areas and product market areas when reviewing bank mergers for antitrust violations. The federal banking agencies tend to use a "cluster market" method, whereas the Department of Justice uses a "disaggregative submarket method." *Id.*

61. *See, e.g.*, Dan Wallach, *Wells Fargo, Wachovia Combine as Largest Bank in Southeast Texas*, THE BEAUMONT ENTERPRISE, Oct. 17, 2008, *available at* http://www.beaumontenterprise.com (accessed from homepage by entering keywords "Wells Fargo, Wachovia Combine as Largest Bank") (last visited Nov. 9, 2009).

62. *See* Andrew Ross Sorkin & Vikas Bajaj, *Radical Shift for Goldman and Morgan*, N.Y. TIMES, Sept. 22, 2008, at A20, *available at* http://www.nytimes.com (accessed from homepage by entering keywords "Radical Shift for Goldman and Morgan") (last visited Nov. 9, 2009).

63. *Id.* Both Goldman Sachs and Merrill Lynch became bank holding companies, rather than investment banks, because only bank holding companies were qualified to receive federal TARP funds. *See* John C. Coates & David S. Scharrfstein, *The Bailout is Robbing the Banks*, N.Y. TIMES, Feb. 17, 2009, *available at* http://www.nytimes.com (accessed from homepage by entering keywords "The Bailout is Robbing the Banks") (last visited Nov. 9, 2009).

64. Constance K. Robinson, Director of Operations, Antitrust Div., U.S. Dep't of Justice, BANK MERGERS AND ANTITRUST 3, Address Before the 31st Annual Banking Law Institute, May 30, 1996, *available at* http://www.usdoj.gov/atr/public/speeches/1003.htm (last visited Nov. 9, 2009).

65. Press Release, *supra* note 49.

government and the FDIC to secure their deposits by agreeing to be acquired by larger banks.[66] Indeed, many believe that the "best hope for many struggling banks is for healthy institutions to snap them up."[67] However, as in most markets that experience rapid consolidation, "customers will face less choice and potential for higher fees."[68] Essentially, one must weigh the benefit of a greater sense of banking security against the possibility of higher fees and interest rates for borrowers.[69]

Many organizations, such as the California Reinvestment Coalition (CRC), have already approached Congress about their concerns regarding the negative, anticompetitive effects of the recent bank mergers.[70] In particular, the CRC contacted the appropriate Senate and House committees on October 15, 2008, asking them to "hold oversight hearings" on how the current state of bank consolidation can "negatively impact neighborhoods, small businesses and homeowners."[71] Throughout the financial crisis, small business owners and homeowners have had limited credit access.[72] The CRC believes that bank consolidations will further limit access to credit, especially for businesses and nonprofit housing development organizations run by minorities and women in under-served neighborhoods.[73]

The CRC's concern is not without merit. Studies show that small business lending in urban areas is dominated by local banks, with only twelve percent of small business loans being administered by larger, out-of-area banks.[74] The reason for this is that "micro-business lending" by larger banks is based heavily on credit scoring, rather than the relationship with the borrower, and is often limited to loan amounts as small as $100,000.[75] This credit score-based system of lending puts

66. *See* Catherine Clifford & Tamy Luhby, *2 More Banks Go Belly-Up*, CNNMONEY.COM, Nov. 7, 2008, *available at* http://money.cnn.com (accessed from homepage by entering keywords "2 More Banks Go Belly-Up") (last visited Nov. 9, 2009).

67. Sidel & Paletta, *supra* note 58, at A1.

68. *Id.*

69. Lazarus, *supra* note 59, at A2.

70. California Reinvestment Coalition, *Unregulated Bank Consolidation Will Hurt Underserved Neighborhoods*, Oct. 15, 2008, *available at* http://www.calreinvest.org (accessed from homepage by selecting "Newsroom" then "Press Releases") (last visited Nov. 9, 2009).

71. *Id.*

72. *Id.*

73. *Id.*

74. Werden, *supra* note 20, at 592.

75. *Id.* at 592-93.

larger banks at an informational disadvantage.[76] In fact, a study by the Small Business Administration calculated that loans made by banks using a credit scoring-based system of lending had a default rate that was twenty-three percent higher than local banks that did not use the same credit-score system.[77] This undoubtedly makes larger banks more reluctant to give small urban developers access to credit. This practice of larger banks swallowing up smaller banks will likely lead to a consolidated market with less credit available for developers in urban areas.[78]

The CRC's concern may have come to life as of late. Many urban areas, such as Detroit, Dallas, and Memphis, among others, have felt the severity of the credit crunch, slowing urban development throughout the country and causing businesses to scatter for capital.[79] In downtown Detroit, for example, developers have renovated the historic Westin Book Cadillac Hotel, a renovation which included sixty-three luxury condominiums.[80] Potential condominium buyers, however, have encountered lending problems.[81] The developers stated that "[they] used to have five or six lenders on these deals and now . . . have one, maybe two" and that they are "talking about people with great credit and have successful careers."[82] Large banks find these urban home loans too risky and new housing developments in these areas have slowed as a result.[83]

Others argue that stronger banks acquiring weaker banks will actually reduce fees and rates for borrowers by creating stronger competition nationally for the bigger firms[84] and, maybe more

76. *Id.*

77. *Id.*

78. *See, e.g., Unregulated Bank Consolidation Will Hurt Underserved Neighborhoods*, *supra* note 70.

79. *See* Louis Aguilar, *Condo Sales Hit Snag at Book Cadillac*, THE DETROIT NEWS, Jan. 19, 2009, at 1A; *see also* Sheryl Jean, *Apartment Construction Credit Crisis Hits Home for JPI-Developer Puts Off Pursuit of New Projects, Lays off Workers*, THE DALLAS MORNING NEWS, Oct. 11, 2008, at 1D; Cassandra Kimberly, *Everyone Feels Pinch As The Economy Slows*, MEMPHIS COMMERCIAL APPEAL, Oct. 5, 2008, at C1, *available at* http://www.commercialappeal.com (accessed from homepage by searching the phrase "Credit Crisis Hitting Home") (last visited Nov. 9, 2009); Ken Bensinger, *Big Automakers Seek To Tap Fed Lending Program; GM, Chrysler, Ford Look To The Government For Aid As The Credit Crisis Dries Up Their Access To Cash*, L.A. TIMES, Oct. 29, 2008, at C3.

80. Aguilar, *supra* note 79, at A1.

81. *Id.*

82. *Id.*

83. *See* Kimberly, *supra* note 79.

84. Lazarus, *supra* note 59, at A2 (quoting Gary Dymski, a professor of economics at NC Riverside: "The conversation now is about fit -- who needs what to be fully national . . . Next comes being biggest among the big boys . . . . Maybe that'll result in greater

importantly, increasing (through funding from the United States Treasury) banks' ability to provide credit.[85] While this theory could very well be true, it pulls us away from the principles of strong antitrust regulation set out in *Philadelphia National Bank.* Justice Brennan explained:

> We reject this application of the concept of 'countervailing power' . . . . If anticompetitive effects in one market could be justified by procompetitive consequences in another, the logical upshot would be that every firm in an industry could, without violating [Section] 7 [of the Clayton Act], embark on a series of mergers that would make it in the end as large as the industry leader.[86]

Therefore, federal regulators' failure to enforce antitrust laws cannot be justified by asserting that such mergers will have procompetitive effects on a national scale, because such benefits come at the cost of smaller markets.[87]

2. *The Creation of Banks that are "Too Big to Fail"*

A second, and more notable, concern arising from the rapid consolidation of the banking market is the concept that these mega-banks will become "too big to fail." The idea is that some banks and other financial institutions grow so large, and become so interconnected into the economy, that allowing them to fail would devastate the economy.[88] With the recent seven-hundred billion dollar bailout plan (the Treasury's Troubled Asset Relief Program, or TARP), the government has essentially conceded that some of the financial institutions are indeed too big too fail and are in need of government funding in order to remain in

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competition for our business, along with lower fees and better interest rates and new branches in distressed communities.") (internal quotations omitted).

85. Len Boselovic, *PNC, National City Deal a Glimpse of What's Ahead*, PITTSBURGH POST-GAZETTE, Oct. 26, 2008, at A1, *available at* http://www.post-gazette.com (accessed from homepage by searching the phrase "PNC, National City Deal a Glimpse") (last visited Nov. 9, 2009).

86. *Phila. Nat'l Bank*, 374 U.S. at 370.

87. *See id.* at 371-72.

88. *See* Marty Schladen, *Banks Too Big to Fail?*, Journalgazzette.net, (Oct. 1, 2008), *available at* http://www.journalgazette.net/apps/pbcs.dll/article?AID=/20081001/BIZ-/810010367&template=printart (last visited Nov. 9, 2009).

operation.[89] Ironically, by using federal funds to bailout these financial entities,

> the government has engineered a series of buyouts and bailouts of financial institutions that were judged to be too big and too interconnected to fail. But doing so has ushered in a wave of consolidation in an industry that will now consist of a few giants that also are too big and too interconnected to fail.[90]

A concern is "that the consolidation of financial services companies won't just create firms that are 'too big to fail' but firms . . . that will be too big to compete."[91] The fear is that these firms become so big that regulators become "co-opted by the industries they regulate."[92] By failing to enforce antitrust laws and ignoring protective procedures such as deposit caps, the federal government is promoting a vicious snowball effect of banks that are growing in size and an economy that is becoming increasingly reliant upon them.

Not only has the government promoted banks that are too big to fail through the inaction of regulatory agencies (lack of antitrust enforcement), it has actively promoted bank consolidation through support of the Treasury Department and Congress.[93] In fact, rather than using federal TARP funds to help banks provide credit to businesses or to wipe troubled assets from struggling banks' books,[94] a significant portion of the TARP funds were used to facilitate the aforementioned, massive bank mergers.[95] For example, among TARP funds distributed to

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89. *Id.*

90. *Id.*

91. Andrew Ross Sorkin, *Why Obama May Assent to Deals*, N.Y. TIMES, Nov. 11, 2008, at B1.

92. *Id.*

93. *See, e.g.*, Boselovic, *supra* note 7.

94. The Treasury recently announced that it will use up to one hundred billion dollars of remaining TARP funds to buy troubled assets from banks. *See Geithner Asks for Patience as Toxic-Asset Purchase Begins*, USA TODAY, Mar. 23, 2009, *available at* http://www.usatoday.com (accessed from homepage by entering keywords "Geithner Asks for Patience") (last visited Nov. 9, 2009).

95. *See generally* Boselovic, *supra* note 7, at 91.

> Analysts say the $7.7 billion in federal support Pittsburgh-based PNC Financial Services Group received to acquire Cleveland's troubled National City Corp. is the first of what is expected to be dozens of government-financed acquisitions of weak banks by strong ones. The infusions are intended to restore confidence in the banking system and credit markets.

Id. However, some Congressmen, like Senator John McCain, have opposed such use of federal bailout funds. Senator McCain has been quoted as saying (with regard to PNC Financials purchase of National City Bank): "I think Congress should . . . . Congress

JP Morgan Chase and other banks to facilitate mergers, Bank of America received twenty billion dollars (in addition to fifteen billion dollars originally apportioned to it) to assist in the completion of its merger with Merrill Lynch.[96]

This type of circular thinking seems counterproductive. Rather than addressing the causes of these bank failures to prevent future occurrences of similar magnitude, the federal government has created a situation where future bank-failures would have even more profound effects.

3. *Public Policy Concerns Trump Antitrust Regulation*

The government has clearly elected to address the significant public policy concerns underlying major bank failures rather than enforce antitrust regulations.[97] The federal bailout of failing banks under TARP is a significant start toward this policy. Some believe, however, that the government will take an even stronger role in preventing the failure of banks rather than enforcing antitrust laws, not only for protecting banking services, but also for other public policy reasons, such as to protect jobs.[98] One expert anticipates that the new Obama administration may be forced to put antitrust laws on the back burner, explaining that "Mr. Obama might want to police antitrust issues, but . . . [i]t just won't be politically palatable to kill deals that could save some jobs. Preserving jobs and economic stability will be perceived as more important than

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needs to exercise oversight. And clearly, we need to focus attention on the homeowner . . . ." Obviously, I do not support these types of deals. I think Congress needs to have hearings." Luke Mullins, *McCain Wants PNC-National City Deal Investigated*, Nov. 15, 2008, *available at* http://www.usnews.com (accessed from homepage by searching the phrase "McCain Wants PNC-National City") (last visited, Nov. 9, 2009).

96. Peter Barnes & Joanna Ossinger, *BofA to Get $20B More From TARP, Plus Backstop on $118B*, foxbusiness.com, Jan. 16, 2009, *available at* http://www.foxbusiness.com/story/markets/industries/finance/bofa-shares-falter-reports-needs-new-tarp-money/ (last visited Nov 9, 2009). The authors explained:

> A source told FOX Business that BofA will use the additional [twenty] billion in TARP funds to help the bank digest and integrate Merrill. The source said that after BofA and Merrill announced their merger deal last fall, Merrill's financial health continued to deteriorate. In mid-December, BofA executives met with Treasury Secretary Hank Paulson and asked him for assurances that if the bank needed additional TARP capital because of the Merrill merger, Treasury would provide it. Otherwise, the executives told Paulson, BofA would cancel the Merrill acquisition. The source said Paulson agreed to the request.

Id.

97. *See* Sorkin, *supra* note 1.

98. *Id.*

preserving competition."[99] Nevertheless, despite the government's lack of concern for antitrust regulation throughout the recent financial crisis, its actions are not unqualified. In fact, a key clause in the Bank Merger Act, 12 U.S.C. § 1828 (c)(5)(b) states that:

> [T]he responsible agency shall not approve – any other proposed merger transaction whose effect in any section of the country may be substantially to lessen competition, or tend to create a monopoly, or which in any other manner would be in restraint of trade, unless it finds that the anticompetitive effects of the proposed transaction 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.[100]

If in fact these public policy concerns outweigh a merger's anticompetitive effects, the Bank Merger Act expressly allows regulators to forgo further analyses by the Department of Justice.[101] The Act states that:

> The responsible agency shall immediately notify the Attorney General of any approval by it pursuant to this subsection of a proposed merger transaction. If the agency has found that it must act immediately to prevent the probable failure of one of the insured depository institutions involved, or if the proposed merger transaction is solely between an insured depository institution and 1 or more of its affiliates, and the report on competitive factors has been dispensed with, the transaction may be consummated immediately upon approval by the agency.[102]

In addition to this "catchall" clause within the Bank Merger Act that allows federal regulators to disregard antitrust issues during periods of financial instability, the government's recent actions are not inconsistent with Justice Brennan's opinion in *Philadelphia National Bank.* Justice Brennan explained that "Section 7 does not mandate cutthroat competition in the banking industry, and does not exclude defenses based on dangers to liquidity or solvency, if to avert them a merger is

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99. *Id.* (quoting antitrust expert, attorney David Boies, who was hired by the Department of Justice to help break up Microsoft in the 1990s).
100. 12 U.S.C. § 1828 (c)(5)(b) (West 2009).
101. 12 U.S.C. § 1828 (c)(6) (West 2009).
102. *Id.*

necessary."[103] Justice Brennan also stated that "the so-called failing-company defense . . . might have somewhat larger contours as applied to bank mergers because of the greater public impact of a bank failure compared with ordinary business failures."[104]

C. Future Regulation

Now that the federal government has turned a cheek to antitrust regulation in the financial markets and decided that Justice Brennan's "failing-company defense"[105] is preferred to stabilize the market, it must understand the consequences of its actions. The already proposed and implemented mergers are beyond the point of limitation. It is impossible to undo the market changes that banks now rely upon (including billions of TARP funds to facilitate their mergers and keep their operations afloat). Yet the effects of future bank failures will probably be substantially greater than what has occurred with the recent string of collapses and buyouts,[106] and to treat the recent "patch-job" of allowing larger banks to swallow smaller banks as a permanent solution would be foolish. With a handful of banks dominating the market,[107] the new presidential administration, along with the Federal Trade Commission and Department of Justice, must strictly enforce antitrust regulations to prevent our economy from becoming any more dependent on just a few banks.

Strict antitrust compliance should continue as many of the large banks divest assets during the post-merger era.[108] This would allow

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103. *Phila. Nat'l Bank*, 374 U.S. at 371-72.

104. *Id.* at 372 n.46.

105. *Id.*

106. *See, e.g.*, Foer, *supra* note 5, at 5. Albert Foer states:

> Bank of America... will be an even more massive employer, with huge leverage over the political and economic system from the money it has discretion to give out or withhold . . . . These mega financial services companies we're in the process of creating are going to be able to demand from Congress, quite persuasively, whatever it is they say they need, using the threat of failure.

Id.

107. *See generally* Lazarus, *supra* note 59, at A2.

108. Albert A. Foer notes:

> when deals are made over the weekend [many of the recent mergers were decided in only a 2 or 3 day span], the likelihood is that they will not work very well. Even well-conceived, carefully planned mergers rarely work out as projected, for a variety of reasons, including clashing corporate cultures. The weekend mergers we are seeing could very easily devolve into a series of voluntary divestures over the next several years, as the parts that don't fit into an evolving corporate strategy get lopped off.

mega-banks to decrease in size and influence, and would prohibit acquisitions for a significant time period. Not only should antitrust regulators continue with market overlap analysis, which is regulators' main focus when reviewing bank mergers,[109] but they should also begin accounting for whether a specific bank merger would further a bank's status as "too big to fail." Albert A. Foer, President of the American Antitrust Institute, suggests that one way of accomplishing this is to modify the Clayton Act to permit federal regulators to include such an analysis into their merger review process.[110]

Amending the Clayton Act to give regulators more power to review bank mergers beyond the current analysis would not be relevant, however, unless regulators have access to the information necessary to make these decisions. In order to prevent a future crises like the recent bank failures, and to properly enforce this "too big to fail" prevention policy, the administration should develop an agency or commission that has the ability to study the current banking market, assess how capital is allocated throughout the economy (specifically within the banking sector) and pinpoint which banks need to be more strongly regulated.[111] This commission would work collaboratively with the Federal Trade Commission, the Federal Reserve, and the Department of Justice, along with cooperation from Congress, private economists, and the financial corporations themselves.[112] Together, amendments to the Clayton Act

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Foer, *supra* note 5, at 7-8.

109. *See supra* Part II.D.

110. *Id.* at 12. Foer explains:

> there is the industrial policy question of whether a merger should be stopped on the theory that the resulting company will be too embedded to be allowed to fail. The required analysis may go beyond the expertise, not to mention current statutory authority, of the antitrust agencies. But Congress could modify the Clayton Act in such a way that the antitrust agencies, together with the Treasury Department and perhaps the Federal Reserve, could participate when a potential merger is characterized as involving a keystone firm.

Id. Another strategy Foer discusses, in addition to modifying the Clayton Act for a "too big to fail analysis," is to amend the Clayton Act so that a bank merger review includes an analysis as to whether a particular merger would weaken the merging bank, thereby making it more susceptible to failure. This would supplement the "too big to fail" analysis, promoting the idea that not only will regulators prevent banks from becoming too intertwined in our economy, but also that any existing mega-banks will not become more susceptible to collapsing through the acquisition of bad assets. This type of analysis would be far more complex than the current bank merger review system. *Id.*

111. *See generally id.* at 14.

112. *Id.* A special commission is necessary because of the complexity of the analysis that would be required. Albert Foer has likened such a commission to the Temporary National Economic Committee (TNEC) that was enacted by the Roosevelt administration during the Great Depression. The TNEC was established "as a joint Congressional-

and the establishment of a special oversight committee would allow the government to limit the effects of failing mega-banks in the future.

IV. CONCLUSION

The failure of investment bank giant Bear Stearns was the first of many bank failures to come to light in 2008. Many large banks took this as an opportunity to expand by acquiring the struggling banks. The federal government's solution to the failing bank crisis was to allow these mergers and permit hyper-consolidation of the banking sector. The regulatory agencies and Congress not only failed to enforce many antitrust laws out of concern for public policy, but also encouraged acquisitions by mega-banks by facilitating mergers with billions of dollars of federal TARP funds.

In addition to concerns regarding competition, this hyper-consolidation of the banking market has reinforced the vicious cycle of banks that are so large and intertwined into our nation's economy that they are simply "too big to fail." The market consolidation of banks should be thought of not as a permanent solution, but as only a temporary answer to an urgent crisis. Congress needs to facilitate statutory changes, amending the Clayton Act and establishing a committee to oversee the post-merger banking market. The Clayton Act must allow for the Federal Trade Commission, the Federal Reserve, and the Department of Justice to consider the "too big to fail" effect during their review of bank mergers. These regulators, together with Congress, private economists, and representatives from the financial markets, must assess current market conditions, determine which financial entities are problematic,

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Executive branch committee, composed of members of both houses of Congress and representatives of several Executive departments and commissions, by joint resolution of Congress, June 16, 1938" and ran until 1941. *See* Records of the Temporary National Economic Committee, Guide to Federal Records in the National Archives of the United States, *available at* http://www.archives.gov (accessed from homepage by searching the phrase "Records of the Temporary National Economic Committee") (last visited Nov. 9, 2009). The TNEC was created "to bring together key members of Congress, relevant government agencies, and civilian experts to undertake a large scale multi-year baseline study of the American economy and to make recommendations as to what should be done." Foer, *supra* note 5, at 13-14. While this author believes that a commission similar to the TNEC may be too broad in scope to review bank mergers and their respective parties, cooperation from multiple groups would be necessary to achieve consensus throughout the review process. With the 2008 presidential election approaching, Foer noted that he would "like to see the next President [now President Obama] take the initiative in appointing a new version of the TNEC with a three-year mission to study the capital allocation system, domestically and internationally, and to make recommendations as to its structure and governance." *Id.* at 14.

and come to a common understanding of how they are to be handled. The first step, however, is realizing that consolidation of the banking market has only stabilized the market for the short-run, and that federal bailout dollars cannot logistically be a solution to a long-term problem.[113]

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113. Foer explains that "we must recognize the problems that we are creating and commit ourselves to dealing with them in an appropriate and timely way. It would be a terrible but easily made mistake to silently accept that whatever happens in the crisis is necessarily going to be permanent." *Id.* at 15.