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Interpreting the 1981 Amendments to the Illinois Bank Holding Company Act

Ray H. Greenblatt*

INTRODUCTION

On July 3, 1981, Governor Thompson signed Public Law 82-21,¹ amending the Illinois Bank Holding Company Act of 1957² (the "1957 Act") to permit bank holding companies commencing January 1, 1982, to acquire multiple banking subsidiaries in Illinois. Basically, the amended statute (the "1981 Act") permits a bank holding company to acquire an unlimited number of banks in Illinois subject to two limitations: first, a bank chartered after January 1, 1982 may not be acquired until it has engaged in the banking business for at least ten years;³ and second, the main banking premises of all banks in Illinois acquired by a bank holding company after January 1, 1982 must be located in the holding company's statutory home region and not more than one contiguous region of the five banking regions into which the 1981 Act divides the state.⁴

This article will explore the manner in which the 1981 amendments will change Illinois bank holding company law and examine a number of questions raised by the 1981 Act. The article will then analyze the impact the 1981 Act is likely to have on antitrust considerations affecting the assessment of bank acquisitions in Illinois.

THE NONCOMMERCIAL BANK

Unlike the 1957 Act, which defines "bank" to mean any bank in Illinois organized under the national banking laws or the laws of

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2. ILL. REV. STAT. ch. 16 1/4, ¶¶ 71-76 (1979). The 1957 Act, as amended by the 1981 amendments, has been renumbered and transferred to chapter 17 in the Smith-Hurd Illinois Annotated Statutes. Citations to the current version of the Act, effective January 1, 1982, will be to the 1981 Smith-Hurd Illinois Annotated Statutes. Citations to superseded or repealed portions of the Act will be to the 1979 Illinois Revised Statutes.


Illinois,\textsuperscript{5} the 1981 Act\textsuperscript{6} defines “bank” in a manner substantially identical to the Federal Bank Holding Company Act (the “Federal Act”).\textsuperscript{7} More specifically, the 1981 Act defines “bank” to mean any national or state bank, wherever organized, which “(1) accepts deposits that the depositor has a legal right to withdraw on demand by check or other negotiable order and (2) engages in the business of making commercial loans.”\textsuperscript{8}

This changed definition of “bank” could be very significant. A bank organized under national or state banking laws which accepts deposits but does not “engage in the business of making commercial loans” is not a “bank” for purpose of the 1981 Act. A bank which restricts its lending operations to consumer loans, residential mortgage loans and loans to charitable entities would be such an institution.\textsuperscript{9} Neither the geographical limitation on holding company expansion (home region plus one contiguous region) nor the prohibition against acquiring \textit{de novo} or recently-chartered banks applies to the acquisition of banking entities not engaged in the business of making commercial loans. Thus, a bank holding company, whether or not based in Illinois, can presumably acquire such banking entities anywhere in the state and can form them \textit{de novo}, provided, of course, that it can obtain Federal Reserve Board approval for such acquisitions.\textsuperscript{10}

\begin{footnotesize}
9. The Federal Reserve Board has confirmed that a bank which restricts its lending activities to loans for personal, family, household and charitable purposes would not be a “bank” within the meaning of § 2(c) of the Federal Act. 12 U.S.C. § 1841(c). Correspondence from (i) James McAfee, Assistant Secretary of the Board of Governors of the Federal Reserve System, to Robert C. Zimmer, Counsel to Associates First Capital Corporation. (March 11, 1981); (ii) Neal L. Peterson, General Counsel, Board of Governors of the Federal Reserve System, to Joshua M. Berman, Counsel to The Boston Company, Inc. (May 19, 1978); (iii) Michael A. Greenspan, Assistant Secretary of the Board of Governors of the Federal Reserve System, to Lee J. Aubrey, Vice President, Federal Reserve Bank of Boston (May 18, 1972); and (iv) Kenneth A. Kenyon, Deputy Secretary, Board of Governors of the Federal Reserve System, to Biaggio M. Maggiacomo, President, Greater Providence Deposit Corporation (July 1, 1971). The foregoing correspondence is on file with the Loyola University of Chicago Law Journal.
10. Indeed, by reason of the closely similar definition of “bank” in the Federal Act, such bank holding company could, subject to Federal Reserve Board approval, acquire noncommercial banks anywhere in the United States without running afoul of the Federal Act’s “Douglas-Amendment” limitation on interstate bank acquisitions not expressly permitted by the law of the state where the target bank is located. 12 U.S.C. § 1842(d)(1) (1976). An application for Board approval of the acquisition of a noncommercial bank would be made.
\end{footnotesize}
Moreover, if the 1981 Act is construed in accordance with federal precedent, an ineligible target bank can be transformed into an eligible "nonbank" by a disposition of its commercial loan portfolio prior to acquisition. Under substantially identical language in the Federal Act, companies have been permitted to acquire deposit-taking banks without registering as bank holding companies or obtaining Federal Reserve approval to control such banks, if prior to such acquisition the bank divests its commercial loan portfolio and does not thereafter engage in the business of making commercial loans.\textsuperscript{11}

under § 4(c)(8) of the Federal Act relating to nonbank activities, 12 U.S.C. § 1843(c)(8), rather than § 3 relating to acquisitions of banks, 12 U.S.C. § 1842. Although the Board has confirmed that companies which are not bank holding companies may acquire noncommercial banks without becoming bank holding companies subject to the Federal Act, see note 11 infra and accompanying text, the Board has not yet had occasion to rule on a bank holding company application to acquire a noncommercial bank. It is clear that a noncommercial bank's activities would be "closely related to banking", thereby satisfying part of the § 4(c)(8) requirement that the activities in question be "so closely related to banking . . . as to be a proper incident thereto." Section 4(c)(8), however, also requires that the Board, "in determining whether a particular activity is a proper incident to banking . . . shall consider whether its performance by an affiliate of a holding company can reasonably be expected to produce benefits to the public . . . that outweigh possible adverse effects." Even though the activities of a noncommercial bank would be "closely related to banking", therefore, the Board would have power under § 4(c)(8) to deny an application on the ground that such activities are not a "proper incident" to banking. \textit{See, e.g.}, Federal Reserve Board orders denying acquisitions by American Fletcher Corporation of Southwest Savings and Loan Association, 60 Fed. Res. Bull. 868 (1974), and by Memphis Trust Co. of Homeowners Savings and Loan Association, 61 Fed. Res. Bull. 327 (1974). In the \textit{American Fletcher} and \textit{Memphis Trust} cases, the Board, after finding savings and loan activities to be "closely related to banking", denied the bank holding company's application to acquire a savings and loan association on the ground that, at least under the circumstances prevailing in 1974 and 1975, bank holding company entry into the savings and loan business would not satisfy the "proper incident" test. The issue of bank holding company acquisition of thrift institutions was reopened in 1981 when, at the request of Congress, the Board commenced a study of the potential effects of such acquisitions. FRB Request for Comments, March 16, 1981. \textit{CCH Fed. Banking L. Rep.}, ¶ 98,649 (Mar. 27, 1981).

THE LIMITATION ON ACQUISITIONS OF NEW BANKS—EXCEPTION FOR BANKS CHARTERED BEFORE EFFECTIVE DATE

Section 3.05 of the 1981 Act provides that a bank chartered after January 1, 1982, cannot be acquired unless it has engaged in the banking business for at least ten years. Although this limitation essentially forecloses expansion through formation of de novo banks, it relates only to banks in Illinois chartered after January 1, 1982. A bank chartered prior to that date need not have engaged in the banking business for any prescribed period in order to be eligible for acquisition. Thus, a bank chartered prior to January 1, 1982, can be lawfully acquired under the 1981 Act even though it has been engaged in the banking business for less than ten years.

Indeed, the exclusion permitting acquisition of a bank chartered prior to January 1, 1982, is not conditioned on any requirement that the bank engage in the banking business prior to that date or to the acquisition date. Does the 1981 Act permit a bank holding company, which has caused a de novo bank in Illinois to be chartered by friendly organizers on or before January 1, 1982, to acquire and commence the operations of such bank after January 1, 1982?

The answer to this question may depend on interpretation of the 1957 Act, which continues in effect until January 1, 1982, the effective date of the 1981 Act. The 1957 Act, through its prohibition of multibank holding companies, prevents a company from acquiring

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12. Section 3.05 provides:

Subject to the provisions of Section 3.06 of this Act, on or after the effective date of this amendatory Act enacted by the 82nd General Assembly, no company may acquire, directly or indirectly, a bank in Illinois chartered after the effective date of this amendatory Act enacted by the 82nd General Assembly until such bank has engaged in the banking business for at least ten years. A bank in Illinois shall not be deemed to have been acquired, for purposes of this Section, if such acquisition is made through a reorganization which results in the transfer of control of a single bank in Illinois to a company formed to effect such reorganization pursuant to a tender offer by such company for the shares of such bank in Illinois, or pursuant to a merger or consolidation of such bank in Illinois with a bank in Illinois formed as a subsidiary of such company to effect the reorganization, if the shareholders of such company, and their respective percentage shareholdings, immediately following such reorganization are substantially identical to the shareholders, and their respective percentage shareholdings, of such bank in Illinois immediately before the reorganization except to the extent shareholders of such bank in Illinois holding voting shares thereof outstanding immediately before such reorganization do not as a result of such reorganization become shareholders of such company either by reasons of not accepting such tender offer or of exercising statutory rights to dissent from any such merger or consolidation.

control of more than one bank in Illinois. More specifically, the 1957 Act prohibits “bank holding companies,” which it defines to include any company “which directly or indirectly owns or controls 15 per centum or more of the voting shares of each of two or more banks.” The 1957 Act’s definition of “bank” is broad enough to include a bank which has not yet commenced business.

The critical issue is whether a company which causes a bank to be chartered prior to January 1, 1982, but does not acquire the bank’s shares until after that date, “indirectly owns or controls” the bank’s voting shares during the interim period. Although the company would presumably not have direct voting power during this period, its relationship with the friendly organizers and its agreements or understanding to acquire the bank from them after January 1, 1982, might be deemed indirect ownership or control.

Language in a recent Federal Reserve Board decision approving a bank holding company application suggests that the Illinois Commissioner of Banks and Trust Companies has concluded that the acquiring company would not, prior to consummation of the acquisition in 1982, “indirectly own or control” the shares of the newly-chartered bank and, therefore, would not be in violation of the 1957 Act during the interim period. In Arlington Bancorp, Inc., the Federal Reserve Board approved an application under the Federal Act regarding a series of related transactions pursuant to which Suburban, a de novo bank in Illinois, would be organized prior to January 1, 1982, as a national bank. At least 80% of the shares of Suburban would be acquired by Arlington, a new company which, subsequent to January 1, 1982, would issue up to 14.9% of its voting shares to each of seven other companies. Each of the seven companies—all controlled by a single individual and his immediate family—already controlled an existing bank in Illinois.

The Federal Reserve Board noted that the applicants had “committed,” in accordance with the “advice” of the Illinois Commissioner: first, to organize Suburban prior to January 1, 1982, in order to avoid the restrictions in the 1981 Act on the acquisition of

banks chartered after that date, and second, to delay consummati-
on of the acquisition of the Arlington shares by the other seven 
bank holding companies until after that date “to avoid any possi-
ble violation . . . [of the 1957 Act’s] prohibition against multibank 
holding companies.”17 This “advice” regarding the proposed acqui-
sition suggests that the Commissioner doubted whether the 14.9% 
limitation on the share interest in Arlington to be acquired by 
each of the seven existing bank holding companies would insulate 
the acquisition of Arlington from the 1957 Act’s prohibition on 
multibank holding companies. The 1957 Act, like the Federal Act, 
defines “company” to include a partnership, joint venture or simi-
lar organization,18 and the Commissioner was obviously concerned 
that the seven existing bank holding companies acting in concert 
with each other and with the controlling individual would together 
constitute a multibank holding company in the nature of a part-
nership, joint venture or similar organization.19

Thus, the Commissioner appears to have taken the position that 
even if the seven existing bank holding companies, together with 
the controlling individual, would be a multibank holding company 
upon their acquisition of the Arlington shares, if the acquisition 
did not occur prior to January 1, 1982, such group would not be-
come a bank holding company for purposes of the 1957 Act during 
the interim period. The Commissioner reached this conclusion al-
though principals of the group were to be the bank’s organizers 
and plans were firm for the acquisition to go forward after the ef-
fective date of the 1981 Act.

17. Id. at 3, n.2 of the Board’s Order.
19. Indeed, the Federal Reserve Board noted that, in a similar instance, it had found a 
group of bank holding companies acting together to acquire the shares of a bank holding 
company to be a “company” and a “bank holding company” within the meaning of the 
Federal Act. The Federal Act defines “company” in substantially the same terms as the 
1957 Act. 12 U.S.C. § 1841(b) (1976). The Board observed that the record in connection with 
the Arlington application also “could support a finding that the seven bank holding com-
panies . . . are together a ‘company’ that would become a ‘bank holding company’ upon con-
summation of the transaction,” but concluded that no regulatory purpose under the Federal 
Act would be served by requiring the group to register as a bank holding company under the 
Federal Act, in view of the group’s intention to reorganize as a multibank holding company 
after the effective date of the 1981 Act. The Illinois Commissioner, however, did not have 
the latitude to make a similar concession, since the question of whether the group would be 
a multibank holding company during the interim period was the basic issue under the 1957 
Act.
Can a Company Previously Unaffiliated with Banking Make a Direct Acquisition of a De Novo Bank or Banks in Operation for Less Than Ten Years?

The section 3.05 prohibition against acquiring banks in Illinois which have not been engaged in the banking business for at least ten years applies to acquisitions by any "company," whether or not at the time of such acquisition it is already a bank holding company by reason of its control over another bank. Section 3.05 excepts from this prohibition transactions in which a holding company specially created for the purpose acquires control of a bank pursuant to a phantom bank reorganization or tender offer in which the bank's shareholders, other than those who dissent or do not tender, become shareholders of the holding company. There is no other exception permitting a "company" to acquire a bank which has not operated for the prescribed period, and "company" as defined in the 1981 Act includes "any corporation, business trust, voting trust, association, partnership, joint venture or similar organization" as well as certain other trusts.

Literally construed, section 3.05 would require individuals forming a bank de novo or acquiring an existing bank in operation for less than ten years, who desire to hold the shares of such bank through a corporation, partnership, trust or other "company," first to purchase the shares of such bank as individuals, and then to transfer the shares to the desired "company" in a tender offer or phantom bank reorganization permitted by the language of the exception. Moreover, literally construed, the 1981 Act may prohibit such individuals from formalizing any partnership, voting trust or similar arrangement among themselves prior to such tender offer or phantom bank reorganization; otherwise, a prohibited acquisition by a "company" may be deemed to have occurred.

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20. A phantom bank reorganization is a reorganization pursuant to which a new, nonoperating bank (called a "phantom" or "interim" bank) is chartered as a subsidiary of an existing or newly-formed corporation solely for purposes of combining with an existing, operating bank through a merger, pursuant to which the corporation emerges as the holder of all the outstanding stock of the bank surviving the merger, and the shareholders of the preexisting operating bank receive shares of the corporation in substitution for their shares of the preexisting bank.


It is unlikely that the Illinois legislature intended to prohibit a company in no way affiliated with a bank or bank holding company from directly acquiring a bank in Illinois formed de novo or in operation less than ten years, at least if such company does not, at the time of such acquisition, and cannot until such bank has been in operation for ten years, acquire any other banks in Illinois. Failure to limit the prohibition on “company” acquisitions of recently-chartered banks could unnecessarily complicate the formation and acquisition of new banking enterprises by those not previously in the banking business. To avoid all risk, a lawyer may be driven to structure the acquisition as one by individuals (and companies no one of which will acquire a “control” position) and subsequently transfer ownership to a holding company through a tender offer or phantom bank reorganization.

It remains to be seen whether this unintended statutory overkill can be ameliorated through regulatory and judicial interpretation. Meanwhile, the lawyer must make a judgment in structuring such a transaction. If the lawyer concludes that a company theretofore totally uninvolved in banking may directly acquire a bank less than ten years old without violating the 1981 Act (at least if it is committed not to acquire additional banks until its subsidiary bank has been engaged in banking for ten years), the Federal Reserve may also have to be convinced of the soundness of this conclusion in order to register the company under the Federal Act. It is not inconceivable that the Federal Reserve would look to the Illinois Commissioner or Attorney General for an interpretation.

Can a Bank Holding Company Not Eligible to Be Acquired Because It Controls a Recently-Chartered Bank Acquire an Eligible Bank Holding Company?

Section 3.05 permits a bank chartered after January 1, 1982, and not yet eligible for acquisition (an “ineligible bank”) to create its own holding company. The 1981 Act is silent as to whether a bank holding company formed to control an ineligible bank could acquire control of one or more banks which were chartered prior to the effective date or which have been in operation for at least ten years (“eligible banks”). If the eligible banks are subsidiaries of a single bank holding company, that company would be prohibited by section 3.05 from acquiring the ineligible bank or its holding company. However, the 1981 Act does not expressly prohibit the parent of the ineligible bank from acquiring the parent of the eli-
If an eligible bank or its holding company causes the formation of an ineligible bank and its holding company, a court might well hold a proposed acquisition of the eligible by the ineligible holding company to be an unlawful attempt to circumvent the prohibition on acquisition of a recently-chartered bank. Even if the eligible bank does not cause the formation of the ineligible bank, a determination that the nominal acquiree is in fact the acquirer could invalidate the acquisition. For example, if a small holding company absorbs through merger a large holding company, and the shareholders of the large company emerge from the transaction as the controlling shareholders of the resulting corporation, a bank regulator or court would probably view the nominal acquiree to be in fact the acquirer. Absent a showing that the eligible bank or its holding company is in fact the acquirer, or that it caused the acquirer to be created, the acquisition of eligible banks or their holding companies by a holding company lawfully controlling an ineligible bank may not be precluded by the 1981 Act.

If a Bank Receives a New Charter in a Charter Conversion or Phantom-Bank Conversion to Holding Company Form, Will it be Deemed for Purposes of the 1981 Act to have been Chartered on the Date of the Abandoned Charter or of the New Charter?

If an eligible bank converts from a national to a state bank or from a state to a national bank, it will receive a new charter. Under section 3.05, does it continue to be a bank eligible to be acquired at any time or does it become ineligible until it engages in banking for ten years from the date of its new charter? Clearly the Illinois General Assembly did not intend a charter conversion to transform an eligible bank into an ineligible bank. Undoubtedly the bank regulators and courts, applying a “tacking” approach, will consider the bank to have been chartered as of the date of the

23. This assumes, of course, that the parent of the eligible bank does not also control an ineligible bank. See note 24 infra.

24. Any holding company, which in addition to controlling eligible banks also controls an ineligible bank, would itself be ineligible for acquisition until the ineligible bank is divested or becomes eligible by operating for ten years.

25. In this country's dual banking system, one of the options available to a bank is to convert from a national to a state charter, or from a state to a national charter, in order to avail itself of any advantage which it may discern in one or the other statutory or regulatory framework. The National Bank Act and the Illinois Banking Act each permit the rechartering of a bank previously chartered under the other statute. 12 U.S.C. § 214a (1976); Ill. ANN. STAT. ch. 17, ¶ 327 (Smith-Hurd, 1981).
abandoned charter in determining whether it was chartered prior to January 1, 1982, or whether it has engaged in banking for at least ten years from the date it was chartered.

A "tacking" approach will undoubtedly also be taken where an eligible bank converts to holding company form through a phantom bank reorganization in which the resulting bank operates under a new charter. Section 3.05 expressly excludes from its prohibition on acquisition of recently-chartered banks the acquisition of a newly chartered bank resulting from a phantom bank reorganization in which a bank converts to holding company form by merging into an interim bank subsidiary of a newly-formed holding company. The 1981 Act is silent, however, as to whether the resulting bank and its new holding company are eligible for immediate acquisition or cannot be acquired until the bank has operated for a period of ten years from the date of the bank's new charter. Again, the bank regulators and courts will undoubtedly look to the date of the eligible bank's original charter in determining whether the resulting bank was chartered before January 1, 1982, or whether it has engaged in banking for at least ten years from the date it was chartered.

Would an Acquiring Company Violate Section 3.05 by Creating a Newly-Chartered Interim Bank and Merging It with an Existing Bank in Order to be Assured of 100% Control of the Existing Bank?

"Tacking" would also seem appropriate where an unaffiliated holding company seeks to acquire an eligible target bank through a phantom bank reorganization. A bank holding company seeking to consummate a friendly acquisition of an eligible target bank may not be able to enter into a stock purchase agreement with each of the target bank's shareholders either because of their number or because a minority are known to be unwilling to sell on the terms offered. The holding company, however, may be reluctant to proceed with the acquisition unless it is assured of 100% control of the target bank upon consummation of the acquisition. Because neither a negotiated purchase nor a tender offer is likely to pro-

26. The holding company would normally prefer 100% control to ensure flexibility in accommodating the subsidiary bank's dividend policy to the holding company's financial needs and objectives (without risk of conferring a bonanza on minority shareholders if an extraordinary dividend is declared) and to avoid possible disagreements with the minority over the conduct of the subsidiary's business or the allocation of opportunities and expenses among the constituent entities in the holding company system.
duce the result desired by the holding company, an alternative method of consummating the acquisition must be found.

In order to assure 100% control, the holding company may desire to proceed with a phantom bank acquisition of the target bank. Under this procedure, the holding company would cause an interim bank to be chartered as its subsidiary. An agreement of merger would be entered into pursuant to which the target bank agrees to merge with the interim bank. The merger agreement would provide that the shareholders of the target bank would receive, upon consummation of the merger, cash or securities of the holding company, or both. If the proposed merger is approved by the required percentage of the target bank's shareholders, the merger would be consummated and the holding company would own all of the shares of the surviving bank. If any of the shareholders of the target bank who voted against the merger exercise dissenters' rights, their sole remedy would be to receive cash in an amount equal to the fair value of their shares immediately before the merger. They could not elect to continue as minority shareholders of the surviving bank.

If the interim bank is chartered after January 1, 1982, and is the survivor of the merger, the acquisition may arguably be prohibited by the provisions of section 3.05 precluding the acquisition of banks in operation for less than ten years. It is difficult to believe, however, that the Illinois General Assembly could have intended to preclude the acquisition of a bank chartered before January 1, 1982, or in operation for more than ten years, solely because the acquisition is accomplished by means of a phantom bank merger. Nevertheless, because section 3.05 is silent as to a third-party acquisition of a bank through a phantom merger, whereas it contains an express exclusion for a phantom bank restructuring into a holding company owned by the same shareholders, “tacking” presents a more difficult problem with regard to a phantom bank acquisition than it does with regard to a charter conversion or change to holding company form.

Because the General Assembly was obviously concerned with the date of chartering and the period of operations of the target rather than the interim bank, no legislative purpose would be served by reading the prohibition to preclude acquisition of the resulting bank in a phantom merger acquisition if the resulting bank retains the charter of the interim rather than the target bank. The purpose of the operating period limitation in section 3.05 is to prohibit a bank holding company from expanding de novo, not to inhibit
use of a merger technique for obtaining 100% control of a bank in Illinois which has operated for ten years or was chartered and in operation prior to January 1, 1982. There is no suggestion in the legislative history or in the principal operative provisions of the 1981 Act of any legislative interest in limiting the method of bank acquisitions to negotiated purchases and tender offers. Moreover, section 28 of the Illinois Banking Act,27 which provides that a “resulting state or national bank shall be considered the same business and corporate entity as each merging bank or [in the case of a charter conversion] the converting bank . . .” lends further support for a “tacking” approach under which the resulting bank would be treated, for purposes of the 1981 Act, as a continuation of the target bank. Thus, “tacking” would again seem to be in order in the case of a phantom merger acquisition.

Although “tacking” seems clearly appropriate, a phantom merger acquisition may also be exempted from the ten year operating requirement by section 3.06 of the 1981 Act.28 Under section 3.06, a company’s acquisition of a newly-chartered interim bank in the course of a phantom bank reorganization would be exempted from section 3.05 if, following the acquisition, the interim bank does not “carry on the banking business as a separate bank in Illi-

27. ILL. ANN. STAT. ch. 17, ¶ 335 (Smith-Hurd, 1981).
28. Section 3.06 provides as follows:

Notwithstanding any other provisions of this Act, (a) if any company causes to be chartered any bank in Illinois or acquires control (whether by purchase of stock, merger, consolidation, acquisition of assets or otherwise) of any bank in Illinois theretofore engaged in the banking business and at no time after such company obtains control thereof does the bank, so caused to be chartered or so acquired, carry on the banking business as a separate bank in Illinois maintaining main banking premises in this State, then, neither the acquisition nor the retention by such company of control of such bank shall be unlawful under paragraph (a) of Section 3.02 of this Act and such bank shall not be considered a bank of which such company has control, a bank caused to be chartered by such company, or a bank control of which is acquired by such company, within the meaning of Sections 3.03, 3.04 or 3.05 of this Act; and (b) if any company causes to be chartered, or acquires or at any time has control of, any bank in Illinois, and thereafter such company ceases to have control of such bank, or such bank ceases all of its Illinois banking operations or such bank ceases to carry on the banking business in Illinois as a separate bank in Illinois maintaining main banking premises in this State, then, from and after the time of any such cessation, such company (notwithstanding that it shall theretofore have acquired or had control of such bank, and whether or not it shall have caused the chartering thereof) shall not be considered to have or retain control of such bank within the meaning of Sections 3.03, 3.04 or 3.05 of this Act.

The above-quoted language may be interpreted to permit the acquisition of an interim bank irrespective of whether the interim bank or the target bank is the survivor of the merger. Under this interpretation, the interim bank, even if it is the surviving bank in the merger, would not be deemed to be "carry[ing] on the banking business as a separate bank in Illinois," because it never had an independent existence as a separate operating institution. Rather, the interim bank is only a structural medium for continuing the previous business of the acquiree bank. Construed literally, however, the language may also mean that the acquisition of the interim bank would only be permissible if, upon the merger, the interim bank ceases to exist and the acquiree bank is the survivor (i.e., if the interim bank is merged into the acquiree bank). This narrow interpretation presumes that if the interim bank is the survivor of the merger, it would then become a bank "carry[ing] on the banking business as a separate bank in Illinois maintaining main banking premises in this State," and hence would not be within the purview of the exemptive language. Although not entirely without merit, this narrow interpretation would appear to be inconsistent with the purpose of section 3.05 and of the 1981 Act generally.

29. Id.

30. The history of the 1981 Act, as well as the apparent purpose underlying the prohibition on acquisition of recently-chartered banks, would appear to reinforce both the "tackling" principle and the broader interpretation of § 3.06. The 1981 Act is a successor to earlier multibank holding company bills sponsored by the Association for Modern Banking in Illinois ("AMBI") and introduced in the Illinois legislature without success in 1973 and later years. Those bills differed in one significant respect from the successful bill, also sponsored by AMBI, which ultimately became the 1981 Act. The earlier bills imposed limits on the number of banks which a bank holding company could acquire during various prescribed periods. See, e.g., Senate Bill 935, introduced in the 78th General Assembly, April 14, 1973; House Bill 2060, introduced in the 79th General Assembly, April 12, 1975; House bill 492, introduced in the 80th General Assembly, February 24, 1977; Senate Bill 1050, introduced in the 80th General Assembly, April 8, 1977; House Bill 1299, introduced in the 81st General Assembly, March 29, 1979.

Language similar in effect to the portion of § 3.06 quoted in the text above appeared in various forms in such bills to ensure, among other things, that in a phantom bank reorganization the acquiring company's acquisition quota would be charged with only one rather than two banks. See, e.g., §§ 7 and 10 of Senate Bill 935 introduced in the 78th General Assembly, April 14, 1973; §§ 7 and 9(c) of House Bill 492 introduced in the 80th General Assembly, February 24, 1977; §§ 3.05, 3.06, and 3.07 of House Bill 1299, introduced in the 81st General Assembly, March 29, 1979. A second purpose for including such language was to ensure that an acquired bank whose main banking premises were, at the time of the acquisition, closed or converted into a limited service facility of an acquiring bank under § 5(15) of the Illinois Banking Act, ILL. ANN. STAT. ch. 17, ¶ 311(15) (Smith-Hurd, 1981), would not be charged against the quota. Language similar to the exemption
Although section 3.05 probably does not prohibit an acquisition through a phantom bank merger in which the interim bank survives, nevertheless, there is sufficient uncertainty that, in the absence of corrective legislation, a careful lawyer might prefer to structure the transaction in a manner not involving an interim bank survivor to a phantom merger.

How can Transactions be Structured to Avoid the Risk that Acquisition of an Interim Bank Surviving a Phantom Merger Would Violate Section 3.05?

If a target bank is already the wholly-owned subsidiary of a holding company which is both eligible and available for acquisition, the transaction can be readily structured so that the interim bank problem will not arise under section 3.05. In these circumstances, the target bank's holding company could be merged with the acquiring corporation or a corporate nonbank subsidiary of that corporation. No interim bank would be needed. The merger would be governed by applicable business corporation statutes, and it would not matter whether it is a forward merger or a reverse merger. However, if the acquisition is for cash and a premium is
offered for depreciable assets of the target bank, a merger with the target bank's holding company would not provide the acquirer with the benefits of a stepped-up tax basis for such assets.33

If the target bank's holding company does not own all of the bank's shares, however, acquisition of the holding company would not produce 100% control of the bank. If the holding company owns less than all of the target's shares, or if the bank does not have a holding company at the time of the proposed transaction, it may be impractical or impossible to transform the bank into a wholly-owned subsidiary of a holding company so that the acquisition can be accomplished through a merger of two business corporations rather than a phantom bank merger.34

The section 3.05 interim-bank problem can also be avoided if it is possible to structure the transaction as a reverse phantom bank merger, although again, in the case of a cash merger in which a premium is offered for depreciable assets, a reverse merger would not provide the acquirer with the benefits of a stepped-up basis for such assets.35 Under this procedure, the acquiring company's newly-chartered interim bank subsidiary would be merged into the target bank. The interim bank would "disappear" when the merger is consummated. No matter how section 3.06 is construed, such a reverse merger would fall within its exemptive language; even under the narrow reading of section 3.06, the interim bank would not survive as "a separate bank maintaining main banking prem-

33. For federal tax purposes, a forward cash merger of the target bank's holding company into the acquiring corporation or its non-bank subsidiary would be treated as an acquisition of the target bank's stock. Rev. Rul. 69-6, 1969-1 Cum. Bull. 104. Although the acquirer's basis for such stock would be equal to the purchase price paid by it, the basis for the bank's assets would be unaffected by the transaction. A reverse cash merger of a non-bank subsidiary of the acquiring corporation into the target bank's holding company would be regarded as an acquisition of the stock of the target bank's holding company. Rev. Rul. 79-273, 1979-2 Cum. Bull. 125. The basis of the target bank's assets would again be unaffected.

34. The exclusion in § 3.05 from the limitation on acquisition of new banks would permit the existing bank to reorganize into holding company form prior to the acquisition. This would not only be time consuming and expensive, however, but tax, regulatory, and other considerations may intervene to prevent or complicate the transaction.

35. In a phantom bank forward cash merger for a price exceeding book value, the resulting bank will receive a stepped-up basis for its assets because the transaction will be treated for federal tax purposes as a sale and purchase of the target bank's assets. Rev. Rul. 69-6, 1969-1 Cum. Bull. 104. In a phantom bank reverse cash merger, the resulting bank would carry over the basis of the acquired bank because the transaction would be treated for federal tax purposes as a purchase of the target bank's stock. Rev. Rul. 79-273, 1979-2 Cum. Bull. 125.
ises in this State."

Would a reverse merger of this kind be permitted under the National Bank Act, where the surviving bank is a national bank, or under the Illinois Banking Act, where it is a state bank? Although the Office of the Comptroller of the Currency ("OCC") has indicated that, under section 215a of Title 12 (the merger section of the National Bank Act), it would deny its approval for a phantom merger in which the target bank rather than the interim bank is the survivor, it would appear that the transaction could be successfully accomplished under section 215 of Title 12 (the consolidation section of the National Bank Act).

This curious difference in treatment by the OCC is a consequence of the National Bank Act's inconsistent treatment of dissenters' rights. Section 215a accords dissenters' rights only to shareholders of the constituent bank which does not survive the merger. If the OCC were to sanction the use of reverse mergers under section 215a, the only shareholders entitled to statutory dis-

36. Under modern state corporation statutes, reverse mergers are routinely permitted, i.e., transactions in which a corporation acquires control of a target company by forming a new "shell" subsidiary and merging it into the target, whose shareholders receive as consideration cash or, in a reverse triangular merger, shares or other securities of the acquiring parent.

37. The OCC, in a publication entitled "Overview and Procedures for an Application to Organize an Interim National Bank," states:

The Comptroller's Office does not accept applications for reverse triangular mergers (i.e., where the interim national bank would be merged into the existing national bank). Therefore, this overview applies only to those applications where the interim national bank is the receiving association in a merger or where an existing national bank proposes to consolidate with an interim [sic] national bank. In such a merger proposal, the resulting national bank will be given the charter of the interim national bank. In consolidation proposals, the resulting bank may take the charter of either the existing national bank or the interim national bank. In all cases the resulting national bank will be given the charter number of the existing national bank.

OCC Document identified as CC 7020 3/81.

In written guidelines regarding the chartering of interim banks in connection with phantom bank reorganizations, the OCC states:

If the proposal involves the merger of an operating national bank or an operating state-chartered bank with an interim national bank that is about to be organized solely for the purpose of facilitating the establishment of a bank holding company, the interim national bank must be the receiving or resulting bank. Therefore, if approved, the resulting bank will have the charter of the interim bank, but may elect to retain the charter number and title of the operating national bank. If the operating bank is state-chartered, a new national bank charter number will be assigned, and the resulting bank's title must contain the word "national."

OCC Document identified as CC 7020-44 3/81 (emphasis in original).

senters' rights would be the shareholders of the interim bank. Since this result would be contrary to the intent of the statute, the OCC, according to its staff, would not authorize a reverse merger under section 215a, even if the merger agreement between the banks reserved to the target bank's dissenting shareholders contractual dissenters' rights identical to those provided for in section 215a.\(^\text{89}\) The staff apparently takes the position that the OCC should not have to make a determination regarding the validity or enforceability of contractual terms designed to preserve dissenters' rights.

Section 215 (the consolidation section), however, which expressly permits a "consolidation" of two banks in which one of the two is the surviving bank, accords dissenters' rights to the shareholders of both banks. If the rationale articulated by the OCC staff is in fact the only reason for the OCC's unwillingness to permit a reverse merger under section 215a, there is no sound basis in logic or policy for an OCC objection to a reverse merger (called a "consolidation") under section 215. The OCC appears to recognize this in its written materials regarding interim banks, which state that "[i]n consolidation proposals, the resulting bank may take the charter of either the existing national bank or the interim national bank."\(^\text{40}\) Moreover, the OCC staff has acknowledged that reverse mergers have been approved under section 215, although there have been few such mergers.\(^\text{41}\)

The Illinois Commissioner's staff has indicated that the Commissioner would probably also permit acquisitions to be effected through reverse phantom bank mergers.\(^\text{42}\) The dissenters' rights provisions of the Illinois Banking Act do not present the difficulties posed by section 215a.\(^\text{43}\)

_In a Contested Takeover, Could a Successful Tender Offer Be Followed by a Phantom Bank Reorganization to Eliminate the_
Remaining Minority Interest?

A company desiring to acquire a bank whose management is hostile to the acquisition may decide to proceed initially with a tender offer to the target bank's shareholders. If the tender offer is successful, the acquiring company may wish to eliminate any remaining minority interest in the bank through use of a phantom bank merger. Section 3.05 exempts from the prohibition on acquisitions of recently-chartered banks a phantom bank reorganization by which a bank converts to holding company form. A phantom bank merger to eliminate minority shareholders, on the other hand, is in the nature of an acquisition rather than a conversion to holding company form, and would not qualify for the exemption. In order for a phantom bank reorganization to come within the language of the exemption, minority shareholders must have the opportunity to become shareholders of the bank holding company created by the reorganization. Since the exemption does not apply, a phantom bank merger to eliminate the minority would present the same interim bank issue under section 3.05 as an acquisition of a target bank by means of a phantom merger.

Additionally, a reorganization accomplished in order to eliminate a minority may present special regulatory problems. The OCC has to date been unwilling to permit a phantom bank reorganization to be used for the purpose of eliminating a minority. Is this reluctance misplaced when an unaffiliated acquiring company discloses in tender offer documentation an intent to proceed with a phantom bank reorganization as a second step following the acquisition of control through the tender offer? The OCC currently has under review its position regarding phantom bank reorganizations, and a written statement of policy may be forthcoming.

44. The § 3.05 exemption requires that in a phantom bank reorganization to restructure an existing bank into holding company form, the shareholders of the new holding company, and their respective percentage shareholdings, immediately following the reorganization be substantially identical to the shareholders, and their respective percentage shareholdings, of such bank immediately before the reorganization, except to the extent that the bank's shareholders exercise statutory dissenters' rights. The language does not expressly require that the minority shareholders be offered the same class of stock which the controlling shareholder would receive. It is therefore conceivable that a reorganization could be effected under the 3.05 exemption in which the controlling shareholder receives common stock and the minority shareholders receive preferred stock, but it is by no means clear that this could be accomplished.


46. Id. Mr. Kuruczza informed the writer that the new policy statement may take the
The Illinois Commissioner's staff advises that over the years it has had only two applications for phantom bank reorganizations proposed for the sole purpose of eliminating minority shareholders. Both applications were turned down by the Commissioner. The Commissioner's office is currently reassessing its position regarding such transactions.

**GEOGRAPHICAL LIMITATIONS**

The 1981 Act divides the State of Illinois into five regions, which are shown on the map of Illinois set forth in the Appendix to this article. The Act prohibits a bank holding company from acquiring, on or after January 1, 1982, direct or indirect control of position that phantom bank reorganizations in which a minority interest is eliminated would be permissible only if, in addition to the desire to eliminate the minority, there is a "valid business purpose" for the reorganization. He expressed doubt that, if the OCC were to impose a business purpose rule, advance notice in the tender offer materials of intent to effect a second step phantom bank reorganization would alone satisfy the requirement.

Courts have engrafted business purpose requirements onto various state corporation laws, but have been singularly unsuccessful in giving them meaningful or consistent content. A number of jurisdictions have held that a valid business purpose must exist for a going private merger, and that a majority shareholder may not effect such a merger for the sole purpose of freezing out minority shareholders. See, e.g., Bryan v. Brock & Blevins Co., 490 F.2d 563, 570 (5th Cir. 1974) (citing Georgia law); Singer v. Magnavox Co., 380 A.2d 969, 980 (Del. 1977); Tanzer Economic Assoc., Inc. Profit Sharing Plan v. Universal Food Specialties, 87 Misc. 2d 167, 383 N.Y.S.2d 472, 479, 482-83 (Sup. Ct. 1976). There is considerable disagreement among the courts and commentators, however, as to what constitutes a valid business purpose. The Delaware Chancery Court, for example, indicated in Young v. Valhi, 382 A.2d 1372, 1377 (Del. Ch. 1978), that tax savings and the elimination of potential conflicts of interest are not proper business purposes. In New York, the rule appears to be contrary. See Schulwolf v. Cerro Corp., 86 Misc. 2d 292, 380 N.Y.S.2d 957 (Sup. Ct. 1976) (upholding a merger purportedly made for the purpose of consolidating the two corporations' tax returns and avoiding conflicts of interest in intercompany transactions). Both Delaware and New York courts have suggested that a going private merger can be justified on the ground that it will reduce the costs and liabilities incident to public status under the federal securities laws. See Temple v. Combined Properties Corp., 410 A.2d 1375, 1378-79 (Del. Ch. 1979); Tanzer Economic Assoc., Inc. Profit Sharing Plan v. Universal Food Specialties, 87 Misc. 2d 167, 383 N.Y.S.2d 472, 483 (Sup. Ct. 1976). Former SEC Commissioner A. A. Sommer, Jr., however, has taken the position that the avoidance of such costs and liabilities would not constitute a valid business purpose. "'Going Private': A Lesson in Corporate Responsibility" (Nov. 14, 1974) (unpublished address in Notre Dame Law School Library), reprinted in [1974] Fed. Sec. L. Rep. (CCH) ¶ 80,010; accord, Berkowitz v. Power/Mate Corp., 137 N.J. Super. 36, 342 A.2d 566, 571 n.4 (Ch. Div. 1975) (dictum).

47. Conversation with Corrine J. Gieseke, Legal Counsel, Illinois Commissioner of Banks and Trust Companies (October, 1981).
48. Id.
49. Id.
51. See Appendix A infra at 81.
banks in Illinois located in more than two regions. More specifically, section 3.04 permits a bank holding company to acquire direct or indirect control only of banks in Illinois located in its home region and in not more than one contiguous region. Since regions I and V are each contiguous to only one other region, only holding companies located in regions II, III and IV have a choice as to the second region in which they make acquisitions. "Bank holding company," as used in the 1981 Act, includes one-bank as well as multibank holding companies.

**Illinois and Out-of-State Bank Holding Companies**

The geographical limitations imposed by the 1981 Act on bank holding companies vary according to whether the operations of a holding company's banking subsidiaries are principally conducted in Illinois ("Illinois bank holding companies") or outside of Illinois ("out-of-state bank holding companies"). In determining the state where the operations of a holding company's banking subsidiaries are principally conducted, section 3.07 provides that deposits shall be used as the measure. Why deposits are used for this purpose, whereas assets are used as the measure for all other purposes relating to the geographical limitations, is unclear.

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53. Section 3.04 provides as follows:
   
   On or after the effective date of this amendatory Act enacted by the 82nd General Assembly, no bank holding company or subsidiary thereof may acquire control of, directly or indirectly, an existing bank or banks except a bank or banks whose main banking premises are located within the banking region designated by the bank holding company in accordance with the provisions of Section 3.03 or Section 3.07 of this Act or in a banking region contiguous to said region. If more than one banking region is contiguous to the banking region designated by the bank holding company under Section 3.03 or Section 3.07 of this Act, the bank holding company may choose one of such contiguous banking regions in which to acquire control of a bank or banks. No bank holding company may acquire control of a bank or banks in more than two banking regions. For purposes of this Section, a bank in Illinois shall be deemed to be in the banking region in which its main banking premises are located.

55. See Appendix A infra at 81.
56. Section 2(d) of the 1981 Act, **ILL. ANN. STAT.** ch. 17, ¶ 2502(d) (Smith-Hurd-1981).
57. The geographical limitations applicable to Illinois bank holding companies are found in §§ 3.01, 3.03 and 3.04. Section 3.07 establishes modified rules for out-of-state bank holding companies. Nevertheless, §§ 3.01, 3.03 and 3.04 presumably apply also to out-of-state bank holding companies to the extent not inconsistent with § 3.07.
Home Regions

Under section 3.03, an Illinois bank holding company is deemed to be located in the region in which the main banking premises of the largest bank in Illinois (measured by total banking assets) controlled by such company are located. Curiously, in the event of a combination of two or more bank holding companies, section 3.03 provides that the resulting company is deemed located not in the region where its largest controlled bank is located, but rather in the home region of the largest of the combining bank holding companies as measured by total banking assets. The reason for this apparent inconsistency is unclear. Moreover, if a holding company resulting from a merger is deemed located in a region other than that where its largest controlled bank is located, and that bank is later divested or closed, section 3.03 produces an additional anomaly. That section provides that if a bank in Illinois, which shall have been the largest such bank controlled by a bank holding company, shall cease to be so controlled or discontinue the banking business, the company's home region shall thereafter be the region in which the largest bank in Illinois which continues to operate under the company's control is located.

Although the applicable language of section 3.07 (indeed, most of section 3.07) defies interpretation, it would appear that an out-of-state bank holding company which controls banks in Illinois located in more than one region may select as its home region the region in which any one of such banks is located.57

A bank holding company is required to notify the Commissioner of its home region within 30 days after the effective date of the Act or within 30 days after it becomes a bank holding company, whichever is later.58 Thereafter, it is required to give notice to the Commissioner of any change in its home region within 30 days after the event resulting in such change.59

Prohibition of Out-of-State Bank Holding Companies and Grandfathering of Those in Existence

Section 3.07 permits an out-of-state bank holding company to

57. Section 3.07 provides in part that, "[f]or purposes of this Act, any [out-of-state] ... bank holding company shall be deemed to be located in the banking region in which such bank holding company owns or controls a majority of the voting shares of a bank or banks in Illinois. ILL. ANN. STAT. ch. 17, § 2510 (Smith-Hurd, 1981).
59. Id.
control a bank or banks in Illinois only if, on December 31, 1981, it is a registered bank holding company under the Federal Act and lawfully controls at least two banks in Illinois. Thus, out-of-state bank holding companies are prohibited by the Act, except for those which lawfully controlled two or more banks in Illinois prior to the effective date of the 1957 Act and were therefore also grandfathered under that Act. To the author's knowledge, there is but one such company, General Bancshares, a Missouri-based corporation which controls several banks in southern Illinois.

Section 3.07 prohibits an out-of-state bank holding company not grandfathered under the 1981 Act from owning more than 5% of the voting shares of any bank in Illinois. Unlike most of the other prohibitions in the 1981 Act, this provision could be interpreted to be retroactive. Under the 1957 Act, a company, whether or not it controlled banks located in other states, could lawfully own up to 14.9% of the voting shares of an unlimited number of banks in Illinois, in addition to controlling 15% or more of the voting shares of one other bank in Illinois. If interpreted and enforced retroactively, the 5% limitation could require an out-of-state bank holding company which lawfully owned shares prior to the effective date of the 1981 Act, to divest a portion of those shares.

Grandfathering of Illinois Multibank Holding Companies

Although specific with regard to out-of-state multibank holding companies, the 1981 Act is not specific regarding the grandfathering of Illinois multibank holding companies in existence on the effective date. Under section 3.03, each Illinois bank holding company “in existence and controlling one or more banks in Illinois” on December 31, 1981, is deemed located in the region where the largest bank in Illinois controlled by such company is located. This suggests that there may be in existence on that date Illinois multibank as well as one-bank holding companies. It is unlikely that there will be in existence on that date any corporations which are Illinois multibank holding companies, but

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61. It is conceivable that there presently exist corporations which were also in existence on the effective date of the 1957 Act and then owned two or more banks in Illinois. If so, they were grandfathered under the 1957 Act. Such corporations, however, would long ago have been required to register under the Federal Act, and the writer is unaware of any which have done so. In any event, any corporation which was an Illinois multibank holding company grandfathered under the 1957 Act, if it exists on December 31, 1981, also will be grandfathered under the 1981 Act, the prohibitions of which apply only to acquisitions on or

it is entirely possible that there may then exist noncorporate Illinois multibank holding companies. Although individuals, whether acting alone or (subject to certain exceptions) in concert, would probably not constitute a "company" under the 1957 Act, it is possible that "chain-banking" arrangements currently exist in Illinois, whereby a "company" has been inadvertently created through use of a formalized partnership, joint venture, voting or similar arrangement, or by reason of joint action by centrally controlled corporate affiliates and their principals.62

To the extent that there are such inadvertent Illinois multibank holding companies in existence on December 31, 1981, it is conceivable that they will be grandfathered under the 1981 Act even though they were unlawful under the 1957 Act when created. Unlike section 3.07, which grandfathers an out-of-state bank holding company only if it lawfully controls banks in Illinois on December 31, 1981, the provisions of the Act inferentially grandfathering pre-existing Illinois multibank holding companies are not limited to companies which were lawful prior to the effective date.63

The 1981 Act does not require a grandfathered Illinois or out-of-state holding company to divest banks in Illinois controlled by it prior to the effective date, even though such banks are located in

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62. The Federal Reserve Board and its staff have taken the position that, to be considered a "company" under the Federal Act, a joint arrangement must be something more than individuals acting in concert. In general, there must be a partnership, joint venture, business or other long-term trust, voting agreement or similar arrangement formalized by written agreement. In some cases, however, the Board has found a "company" in the absence of such a written agreement, usually where there is joint action by the members of a corporate group with unified control, such as the group in Arlington Bancorp, Inc. See text accompanying notes 16-19 supra. Neither the courts, nor the Illinois Attorney General or the Commissioner, has interpreted the word "company" in the context of the 1957 Act. In view of the similarity of the 1957 and 1981 Acts to the Federal Act in this regard, it is probably fair to assume that if the issue were to arise under the 1957 or 1981 Act, the courts or Illinois officials would take a position not unlike that of the Federal Reserve Board. It is perhaps noteworthy that, to date, there has been relatively little enforcement activity by the Board regarding failure of partnerships, joint ventures, or trusts to register as bank holding companies under the Federal Act. Similarly, the author is not aware of any judicial or administrative action in Illinois with respect to noncorporate bank holding companies under the 1957 Act.

It is also conceivable that an entity organized in corporate form might be an inadvertent "bank holding company." The definition of "bank holding company" in the 1957 Act not only refers to direct "or indirect" control of the requisite number of voting shares of two or more banks, but also includes any company which "controls in any manner" the election of a majority of the directors of each of two or more banks. The words "indirect" and "control in any manner" could present close factual issues in some cases.

regions other than the two in which such holding company is permitted to expand after January 1, 1982. Neither does the 1981 Act condition acquisitions of additional banks on divestiture of banks located in regions other than the home region or a contiguous region. Thus, if on January 1, 1982, an Illinois bank holding company controls three banks, one in Chicago (Region I), one in Peoria (Region III), and one in Springfield (Region IV), it would be required to designate as its home region the region in which the largest of such banks is located. The company could thereafter acquire, without any obligation to divest any of the original three banks, additional banks located in its home region and in not more than one contiguous region. If, in the above example, the Chicago bank is the largest, Region I would be the home region, and the holding company could, after January 1, 1982, acquire additional banks located in Region I or II. Thus, after the effective date, it could control banks in Regions I, II, III and IV, although it could not expand by acquisition of additional banks in Regions III and IV.

If the multibank holding company referred to in the foregoing example is a noncorporate "company" in the nature of a partnership, joint venture, or trust, it will be faced with an interesting legal question. Should it file a home region notice of the kind which bank holding companies existing on the effective date are required to file with the Commissioner not later than January 31, 1982? If it does, it will probably be conceding that it was an unlawful bank holding company under the 1957 Act.

**Purchase of Additional Shares of Controlled Banks**

Section 3.07 also provides that an out-of-state bank holding company which, on December 31, 1981, lawfully holds a majority of the voting shares of any bank or banks in Illinois, may continue to own such shares and may acquire additional shares of such banks. This provision would permit acquisitions of additional shares of banks located in regions other than those in which such a company could expand by acquisition of additional banks in Illinois.

Although there is no similar provision regarding acquisition by an Illinois bank holding company of additional shares of a bank controlled on the effective date but not located in a region within which such company is permitted to expand, the rule for Illinois companies is probably at least as favorable. An Illinois bank hold-

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64. *Id.*
ing company’s acquisition of further shares of a bank which it already controls would not cause the company to “acquire control” of such bank, and consequently such acquisition would not violate section 3.04 of the 1981 Act. 65

**ACQUISITION OF OUT-OF-STATE COMMERCIAL BANKS**

Section 3.04 provides that, on or after the effective date of the 1981 Act, “no bank holding company . . . may acquire control of . . . an existing bank or banks” except for banks located in its home region and not more than one contiguous region. This prohibition is not, by its terms, limited to any “bank or banks in Illinois” as are most of the other provisions of the 1981 Act. Does this mean that a bank holding company subject to the 1981 Act cannot acquire banks located outside of Illinois? In view of the current debate over the wisdom of federal statutes prohibiting acquisition of banks located outside a holding company’s home state, particularly financially troubled banks, this may not be a moot question. 66

The failure to limit the geographical limitation of section 3.04 to acquisition of banks in Illinois should not foreclose a bank holding company subject to the 1981 Act from acquiring banks located in other states. The operative prohibitions of the 1981 Act are in section 3.02, and the prohibitions on acquisition in section 3.02 refer only to banks in Illinois, not to banks located out of state. Although section 3.02 declares unlawful a wide array of acquisition transactions, it permits substantially all acquisitions which are not prohibited by sections 3.04 or 3.05. Thus, although sections 3.04 and 3.05 are themselves phrased as prohibitions, they are strange prohibitions, indeed, as they appear only to narrow, and not to broaden, the prohibitions set forth in section 3.02. Moreover, the prohibition in section 3.04, if read literally, would apply to bank holding companies subject to the Illinois Act whether or not they

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65. Since such acquisition of further shares would be permissible under § 3.04, it would not violate § 3.02(a)(3). Indeed, since § 2(d) of the 1981 Act defines “control” to include situations in which a company owns less than a majority of voting shares (ILL. ANN. STAT. ch. 17, ¶ 2502(d) (Smith-Hurd, 1981)), an Illinois bank holding company might be able to argue that it can lawfully acquire additional shares of “controlled” banks in which it did not have a majority interest at the effective date, even though such banks are not located in its home or applicable contiguous region. There is a significant risk, however, that a court would reject such an argument.


67. Opponents of the so-called “Douglas-Amendment” to the Federal Act, 12 U.S.C. § 1842(d)(1) (1976) are becoming more vocal, and the possibility has become real that the age of interstate banking is close at hand, at least within circumscribed limits.
are Illinois bank holding companies. It is most unlikely that the Illinois General Assembly intended to prohibit out-of-state bank holding companies from acquiring banks located outside of Illinois.

**ANTITRUST CONSIDERATIONS: IMPACT OF THE 1981 ACT**

The 1981 Act does not prohibit or restrict banking acquisitions which are or may be anticompetitive. Rather, the competitive effects of an acquisition permitted by the 1981 Act will be tested under section 7 of the Clayton Act and section 3(c)(2) of the Federal Bank Holding Company Act. Nevertheless, the 1981 Act's geographical limitations and prohibition of expansion through de novo entry or acquisition of recently-chartered banks should prove to be important contextual factors, together with the Illinois prohibition on branch banking, in the competitive assessment of bank acquisitions in Illinois.

The Federal Bank Holding Company Act, like the Bank Merger Act, requires the reviewing banking agency to make a two-step analysis of a contemplated bank merger. First, the agency must determine whether the effect of the acquisition "in any section of the country may be substantially to lessen competition, or tend to create a monopoly ...." Second, if such an effect is found to be reasonably likely to result, the agency must determine whether

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73. Id. The Bank Merger Act adopts the same standard. 12 U.S.C. § 1828(c)(15)(B)(1976). This standard is identical to that included in § 7 of the Clayton Act, 15 U.S.C. § 18 (1976). Additionally, the Federal Bank Holding Company Act, 12 U.S.C. § 1842(c)(1) (1976), forbids approval of the contemplated acquisition if it would result in monopoly or is part of an attempt to monopolize, as does the Bank Merger Act, 12 U.S.C. § 1828(c)(5)(A). Thus, the two acts adopt the same standard of illegality that is incorporated in § 2 of the Sherman Act, 15 U.S.C. § 2 (1976). See United States v. Connecticut Nat'l Bank, 418 U.S. 656, 668-71 (1974). Therefore, presumably the same principles govern administrative review by banking agencies under the Bank Holding Company Act and Bank Merger Act that apply to the judicial consideration of a case brought by the Department of Justice under § 7 of the Clayton Act, or under § 2 of the Sherman Act. See Decision, 91 BANCING L. J. 64 (1974). The Illinois antitrust statute, which would also apply to acquisitions of banks in Illinois pursuant to the 1981 Act, was modeled upon and, as interpreted by the courts, is similar in effect to the Sherman Act. ILL. REV. STAT. ch. 38, ¶ 60-1 et seq. (1979). The Illinois statute is therefore not discussed separately in this article.

74. Only those acquisitions posing a reasonable probability of substantially lessening competition have been found to violate § 7 of the Clayton Act. Brown Shoe Co. v. United
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."  

Although there have been numerous administrative and judicial interpretations of these laws as applied to bank acquisitions, the discussion in this article of past decisions will be limited to a brief exploration of the principal bank acquisition decisions of the United States Supreme Court. Additionally, the likely effects of the 1981 Act on the application of the antitrust laws to the acquisition of banks in Illinois will be discussed.

Determining the Relevant Geographic Market

In order to determine whether an acquisition is likely to affect competition adversely, it is first necessary to determine the relevant markets in which competition will be affected by the acquisition. Definition of the relevant market is, of course, frequently outcome-determinative in the assessment of a proposed acquisition under the standards of section 7 of the Clayton Act. The more broadly the market is defined, the smaller the market shares the constituent banking entities will hold; the smaller the market shares, the less likely it is that a court or regulator will prohibit the acquisition on the ground that its "effect . . . may be substantially to lessen competition." Conversely, if the relevant market is narrowly defined, the constituent entities may not be considered to be in direct competition, and a challenge premised upon the theory of potential competition would not be likely to succeed.

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75. 12 U.S.C. § 1842(c)(2) (1976). The "convenience and needs" defense is available only if the acquisition is deemed anticompetitive under the standard analogous to that of § 7 of the Clayton Act, but not anticompetitive under the standard analogous to § 2 of the Sherman Act. In United States v. Third Nat'l Bank, 390 U.S. 171, 192 (1968), the Supreme Court held that in assessing the "convenience and needs" of the community, means alternative to the merger should be considered. Additionally, in United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 372 (1963), the Supreme Court determined that the "convenience and needs" assessed should be those in the same geographic market as that used in assessing the anticompetitive effect of the acquisition.

76. The potential competition theory relates to geographical market extension acquisitions involving parties operating in the same product market but not in the same geographic market, or to product market extension acquisitions, involving parties operating in the same geographic market but not in the same product market. Essentially, the theory is premised on the desirable effects a perceived potential entrant to a market will have on the competitive practices of firms operating within the market, and on the belief that actual entry of the acquirer into the market through de novo entry or a foothold acquisition (acquisition of an
Direct Competition

In the landmark 1963 case of United States v. Philadelphia National Bank, in which section 7 of the Clayton Act was held to be applicable to bank mergers, the United States Supreme Court for the first time articulated guidelines governing the geographic market in which the likely effects of a proposed bank acquisition would be assessed. The proper inquiry, according to the Court, “is not where the parties to the merger do business or even where they compete, but where, within the area of competitive overlap, the effect of the merger on competition will be direct and immediate.”

The Supreme Court concluded that since locational convenience is a critical factor in banking, the relevant market is the local market within which it is practicable for average bank customers to turn for banking services. Such customers, according to the

existing competitor so small that it is equivalent to expanding de novo will reduce concentration and enhance competitive market performance. See United States v. Falstaff Brewing Corp., 410 U.S. 526 (1973); FTC v. Proctor & Gamble Co., 386 U.S. 568 (1967).


80. 374 U.S. at 357.

81. Id. at 357-59.
Court, are those neither so large that they can readily shop outside local markets for banking services, nor so small that they would be unlikely to select any bank other than the closest one.\textsuperscript{82} The Court's apparent concern was to avoid standards which might, in effect, exempt the banking industry from constraints on anticompetitive acquisitions. If the relevant market were international, national or even regional in scope, the market shares of even the very largest banks would be so small that virtually no bank acquisition would be anticompetitive. If, on the other hand, each bank's relevant geographical market were only its immediate neighborhood, it would be relatively infrequent that any two banks would be in the same market.

In \textit{Philadelphia National Bank}, the merging banks had assets of more than $1 billion and $750 million respectively.\textsuperscript{83} The Court determined the relevant geographical market to be the four-county Philadelphia metropolitan area.\textsuperscript{84} The banks were the second and third largest in that market, the former being the 21st largest in the United States.\textsuperscript{85} The bank resulting from the proposed merger would have controlled at least thirty percent of the commercial banking business in the market.\textsuperscript{86} The merger would have caused the combined market share of the two largest banks in the market to rise from forty-four percent to fifty-nine percent, a significant increase in concentration.\textsuperscript{87} The Court held that the merger would violate section 7 of the Clayton Act, because its effect might be substantially to lessen competition in the relevant market.\textsuperscript{88}

Again, in \textit{United States v. Connecticut National Bank},\textsuperscript{89} the Supreme Court considered a proposed merger between two relatively large banks, the fourth and eighth largest in Connecticut. The two banks operated in adjoining regions in the southwest portion of

\begin{itemize}
  \item \textsuperscript{82} \textit{Id.} at 361.
  \item \textsuperscript{83} \textit{Id.} at 331.
  \item \textsuperscript{84} \textit{Id.} at 361.
  \item \textsuperscript{85} \textit{Id.} at 331.
  \item \textsuperscript{86} \textit{Id.} at 364.
  \item \textsuperscript{87} \textit{Id.} at 365.
  \item \textsuperscript{88} \textit{Id.} at 371. The Supreme Court concluded:
  Specifically, we think that the merger which produces a firm controlling an undue percentage share of the relevant market, and results in a significant increase in the concentration of firms in that market, is so inherently likely to lessen competition substantially that it must be enjoined in the absence of evidence clearly showing that the merger is not likely to have such anticompetitive effect.
  \textit{Id.} at 363.
  \item \textsuperscript{89} 418 U.S. 656 (1974).
\end{itemize}
the state, one in New Haven and nearby towns and the other in Bridgeport and nearby towns.\textsuperscript{90} As part of the merger plan, the banks agreed to divest themselves “of a sufficient number of offices in the four-town area [located between Bridgeport and New Haven] to render insignificant the degree of overlap of the areas of actual operation.”\textsuperscript{91} “Accordingly,” the Court stated, “the case has been presented to us strictly as a geographic market extension merger on the part of both banks.”\textsuperscript{92}

The district court had concluded, in a decision in favor of the banks, that the relevant geographic market was the State of Connecticut.\textsuperscript{93} Reversing and remanding for further findings, the Supreme Court rejected the district court’s market assessment, holding that “the relevant geographic market of the acquired bank is the localized areas in which that bank is in significant, direct competition with other banks, albeit not the acquiring bank.”\textsuperscript{94} The Court conceded that the district court’s task on remand would be difficult, because of the fragmented distribution of banking offices

\textsuperscript{90} Id. at 658.
\textsuperscript{91} Id. at 659.
\textsuperscript{92} Id. Thus, the Supreme Court was presented with an action premised in part upon the theory of potential competition. See note 76 \textit{supra}.
\textsuperscript{93} United States v. Connecticut Nat’l Bank, 362 F. Supp. 240, 281-83 (D. Conn. 1973). In addition, the district court concluded that although New York was not an extension of the Connecticut market, “the influences of the New York banks require serious consideration and analysis” with regard to “the impact of the merger upon competition and its effect in serving the convenience and needs of the community.” Id. at 283. By defining the relevant market as the entire state, the district court appears to have laid the foundation for analyzing the case as one involving direct competition in the large, statewide market, rather than potential competition. The district court’s opinion includes, however, an analysis of both potential competition, id. at 286-88, and direct competition, id. at 283-86. Apparently concluding that the district court had never focused on the correct issues, the Supreme Court rejected the district court’s definition of the relevant geographic market, stating:

The State cannot be the relevant geographic market, however, because CNB and FNH are not direct competitors on that basis (or for that matter on any other basis pertinent to this appeal). The two banks do not operate statewide, nor do their customers as a general rule utilize commercial banks on that basis. The offices of the two banks are restricted to adjoining sections of the southwest segment of Connecticut. Although the two banks presumably market a small percentage of their loans to large customers on a statewide or broader basis, it is undoubtedly true that almost all of their business originates locally. For example, “about 88% of CNB’s total deposit business derive[s] from the towns in which CNB has offices.” 362 F. Supp., at 250. As the district court noted in a finding that is inconsistent with its conclusion on the appropriate section of the country, “[c]ommon sense . . . would indicate that the relevant market areas of CNB and FNH generally coincide with where each has established branch offices.”

\textsuperscript{94} 418 U.S. at 667.
of the two banks resulting from the Connecticut branching statute which had “created a checkerboard of ‘open’ and ‘closed’ towns.”

Noting that the Government could not rely, without more, on Standard Metropolitan Statistical Areas, or on town boundaries, to define the relevant geographic markets of the two banks, the Court indicated that the Government on remand would be required to produce evidence supporting geographical local market definitions based on economic realities.

In *Lexington Bank*, a case involving relatively small banks operating in small metropolitan communities, the Supreme Court defined the relevant geographic market more narrowly than it had in *Philadelphia National Bank*. The banks involved in the challenged merger were the first and fourth largest in Lexington, Kentucky, with assets of $65 million and $21 million respectively. The bank resulting from the merger would also have been relatively small, although it would have been larger than all of the remaining banks in Fayette County combined. Less than three percent of the aggregate dollar deposits of each bank were held by depositors located outside of Lexington. Except for large, national concerns, most business customers in the area were “restricted to the Fayette County banks for their working capital loans” and non-Lexington banks did a “negligible amount of business in the county.” The Supreme Court found the relevant geographic market to be Fayette County. Concluding that substantial competition in this market would have been eliminated by the merger, the Court held that it was a combination in restraint of trade and in violation of section 1 of the Sherman Act.

In *United States v. Phillipsburg National Bank & Trust Co.*, the merger was not challenged under the Clayton Act, apparently because the Government had brought the *Lexington Bank* case under the Sherman Act prior to the Supreme Court’s decision in *Philadelphia National Bank*, which for the first time applied the Clayton Act to bank mergers. There is no reason to believe that the Court’s definition of geographical market would have differed had the case arisen under the Clayton Act.

95. *Id.* at 669.
96. 418 U.S. at 669-70.
98. *Id.* at 668.
99. *Id.* at 676 (Harlan, J., dissenting).
100. *Id.* at 669.
101. *Id.* at 668. Less than 5% of each bank’s depositors were located outside of Lexington.
102. *Id.*
103. *Id.* at 672-73. The merger was not challenged under the Clayton Act, apparently because the Government had brought the *Lexington Bank* case under the Sherman Act prior to the Supreme Court’s decision in *Philadelphia National Bank*, which for the first time applied the Clayton Act to bank mergers. There is no reason to believe that the Court’s definition of geographical market would have differed had the case arisen under the Clayton Act.
the Supreme Court analyzed the factors relevant to the definition of geographic market when assessing a combination of relatively small banks in a small community. The two combining banks were located in Phillipsburg, New Jersey. The population of Phillipsburg and its bordering suburbs was 28,500, and the population of Easton, Pennsylvania and its bordering suburbs, immediately across the river from Phillipsburg, was 60,000. The metropolitan areas of the two cities in effect constituted “one town.”

All seven banks in “one town” were small, with assets ranging from $13.2 million to $75.6 million. The two combining banks had assets of $23.9 and $17.3 million respectively. They were the two largest of the three banks in Phillipsburg, but only the fourth and sixth largest in “one town.” The resulting bank would have had assets of $41.1 million and would have been the second largest of the six remaining banks in “one town.” The main offices of the two banks were directly opposite one another on the same downtown street. The only branch of one was located across a suburban highway from one of the two branches of the other. Approximately seventy-five percent of the deposits of each of the banks were $1,000 or less, and substantially all of the deposits of each were $10,000 or less. The vast majority of the loans of both banks were in the range of $2,500 or less, and approximately ninety percent of the loans were $10,000 or less. More than ninety percent of the depositors of each bank were residents of “one town,” and of these less than ten percent lived in Easton.

“One town” is part of the Lehigh Valley, which was then a region of 1,000 square miles with a population of 492,000 and served by 38 commercial banks. Although there was considerable mobility among the residents of the Lehigh Valley for social, shopping, and employment purposes, “[c]ustomer preference and conservative banking practice . . . tended to limit the bulk of each . . . bank’s business to its immediate geographic area.”

The OCC approved the merger, defining the relevant geographic market not as “one town,” but rather as most of the Lehigh Valley. Approval was granted despite independent reports from the Federal Reserve Board, the Federal Deposit Insurance Corporation

105. Id. at 354.
106. Id.
107. Id.
108. Id. at 356.
109. Id.
110. Id. at 357.
and the Attorney General finding "one town" to be the relevant market and reporting that the merger would have a significantly harmful effect upon competition in this market. The district court found in favor of the defendant banks in the ensuing litigation, selecting as the relevant geographic market an area approximately four times the size of "one town" with a population of 216,000 and served by eighteen banks.

The Supreme Court reversed, disagreeing with both the district court and the OCC on the selection of the relevant geographic market. The Court selected "one town" as the relevant market, stating:

Commercial realities in the banking industry make clear that banks generally have a very localized business. We observed in Philadelphia Bank . . . that "[i]n banking, as in most service industries, convenience of location is essential to effective competition. Individuals and corporations typically confer the bulk of their patronage on banks in their local community; they find it impractical to conduct their banking business at a distance . . . . The factor of inconvenience localizes banking competition as effectively as high transportation costs in other industries." In locating "the market area in which the seller operates," it is important to consider the places from which it draws its business, the location of its offices, and where it seeks business.

Focusing on the predominance of small customers constituting the banks' clientele, the Court concluded that the banks competed within a radius of only a few miles. Having assessed the competi-

111. Id. at 358. The Bank Merger Act requires the responsible bank regulatory agency, prior to approving an application for approval of a merger transaction, to solicit reports from the Attorney General and the two other federal banking agencies on the competitive impact of the proposed combination. 12 U.S.C. § 1828(c)(4) (1976).
113. 399 U.S. at 362-63. The Justice Department had sought to define the relevant market as metropolitan Phillipsburg only. Nevertheless, it subsequently expressed willingness to "accept 'one town'" as the relevant geographic market. There are indications in the Supreme Court's opinion that, had the Justice Department persevered in the narrower geographical definition, the Court might well have selected only Phillipsburg as the relevant market. Id. at 362-65.
114. The Supreme Court specifically noted:

The localization of business typical of the banking industry is particularly pronounced when small customers are involved. . . . Small depositors have little reason to deal with a bank other than the one most geographically convenient to them. For such persons, geographic convenience can be a more powerful influence than the availability of a higher rate of interest at a more distant, though still nearby, bank. The small borrower, if he is to have his needs met, must often depend upon his community reputation and upon his relationship with the local
tive effect of the proposed merger in this drastically smaller market, the Court concluded that it was "inherently likely to lessen competition substantially."\textsuperscript{115}

The federal bank regulatory agencies, in contrast to the Supreme Court, have adopted a more ad hoc approach to defining the geographic market likely to be affected by a proposed bank combination. With regard to the Federal Reserve Board, this seems incongruous because, according to its former general counsel, the Board has over the years developed a list of standardized geographical markets and "advises prospective applicants to consult their local Federal Reserve Bank in advance of filing to get the latest market delineation."\textsuperscript{116} In a 1981 decision regarding the proposed acquisition of a newly chartered small suburban bank near Chicago by a company affiliated with other banks in Chicago suburbs, the Board found the relevant market to be the "Chicago banking market," which it defined as "approximated by Cook, DuPage, and Lake Counties, Illinois."\textsuperscript{117}

At a recent seminar, a member of the staff of the Federal Reserve Bank of Chicago confirmed the Federal Reserve practice of advising the parties to a proposed bank combination of the Federal Reserve's definition of the market. He acknowledged, however, that with respect to Illinois there is less experience and precedent to draw upon to define geographical markets than in states where

\textsuperscript{115} Id. at 363-64.

\textsuperscript{116} Id. at 367. Summarizing the competitive impact of the proposed merger, the Supreme Court noted:

The combined bank would become the second largest in the area, with assets of over $41,100,000 (19.3\% of the area's assets), total deposits of $38,400,000 (23.4\%), and total loans of $24,900,000 (27.3\%). The assets held by the two largest banks would then increase from 49\% to 55\%, the deposits from 56\% to 65\%, the loans from 49\% to 63\%, and the banking offices from seven to 10. The assets held by the three largest banks would increase from 60\% to 68\%, the deposits from 70\% to 80\%, the loans from 64\% to 76\%, and the banking offices from 10 to 12. In Phillipsburg alone, of course, the impact would be much greater: banking alternatives would be reduced from three to two; the resultant bank would be three times larger than the only other remaining bank, and all but two of the banking offices in the city would be controlled by one firm.

\textsuperscript{116} In contrast, according to one commentator, the OCC and FDIC tend to determine relevant geographic markets case-by-case on the basis of the service areas of the banks involved. Hawke, "Competitive Factors: Review of the 1980 Decisions"; Legal Times of Washington, Vol. III, No. 37, February 23, 1981.

mergers and acquisitions have been more common. He indicated
that applicants who disagree with the Federal Reserve's definition
of the market in their case are welcome to register their objections
and request reconsideration.118

Potential Competition

In United States v. Marine Bancorporation, Inc.,119 the Su-
preme Court addressed at length the potential competition the-
ory120 as a ground for establishing a section 7 violation in bank
acquisition cases. Significantly, the banks involved were located
in the State of Washington, where the prevailing state law relevant
to the proposed merger was similar in several respects to that prevail-

The Government brought an action under section 7 of the Clay-
ton Act, challenging a proposed merger between the second largest
bank in the state, with $1.8 billion in assets, and the ninth largest,
with $112 million in assets.121 The former was based in Seattle, the
latter in Spokane, and neither bank had offices in the home city of
the other. The proposed merger would permit the Seattle-based
bank to operate for the first time as a direct participant in the
Spokane market.122 The Spokane-based bank had seven branch of-
fices in the Spokane metropolitan area, being the third largest in
the Spokane market and holding 18.6 percent of the total deposits
there.123 The three largest banks in the Spokane market controlled
ninety-two percent of the total deposits.124

Under Washington state law, a state bank was prohibited from
branching in any municipality (in which any other bank transacted
business) outside the municipality in which its own home office
was located, except by acquiring an existing bank.125 By virtue of
the McFadden Act,126 this branching limitation also applied to na-
tional banks based in Washington. Washington state law also pro-
hibited a bank, in the absence of consent from the State Supervi-

118. Remarks of David R. Allardice, Senior Economist, Federal Reserve Bank of Chi-
icago, at a seminar presented as part of the Continuing Legal Education Program of the
120. See note 76 supra.
121. 418 U.S. at 606-07.
122. Id. at 605.
123. Id. at 607.
124. Id. at 609.
125. Id. at 610.
sor of Banking, from acquiring or merging with a new bank for a period of at least ten years. In addition, Washington state law prohibited a bank which acquired an existing bank operating in a municipality other than that of the acquiring bank from maintaining branch locations in that municipality in addition to the ones maintained by the acquired bank at the time of the acquisition. Finally, multibank holding companies were prohibited by Washington law.

The Court noted that under a potential competition analysis,

"a market extension merger may be unlawful if the target market is substantially concentrated, if the acquiring firm has the characteristics, capabilities and economic incentive to render it a perceived potential de novo [or foothold] entrant and if the acquiring firm's premerger presence on the fringe of the target market in fact tempered oligopolistic behavior on the part of existing participants in that market."

In other words, the competitive conditions in a concentrated market can be changed in a manner violative of section 7 if a real possibility that a significant potential competitor "waiting in the wings" might come into the market is a deterrent to anticompetitive behavior by the dominant participants in the market, and that possibility is eliminated through merger of the potential competitor with one of such participants.

The Government contended, as a second potential competition theory, that a merger which "eliminates the prospect for a long-term deconcentration of an oligopolistic market that in theory might result if the acquiring firm were forbidden to enter except through a de novo undertaking or through [a foothold] acquisition" violates section 7. The Court acknowledged that it had left this question open in prior potential competition cases.

As a predicate to its analysis, the Court held that "geographic market extension mergers by commercial banks must pass muster under the potential-competition doctrine" but that "the application of the doctrine to commercial banking must take into account

127. 418 U.S. at 610.
128. Id. at 610-11.
129. Id. at 611.
130. Id. at 624-25.
131. Id. at 625.
132. Id. at n.28. The question was left open in United States v. Falstaff Brewing Corp., 410 U.S. 526 (1973).
the unique federal and state regulatory restraints on entry into that line of commerce.”\textsuperscript{133} Moreover, a prerequisite to a successful potential competition challenge, according to the Court, is a finding of “dominant participants in the target market engaging in interdependent or parallel behavior and with the capacity effectively to determine price and total output of goods or services.”\textsuperscript{134} Finally, the Court stated that the Government, in order to be successful in asserting the potential competition theory, must show that there are means available for the acquiring entity to enter the target market through \textit{de novo} expansion or through a foothold acquisition.\textsuperscript{135}

The Court found the Spokane market to be oligopolistic.\textsuperscript{136} Nevertheless, it concluded that, because of the state limitations on branch banking and multibank holding companies, the acquirer could not have been perceived as a true potential competitor “waiting in the wings” under the traditional potential competition theory.\textsuperscript{137}

With respect to the Government’s second theory, the Court held that even if the Government were correct that the acquirer could move into the Spokane market through foothold acquisition, it had failed to prove that the acquirer could have contributed significantly to the deconcentration of that market over time.\textsuperscript{138} The Court noted that two small banks existed in the Spokane market which might be available to the acquirer for foothold entry, but concluded that state law restraints on expansion were likely to preclude the acquirer from becoming a significant competitor in the market following a foothold acquisition.\textsuperscript{139} Because the Govern-

\textsuperscript{133} 418 U.S. at 627.
\textsuperscript{134} Id. at 630.
\textsuperscript{135} Id. at 633.
\textsuperscript{136} Id. at 632.
\textsuperscript{137} Id. at 639-40.
\textsuperscript{138} Id. at 638.
\textsuperscript{139} The Court particularly stressed Washington’s prohibition on branch banking, stating:

[It does not follow that an acquisition of either would produce the long-term market-structure benefits predicted by the Government. Once NBC acquired either of these banks, it could not branch from the acquired bank. This limitation strongly suggests that NBC would not develop into a significant participant in the Spokane market, a prospect that finds support in the record. In 1964, one of the largest bank holding companies in the country, through its Seattle-based subsidiary, acquired a foothold bank with two offices in Spokane. Eight years later this bank, Pacific National Bank, held a mere 2.2% of total bank deposits in the Spokane metropolitan area, an insignificant increase over its share of the market at
ment had failed to show that any means of entry into the market other than the proposed merger would have significant procompetitive effects, the second theory was rejected.\textsuperscript{140}

The Court concluded its opinion with the following guidelines for future courts considering potential competition issues in geographic market extension cases involving banks:

In applying the doctrine of potential competition to commercial banking, courts must, as we have noted, take into account the extensive federal and state regulation of banks. Our affirmance of the District Court's judgment in this case rests primarily on state statutory barriers to \textit{de novo} entry and to expansion following entry into a new geographic market. In States where such stringent barriers exist and in the absence of a likelihood of entrenchment, the potential-competition doctrine—grounded as it is on relative freedom of entry on the part of the acquiring firm—will seldom bar a geographic market extension merger by a commercial bank. In States that permit free branching or multibank holding companies, courts hearing cases involving such mergers should take into account all relevant factors, including the barriers to entry created by state and federal control over the issuance of new bank charters. Testimony by responsible regulatory officials that they will not grant new charters in the target market is entitled to great weight, although it is not determinative. To avoid the danger of subjecting the enforcement of the antitrust laws to the policies of a particular bank regulatory official or agency, courts should look also to the size and growth prospects of the target market, the size and number of banking organizations participating in it, and past practices of regulatory agencies in granting

\hspace{1cm} the date of the acquisition. . . . An officer of this bank, called as a witness by the Government, attributed the poor showing to an inability under state law to establish further branches in Spokane.

\textit{Id.}

140. Specifically, the Court observed:

[The Government] failed to demonstrate that the alternative means offer a reasonable prospect of long-term structural improvement or other benefits in the target-market. In fact, insofar as competitive benefits are concerned, the Government is in the anomalous position of opposing a geographic market extension merger that will introduce a third full-service banking organization to the Spokane market, where only two are now operating, in reliance on alternative means of entry that appear unlikely to have any significant procompetitive effect. Accordingly, we cannot hold for the Government on . . . [the second theory]. Indeed, since the preconditions for that theory are not present, we do not reach it . . . . We reiterate that this case concerns an industry in which new entry is extensively regulated by the State and Federal Governments.

\textit{Id.} at 638-39.
charters. If regulatory restraints are not determinative, courts should consider the factors that are pertinent to any potential-competition case, including the economic feasibility and likelihood of de novo entry, the capabilities and expansion history as well as the structural characteristics of the target market.¹⁴¹

Market extension acquisitions permitted under the 1981 Act are subject to challenge under the potential competition theory. Nevertheless, in light of the Supreme Court’s decision in Marine Bancorporation, the significant limitations on geographic expansion in Illinois would be likely to render such a challenge ineffective.¹⁴²

Determining the Relevant Product Market

In 1963, the Supreme Court in Philadelphia National Bank¹⁴³ held that “the cluster of products (various kinds of credit) and services (such as checking accounts and trust administration) denoted by the term ‘commercial banking’ . . . composes a distinct line of commerce.”¹⁴⁴ The Court observed that “[c]ommercial banks are unique among financial institutions in that they alone are permitted by law to accept demand deposits” and “[t]his distinctive power gives commercial banking a key role in the national economy.”¹⁴⁵

In 1969, the Supreme Court in Phillipsburg¹⁴⁶ reaffirmed Philadelphia National Bank in this regard. It observed:

Philadelphia Bank emphasized that it is the cluster of products and services that full-service banks offer that as a matter of trade reality makes commercial banking a distinct line of commerce. Commercial banks are the only financial institutions in which a wide variety of financial products and services—some unique to commercial banking and others not—are gathered together in one place. The clustering of financial products and services in banks facilitates convenient access to them for all banking customers. For some customers, full-service banking makes possible access to certain products or services that would otherwise be unavailable to them; the customer without significant collateral, for example, who has patronized a particular bank for a variety of financial products and services is more likely to be able

¹⁴¹. Id.
¹⁴². See note 76 supra.
¹⁴⁴. 374 U.S. at 356.
¹⁴⁵. Id. at 326.
to obtain a loan from that bank than from a specialty financial
institution to which he turns simply to borrow money. In short,
the cluster of products and services termed commercial banking
has economic significance well beyond the various products and
services involved.\textsuperscript{147}

In the intervening years, these distinctions have persistently
eroded with the advent of checking privileges for money market
funds, NOW accounts, and share drafts offered by thrift institu-
tions, and with the expansion of statutory lending powers of non-
bank depositary institutions. The Federal Reserve's various com-
putations of the money supply and the mounting confusion over
whether a decrease in the supply of money determined by one
measure can be accounted for by an increase in another measure
are silent testimony to the fact that bank demand deposit services
face fierce direct competition.

In the face of these rapid changes that are restructuring the roles
of financial institutions, the courts and regulators have persevered
in their treatment of commercial banks as competitors in a product
market separate from thrifts and other depository, lending, and
fiduciary institutions when assessing the effects of bank acquisi-
tions on competition. The Supreme Court has predicted, however,
that this may not continue to be appropriate. Although the Court
reaffirmed its position that commercial banking is a separate line
of commerce in \textit{Connecticut National},\textsuperscript{148} it acknowledged that a
large measure of similarity existed between the services marketed
by commercial and savings banks in Connecticut.\textsuperscript{149} Nevertheless,
the Court concluded that the overlap was "not sufficient at this
stage of the development of savings banks in Connecticut to treat
them together with commercial banks."\textsuperscript{150} Although it recognized
that savings banks would soon be able to provide checking account
services which would increase direct competition between savings
and commercial banks, the Court considered it significant that,
even with this new check authority, savings banks would be per-
mitted to have only personal checking accounts, not business
accounts.\textsuperscript{151}

\begin{itemize}
\item \textsuperscript{147} 399 U.S. at 360-61 (emphasis in original).
\item \textsuperscript{149} 418 U.S. at 663.
\item \textsuperscript{150} \textit{Id.} at 664.
\item \textsuperscript{151} \textit{Id.} at 665.
\end{itemize}
Unlike earlier Supreme Court decisions, the court's opinion in Connecticut National foresees a day when commercial banking will no longer be considered the relevant product market, at least in some sections of the country. In light of the accelerated erosion of the lines between commercial banks and other depository and nondepository financial entities in recent years, the position of bank regulatory agencies appears to be moving in this direction. In several recent decisions assessing the competitive effects of bank acquisitions, bank regulators have defined the relevant product market to be commercial banking, but then have "shaded" the market by considering competition from thrift and other nonbanking entities in order to support a determination that the proposed combination would not be likely to substantially lessen competition. Even the Federal Reserve Board has begun to "flirt more brazenly with the idea that competition from thrift institutions should be taken into account in assessing the competitive impact of a commercial bank acquisition." Finally, over the years the lower federal courts have paid increasingly greater attention to the competitive market shares of nonbank competitors when analyzing various product submarkets. In short, the day is probably not far off when the Supreme Court will reassess its position that commercial banking is a separate line of commerce, but that day has not yet arrived.

152. The Supreme Court concluded:

We do not say, and Phillipsburg National Bank ... and Philadelphia National Bank ... do not say, that in a case involving a merger of commercial banks a court may never consider savings banks and commercial banks as operating in the same line of commerce, no matter how similar their services and economic behavior. At some stage in the development of savings banks it will be unrealistic to distinguish them from commercial banks for purposes of the Clayton Act. In Connecticut, that point may well be reached when and if savings banks become significant participants in the marketing of bank services to commercial enterprises. But, in adherence to the tests set forth in our earlier bank merger cases, which we are constrained to follow, we hold that such a point has not yet been reached.

Id. at 666.


The Federal Reserve Board has been the least liberal of the federal bank regulators in permitting expansion through bank acquisitions. Consequently, counsel in other jurisdictions have sought, whenever possible, to structure such transactions as bank mergers or asset acquisitions by banks, rather than holding company acquisitions, so that the OCC or FDIC, rather than the Board, would have final authority to grant or deny the application.156 Branch banking continues to be unlawful in Illinois, however, and the 1981 Act provides the only authority for geographical expansion of full-service banking in Illinois. Thus, counsel dealing with acquisitions of banks in Illinois pursuant to the 1981 Act will not have the luxury of such forum shopping, and applications to the Federal Reserve Board pursuant to the Federal Act will be a standard requirement.


In states where branch banking is permitted, a holding company system can take over a target bank either through a stock acquisition by the holding company which maintains the acquired bank as a separate bank subsidiary, through merger of the target bank with an existing or newly created bank subsidiary of the holding company, or by acquisition of the target bank’s assets by a bank subsidiary. Direct acquisition by the holding company is subject to approval of the Federal Reserve Board under the Federal Bank Holding Company Act, 12 U.S.C. § 1842 (1976). Approval of a merger with, or an acquisition of assets by, a bank subsidiary is governed by the Bank Merger Act, 12 U.S.C. § 1828 (1976). The federal regulator with final decision powers is the principal regulator of the resulting bank, which will be the Comptroller of Currency in the case of a national bank, the Board of Governors of the Federal Reserve System in the case of a state chartered bank which is a member of the Federal Reserve System, and the Federal Deposit Insurance Corporation in the case of a state nonmember bank insured by the corporation. 12 U.S.C. § 1828(c)(2) (1976). Therefore, only those mergers which result in a state bank which is a member of the Federal Reserve System are subject to the principal regulation of the Board.

The provisions of the Bank Merger Act regarding competitive aspects are substantially identical to those of the Federal Bank Holding Company Act, but the OCC, with respect to mergers in which a national bank results, and the FDIC, with respect to mergers in which a state nonmember bank results, have interpreted such provisions with greater leniency than the Board. Hawke, “Competitive Factors: Review of 1980 Decisions,” Legal Times of Washington, Vol. III, No. 37, February 23, 1981. Indeed, in several situations where the Board denied an application on competitive grounds, the parties have restructured the transaction so that it would be subject to the primary jurisdiction of a different federal regulator and then applied and received approval from such regulator. For example, early in 1980, the Federal Reserve Board denied an application by Toledo Trustcorp to acquire Defiance Bank, on the ground that even if market shares were shaded to reflect thrifts, the acquisition would still present substantially adverse competitive effects. In December 1980, the OCC approved the same transaction restructured as a merger between banks, noting that “the presence of aggressive savings and loan associations exerts a procompetitive influence on the commercial banks” in the relevant market. Id.
Under the Board's delegation rules, less sensitive applications to acquire banks in Illinois will be processed by the Federal Reserve Bank of Chicago. The circumstances requiring an application to be processed by the Board of Governors in Washington include the following: (i) the acquirer and acquiree each ranks among the State's ten largest banking institutions in terms of total domestic banking assets, or each holds more than $100 million of total deposits in banking offices in the same local market and together they control over 5% of total deposits in banking offices in that local market; (ii) the application raises a significant policy issue or legal question on which the Board of Governors has not established its position; or (iii) a written substantive objection to the application has been properly made.

The Board has historically sought to play a major discretionary role in shaping the structure of evolving banking markets. To this end, the Board has interpreted the Federal Bank Holding Company and Bank Merger Acts to authorize it to deny, on competitive grounds, applications to acquire banks even where the proposed acquisition would not violate the antitrust laws. However, four federal courts of appeals have reached the opposite conclusion.

Although the special provisions regarding competition set forth in the Federal Bank Holding Company and Bank Merger Acts permit the federal bank regulators, upon a finding that community needs and benefits outweigh anticompetitive considerations, to approve a bank acquisition which, in the absence of such special provisions, would violate the antitrust laws, the courts of appeals are in agreement that such special provisions do not confer authority on the bank regulators to deny on competitive grounds acquisitions permissible under the antitrust laws. The unanimity among the circuits to date on this point would suggest that any denial by the Board on competitive grounds will be reversed on appeal, unless the reviewing court is satisfied that the proposed acquisition would tend substantially to lessen competition in any market within the

160. County Nat'l Bancorporation v. Board of Governors, ___ F.2d ___ (8th Cir. 1981)(en banc); Mercantile Texas Corp. v. Board of Governors, 638 F.2d 1255 (5th Cir. 1981); Mid-Nebraska Bancshares v. Board of Governors, 627 F.2d 266 (D.C. Cir. 1980); Washington Mutual Savings Bank v. FDIC, 482 F.2d 459 (9th Cir. 1973).
meaning of section 7 of the Clayton Act.

Antitrust Role of the Justice Department

The Federal Bank Holding Company Act requires the Board, upon receipt of a company's application to acquire a bank, to notify the bank's principal regulator (in the case of a national bank, the OCC, and in the case of a state bank, the State supervisory authority) and to allow 30 days for such regulator to submit its views and recommendations. Additionally, immediately upon Board approval of an application, the Board is required to notify the Justice Department, so that the latter may challenge the acquisition on antitrust grounds if it elects to do so. The acquisition may not be consummated until 30 days after the date of Board approval. If the Justice Department elects to contest the acquisition under the antitrust laws, it must commence an action within such 30-day period. Commencement of such an action stays the effectiveness of the Board's approval, unless otherwise ordered by the court. In such action, the court reviews de novo the issues presented. If the Justice Department fails to commence action under the antitrust laws within the 30-day period, it cannot thereafter bring an action to challenge the acquisition on antitrust grounds.

Justice Department Merger Guidelines

Parties to a contemplated acquisition have a strong interest in knowing whether the acquisition is likely to be challenged by the Justice Department. The Justice Department Merger Guidelines, adopted in 1968, have been viewed, at least until very recently, as reflecting the Antitrust Division's position regarding

161. 12 U.S.C. § 1842(b) (1976). If the principal regulator disapproves the application, the Board so notifies the applicant. A hearing then must be held not less than 10 nor more than 30 days from the time such notice is given. The Board then grants or denies the application on the basis of the record made in such hearing.
162. 12 U.S.C. § 1849(b) (1976). Unlike the Bank Merger Act, 12 U.S.C. § 1828(c)(4) (1976), the Federal Bank Holding Company Act does not require the Board to notify the Justice Department, and to request from it a report on competitive factors, before acting on an application for acquisition of a bank. The Board, in nondelegation cases (i.e., cases reserved for decision to the Board of Governors rather than delegated to a Federal Reserve bank), however, follows the procedure of notifying the Justice Department and requesting such a report prior to acting on an application, in addition to notifying Justice at the time of approval. See Federal Reserve Board Internal Procedures regarding bank acquisitions under the Federal Bank Holding Company Act.
mergers and acquisitions.

The Guidelines define a "market" to include "any grouping of sales (or other commercial transactions) in which each of the firms whose sales are included enjoys some advantage in competing with those firms whose sales are not included." Since customer proximity provides a competitive advantage to a particular bank, the Guidelines are consistent with the Supreme Court's position that the relevant market for testing the competitive effect of a bank acquisition is local.

The Guidelines define the relevant product market as a service which "is distinguishable as a matter of commercial practice from other . . . services." Thus, if an appreciable segment of the public for some reason prefers services provided by banks to similar services provided by thrift institutions, bank services would comprise the relevant product market. Banks, by this analysis, would enjoy an advantage over thrift institutions in providing those services, justifying the exclusion of thrifts from the market. On the other hand, if the public ceases to distinguish between banks and other types of financial institutions in its selection of the source of financial services, the Guidelines would require the inclusion of those other types of institutions in the relevant product market.

The legality of a merger between competitors in a relevant market is tested under the Guidelines on the basis of market share data. The Guidelines distinguish those markets which are highly concentrated, defined as those markets in which the market share of the four largest firms totals seventy-five percent or more, from markets which are not highly concentrated, with mergers in the former type of market, of course, being more vulnerable to Justice Department challenge. The Guidelines assess the impact of po-

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165. Id. at ¶ 3.
166. See notes 76-115 supra and accompanying text.
167. See, e.g., United States v. First Nat'l Bank & Trust Co. of Lexington, 376 U.S. 665 (1964). Geographic markets are further defined as any "commercially significant" section where the product is sold, so long as it does not "clearly appear that there is no economic barrier that hinders sales from outside." Dep't. of Justice Merger Guidelines, ¶ 3(ii) (1968).
168. Id. at ¶ 3(i).
169. Id. at ¶ 5.
170. Id. at ¶ 6. The Guidelines indicate that the Department of Justice will "ordinarily challenge" a merger if the market shares of the constituent firms exceed the following:
potential competition in terms of market shares, indicating disapproal where "one of the most likely entrants to the market" ac-
quires any firm with twenty-five percent or more of the market, or, if the market is highly concentrated, where it acquires any of the leading firms in the market.\textsuperscript{171}

William Baxter, Assistant Attorney General and head of the Anti-
trust Division, has been highly critical of the Merger Guide-
lines.\textsuperscript{172} He has expressed particular displeasure with the Guide-
lines' emphasis on market share data, favoring a case-by-case analysis of the probable effects of mergers on the basis of all rele-
vant information.\textsuperscript{173} Mr. Baxter has stated that the Antitrust Divi-
sion is currently in the process of preparing a new Merger Guide for publication by Spring of 1982.\textsuperscript{174} If the new Merger Guide re-


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\textit{Id.} at § 5.

\textsuperscript{171} \textit{Id.} at § 18. The Guidelines state that the Department of Justice will "ordinarily challenge" a combination between one of the most likely entrants to the market and (i) any firm with approximately 25\% or more of the market; (ii) one of the two largest firms in a market in which the shares of the two largest firms amount to approximately 50\% or more; (iii) one of the four largest firms in a market in which the shares of the eight largest firms amount to approximately 75\% or more, provided the acquiree firm's share of the market amounts to approximately 10\% or more; or (iv) one of the eight largest firms in a market in which the shares of these firms amount to approximately 75\% or more, provided either (A) the acquiree firm's share of the market is not insubstantial and there are not more than one or two likely entrants into the market, or (B) the acquiree firm is a rapidly growing firm. \textit{Id.}

\textsuperscript{172} In a press conference in August of 1981, Baxter stated:

The merger guidelines, in existence since 1968, have not in fact been followed by any Administration over the last eight years at least. The private bar did not take them seriously. Everyone knew that they did not reflect enforcement intentions of the Division. There is a body of case law on mergers and to the extent there is guidance available to anyone it is in that "case law."

\textsuperscript{173} \textit{1025 ANTITRUST & TRADE REG. REP. (BNA) AA-2 (July 30, 1981).}

\textsuperscript{174} \textit{1027 ANTITRUST & TRADE REG. REP. (BNA) A-4 (August 13, 1981) (statement by Assistant Attorney General Baxter).}
as the statutory limitations in Illinois upon de novo expansion, branch banking, the number of off-premises limited-service facilities which a bank can maintain, and the scope of services which can be offered at such a facility are likely to be accorded significant weight by the Antitrust Division, both in defining the relevant markets and in testing the competitive effects of mergers.

**Antitrust Aspects of Proposed Acquisitions Under the 1981 Act**

Several inferences may be drawn from the decisions of the courts, determinations of bank regulators, and the Guidelines of the Justice Department regarding the manner in which the antitrust laws will be applied to acquisitions of banks in Illinois accomplished pursuant to the 1981 Act.

The impact of a proposed acquisition on competition will be tested against a local geographical market. The State of Illinois will not be viewed as the relevant market, and it is highly unlikely that the five regions designated in the 1981 Act will give content to the geographical market definition. The fact that companies will be limited to acquiring banks located in their home and not more than one contiguous region, however, probably will result in a relatively large percentage of acquisitions of banks in Illinois tested as direct rather than potential competition cases. The size of the relevant geographic market will probably vary with the size of the constituent banking entities, the composition of their customer base, and the urban, suburban, or rural nature of their local and surrounding communities. The Board and Justice Department will probably view a market in which the shares of the four largest banking entities total seventy-five percent or more to be a highly concentrated market in which acquisitions will be very closely scrutinized.

Unless and until the Supreme Court overrules its earlier decisions on the matter, commercial banking will probably be deemed the relevant product market, and the Board will undoubtedly require that the market-share statistics furnished to it regarding a proposed acquisition reflect commercial banking as the product market. In markets where it can be shown statistically that thrifts are a genuine competitive presence, however, the Board will probably consider competition from thrifts as a factor tending to reduce the anticompetitive effects of a proposed acquisition.

Finally, the Illinois restrictions on holding company expansion through acquisition of de novo or recently-chartered banks, and the restrictions on branch banking and limited service facilities...
should prove to be important factors (i) limiting the application of potential competition as a ground for denial of applications, and (ii) reducing the likelihood that a banking institution which is a major competitor in the relevant market will be prevented from establishing additional locations in other geographical areas of that market through acquisitions of small banks with insignificant market shares.

**CONSTITUTIONAL CHALLENGE TO THE 1981 ACT**

On September 1, 1981, three small banks in Illinois filed a complaint in the Circuit Court of Sangamon County against the Illinois Commissioner of Banks and Trust Companies seeking a declaratory judgment that the 1981 Act was enacted in violation of the Illinois Constitution.\(^\text{175}\) More specifically, the plaintiffs contend that the provisions of the 1981 Act permitting multibank holding companies and an additional limited service facility authorize branch banking and that the 1981 Act was not adopted by the necessary vote required by the Constitution for adoption of branch banking legislation.\(^\text{176}\) With regard to the provision authorizing multibank holding companies, although the plaintiffs concede that multibank holding companies do not constitute branch banking \textit{per se}, they argue that because the banks in a holding company system can be operated in a unitary manner constituting \textit{de facto} branch banking, the Act authorizes branch banking. The plaintiffs further contend that the 1981 Act unlawfully delegates to the Federal Reserve Board power to decide whether a bank holding company seeking Board approval to acquire an additional bank will, if granted approval, operate any of the subsidiary banks in its holding company system as \textit{de facto} branch banks in violation of Illinois law. In addition, they contend that various references in the 1981 Act to the Federal Bank Holding Company Act and actions of the Federal Reserve Board thereunder amount to an unlawful general delegation of legislative power by the Illinois General Assembly to the Congress of the United States and the Federal Reserve Board. The Commissioner and the intervening codefendant, The Association for Modern Banking in Illinois, contend that even if

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\(^{176}\) Article XIII, Section Eight, of the Illinois Constitution provides: "Branch banking shall be authorized only by law approved by three-fifths of the members voting on the question or a majority of the members elected, whichever is greater, in each house of the General Assembly." \textit{ILL. CONST. art. XIII, § 8}. 
the 1981 Act can be construed to authorize branch banking, the statute was adopted by the extraordinary constitutional majority necessary for enactment of branch banking legislation. The defendants further contend that neither the provision permitting multibank holding companies nor that permitting an additional limited service facility authorizes branch banking within the meaning of the Illinois Constitution. They argue that whether or not Illinois branch banking laws are effectively enforced at the Federal Reserve level, if a multibank holding company system in fact engages in de facto branch banking, the Commissioner, Illinois Attorney General and affected competitors have adequate recourse to the courts. Moreover, they suggest that the references to the Federal Bank Holding Company Act and the Federal Reserve Board merely recognize federal powers already reserved under the United States Constitution and federal statutes and such federal powers would not be different even if the 1981 Act omitted all reference to them.

On December 28, 1981, the Circuit Court dismissed the complaint. The plaintiffs were granted leave to appeal directly to the Supreme Court of Illinois. The case was argued before the Supreme Court on January 27, 1982. At the time of this writing, the Supreme Court has not rendered a decision on appeal.

**CONCLUSION**

By authorizing bank holding companies to acquire multiple bank subsidiaries in Illinois, the 1981 Act narrows the Illinois banking industry's handicap vis-a-vis Illinois savings and loan, credit union, and finance company competitors in the offering of multilocational financial services. The handicap, however, is by no means eliminated. First, branch banking continues to be prohibited in Illinois. Second, the 1981 Act imposes geographic limits on holding company expansion and prohibits holding companies from expanding de novo or through acquisitions of recently-chartered banks.

The provisions of the 1981 Act circumscribing holding company expansion are complex and in some respects ambiguous. The ambiguities may offer opportunities for holding company acquisition of

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177. The issue regarding the General Assembly's vote is whether a legislator answering "present" is deemed to have cast a vote or abstained. If an answer of "present" is a vote, the 1981 Act failed to receive the extraordinary majority required by the Illinois Constitution; if it is an abstention, the constitutional voting requirement was satisfied.
noncommercial banks, free from geographic and *de novo* expansion restrictions, and may afford a brief “window period” for geographically limited *de novo* expansion through acquisition of *de novo* banks caused to be chartered prior to January 1, 1982.

The ambiguities pose several problems for lawyers attempting to structure holding company acquisitions of banks in Illinois. In situations in which a bank eligible to be acquired under the Act is rechartered by reason of a charter conversion, acquisition by phantom bank merger or phantom bank restructuring into holding company form, the courts and regulators should, through a “tacking” approach, view the rechartered bank as a continuation of the predecessor eligible bank. In many, but not all, cases, resourceful lawyers will be able to avoid this issue by structuring phantom bank acquisitions so that they do not result in a rechartering of the acquired bank.

Antitrust considerations will significantly affect the contours of holding company expansion in Illinois. In assessing the possible anticompetitive effects of proposed acquisitions, the bank regulators, Justice Department, and courts can be expected to apply traditional Clayton Act standards already extensively interpreted in the banking context by the United States Supreme Court. The structure of the banking industry in Illinois and the statutory limitations which will shape the continuing evolution of that structure will undoubtedly play a major role in the application of antitrust principles to proposed acquisitions of banks in Illinois.