FRB Order No. 2015-17
June 15, 2015

FEDERAL RESERVE SYSTEM

Merchants & Farmers Bancshares, Inc.
Leesville, Louisiana

Order Approving the Acquisition of a Bank Holding Company

Merchants & Farmers Bancshares, Inc. ("M&F") has requested the Board's approval under section 3 of the Bank Holding Company Act ("BHC Act")[1] to acquire Vernon Bancshares, Inc. ("Vernon"), and thereby indirectly acquire its subsidiary bank, The Vernon Bank ("Vernon Bank"), all of Leesville, Louisiana. Following the proposed acquisition, Vernon Bank, a state nonmember bank, would be merged into M&F's subsidiary state nonmember bank, Merchants & Farmers Bank and Trust Company ("M&F Bank"), Leesville, Louisiana.[2]

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published (80 Federal Register 9720 (2015)).[3] The time for submitting comments has expired, and the Board has considered the proposal and all comments received in light of the factors set forth in section 3 of the BHC Act.

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[1] 12 U.S.C. § 1842(a)(5).

[2] The merger of Vernon Bank into M&F Bank is subject to the approval of the Federal Deposit Insurance Corporation ("FDIC") pursuant to section 18(c) of the Federal Deposit Insurance Act, 12 U.S.C. § 1828(c). The FDIC approved the merger on March 25, 2015.

[3] 12 CFR 262.3(b).

M&F, with consolidated assets of approximately $320.8 million, is the 2099th largest insured depository organization in the United States.[4] M&F Bank operates only in Louisiana and is the 47th largest depository institution in that state, controlling deposits of approximately $252.5 million, which represent less than 1 percent of the total deposits of insured depository institutions in Louisiana.[5]

Vernon, with consolidated assets of approximately $78.6 million, is the 5037th largest insured depository organization in the United States. Vernon controls Vernon Bank, which is the 113th largest depository institution in Louisiana. Vernon Bank, which operates only in Louisiana, controls deposits of approximately $69.2 million, which represent less than 1 percent of the total deposits of insured depository institutions in that state.

On consummation of this proposal, M&F would become the 1688th largest depository organization in the United States, with consolidated assets of approximately $399.4 million, which represent less than 1 percent of the total assets of insured depository institutions in the United States. M&F Bank would control total deposits of approximately $315.0 million, which represent less than 1 percent of the total amount of deposits of insured depository institutions in the United States. In Louisiana, M&F would become the 36th largest depository organization, controlling deposits of approximately $321.7 million, which represent less than 1 percent of the total deposits of insured depository institutions in that state.

Competitive Considerations

Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or would be in furtherance of an attempt to monopolize

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[4] Nationwide deposit, asset, and ranking data are as of December 31, 2014, unless otherwise noted. In this context, insured depository institutions include commercial banks, savings banks, and savings and loan associations.

[5] State deposit, market share, and ranking data are as of June 30, 2014, unless otherwise noted.

the business of banking in any relevant market. The BHC Act also prohibits the Board from approving a proposal that would substantially lessen competition in any relevant banking market, unless the anticompetitive effects of the proposal are clearly outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the communities to be served.[6]

M&F's and Vernon's subsidiary depository institutions compete directly in the Vernon/Beauregard area, Louisiana banking market ("Vernon/Beauregard banking market").[7] The Board has considered the competitive effects of the proposal in this banking market in light of all the facts of record. In particular, the Board has considered the number of competitors that would remain in the banking market; the relative share of total deposits in insured depository institutions in the market ("market deposits") that M&F would control upon consummation of the proposal;[8] the concentration levels of market deposits and the increase in these levels as measured by the Herfindahl-Hirschman Index ("HHI") under the Department of Justice Bank Merger Competitive Review guidelines ("DOJ Bank Merger Guidelines");[9] and other characteristics of the market.

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[6] 12 U.S.C. § 1842(c)(1).

[7] The Vernon/Beauregard banking market is defined as Vernon Parish and the northern half of Beauregard Parish, both of Louisiana.

[8] Deposit and market share data are as of June 30, 2014, and are based on calculations in which the deposits of thrift institutions are included at 50 percent. The Board previously has indicated that thrift institutions have become, or have the potential to become, significant competitors to commercial banks. See, e.g., Midwest Financial Group, 75 Federal Reserve Bulletin 386 (1989), and National City Corporation, 70 Federal Reserve Bulletin 743 (1984). Thus, the Board regularly has included thrift deposits in the market share calculation on a 50-percent weighted basis. See, e.g., First Hawaiian, Inc., 77 Federal Reserve Bulletin 52 (1991).

[9] Under the DOJ Bank Merger Guidelines, a market is considered unconcentrated if the post-merger HHI is under 1000, moderately concentrated if the post-merger HHI is between 1000 and 1800, and highly concentrated if the post-merger HHI exceeds 1800. The Department of Justice ("DOJ") has informed the Board that a bank merger or acquisition generally would not be challenged (in the absence of other factors indicating

In the Vernon/Beauregard banking market, the change in concentration level and the concentration level on consummation would exceed the threshold levels in the DOJ Bank Merger Guidelines. M&F Bank is the largest insured depository institution in the Vernon/Beauregard banking market, controlling deposits of approximately $182.6 million, which represent approximately 25.8 percent of market deposits. Vernon Bank is the fifth largest insured depository institution in the market, controlling deposits of approximately $69.2 million, which represent approximately 9.7 percent of market deposits. On consummation of the proposal, M&F Bank would remain the largest depository institution in the Vernon/Beauregard banking market, controlling deposits of approximately $251.7 million. The market concentration level in the Vernon/Beauregard banking market as measured by the HHI would increase by 503 points, from 1889 to 2392, and the market share of the combined entity would represent approximately 35.5 percent of market deposits.

The Board has considered whether other factors either mitigate the competitive effects of the proposal or indicate that the proposal would not have a significantly adverse effect on competition in the market.[10] Several factors indicate that the increase in concentration in the Vernon/Beauregard banking market, as measured by the HHI, and the market share of the combined organization overstate the potential competitive effects of the proposal in the market.

The Board has considered the competitive influence of two active credit unions, Barksdale Federal Credit Union ("Barksdale Credit Union"), Bossier City,

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anticompetitive effects) unless the post-merger HHI is at least 1800 and the merger increases the HHI by more than 200 points. Although the DOJ and the Federal Trade Commission issued revised Horizontal Merger Guidelines in 2010, the DOJ has confirmed that its Bank Merger Guidelines, which were issued in 1995, were not modified. See Press Release, Department of Justice (August 19, 2010), www.justice.gov/opa/pr/2010/August/10-at-938.html.

[10] The number and strength of factors necessary to mitigate the competitive effects of a proposal depend on the size of the increase in, and the resulting level of concentration in, a banking market. See NationsBank Corp., 84 Federal Reserve Bulletin 129 (1998).

Louisiana, and Navy Federal Credit Union ("Navy Federal"), Vienna, Virginia, in the Vernon/Beauregard banking market and determined that the activities of the credit unions exert a competitive influence that mitigates, in part, the potential effects of the proposal.[11] Each of these credit unions offers a wide range of consumer banking products, operates street-level branches, and has membership criteria that include a majority of the residents in the Vernon/Beauregard banking market.[12] The Board finds that these circumstances warrant including the deposits of these credit unions at a 50-percent weight in estimating market influence.[13] Adjusting to reflect competition by these credit unions in the market, the market concentration level in the Vernon/Beauregard banking market as measured by the HHI would increase by 389, from a level of 1582 to 1971, and the market share of M&F resulting from the transaction would increase in the market from 22.7 percent to 31.2 percent.

After consummation of the proposal, the merged entity would face competition from nine competitors in the market, some with a significant presence in the market. The second and third largest competitors in the market would control

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[11] The Board previously has considered competition from certain active credit unions with these features as a mitigating factor. See, e.g., Chemical Financial Corporation, FRB Order No. 2015-13 (April 20, 2015); Central Bank of Audrain County, FRB Order No. 2014-17 (October 17, 2014); Chemical Financial Corporation, FRB Order No. 2014-16 (September 30, 2014); ANB Bank, FRB Order No. 2014-14 (September 11, 2014); Old National Bancorp, FRB Order No. 2014-13 (July 14, 2014); First Interstate BancSystem, Inc., FRB Order No. 2014-11 (June 30, 2014); Mitsubishi UFJ Financial Group, Inc., FRB Order No. 2012-12 (November 14, 2012); Old National Bancorp, FRB Order No. 2012-9 (August 30, 2012); and United Bankshares, Inc. (order dated June 20, 2011), 97 Federal Reserve Bulletin 19 (2nd Quar. 2011).

[12] Notably, the membership criteria of both Barksdale Credit Union and Navy Federal include, among others, active and retired military personnel and their families. As the largest employer in the Vernon/Beauregard banking market is the United States Army Base at Fort Polk, and because a significant population of active and retired military personnel and their family members reside in the Vernon/Beauregard banking market, a majority of the residents in the banking market are eligible to join these credit unions.

[13] Weighting the deposits at 50 percent takes into account the limited lending done by these credit unions to small businesses relative to commercial banks' lending levels.

approximately 21.3 percent and 17.5 percent of market deposits, respectively, and the fourth largest competitor in the market would control approximately 11.0 percent of market deposits, when weighting the deposits of Barksdale Credit Union and Navy Federal at 50 percent.

The record also indicates that the Vernon/Beauregard banking market may be attractive for entry and expansion by bank competitors. In 2008, Navy Federal entered the market, and the fourth largest bank competitor in the market is expanding its presence in the market by opening a second branch.

The DOJ conducted a review of the potential competitive effects of the merger and has advised the Board that consummation would not be likely to have a significantly adverse effect on competition in any relevant banking market. In addition, the appropriate banking agencies have been afforded an opportunity to comment and have not objected to the proposal.

Based on all the facts of record, the Board concludes that consummation of the proposal would not have a significantly adverse effect on competition or on the concentration of resources in the Vernon/Beauregard banking market or in any other relevant banking market. Accordingly, the Board determines that competitive considerations are consistent with approval.

Financial, Managerial, and Other Supervisory Considerations

In reviewing a proposal under the BHC Act, the Board considers the financial and managerial resources and the future prospects of the institutions involved. In its evaluation of financial factors, the Board reviews the financial condition of the organizations involved on both parent-only and consolidated bases, as well as the financial condition of the subsidiary depository institutions and the organizations' significant nonbanking operations. In this evaluation, the Board considers a variety of information, including capital adequacy, asset quality, and earnings performance. The Board evaluates the financial condition of the combined organization, including its capital position, asset quality, liquidity, earnings prospects, and the impact of the proposed funding of the transaction. The Board also considers the ability of the organization to absorb the costs of the proposal and the proposed integration of the operations of the institutions. In assessing financial factors, the Board considers capital adequacy to be especially important. The Board considers the future prospects of the organizations involved in the proposal in light of the financial and managerial resources and the proposed business plan.

M&F and Vernon are both well capitalized and would remain so on consummation of the proposal. The transaction is structured as an all cash deal, with each share of Vernon being purchased directly, based upon the agreed price.[14] The asset quality, earnings, and liquidity of M&F and Vernon are consistent with approval, and M&F appears to have adequate resources to absorb the costs of the proposal and to complete integration of the institutions' operations. In addition, future prospects are considered consistent with approval. Based on its review of the record, the Board finds that the organization has sufficient financial resources to effect the proposal.

The Board also has considered the managerial resources of the organizations involved and of the proposed combined organization. The Board has reviewed the examination records of M&F, Vernon, and their subsidiary depository institutions, including assessments of their management, risk-management systems, and operations. In addition, the Board has considered information provided by M&F, the Board's supervisory experiences and those of other relevant bank supervisory agencies with the organizations, and the organizations' records of compliance with applicable banking and anti-money-laundering laws.

M&F, Vernon, and their subsidiary depository institutions are each considered to be well managed. M&F's existing risk-management program and its directorate and senior management are considered to be satisfactory. The directors and

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[14] M&F would fund the transaction with available cash on hand and through the liquidation of marketable securities. M&F has the resources to effect the proposed transaction.

senior executive officers of M&F have substantial knowledge of and experience in the banking and financial services sectors.[15]

The Board also has considered M&F's plans for implementing the proposal. M&F would implement its risk-management policies, procedures, and controls at the combined organization, and these are considered acceptable from a supervisory perspective. In addition, M&F's and Vernon's management has the experience and resources to ensure that the combined organization operates in a safe and sound manner, and M&F plans to integrate Vernon's existing management and personnel in a manner that augments M&F's management.

Based on all the facts of record, including M&F's supervisory record, managerial and operational resources, and plans for operating the combined institution after consummation, the Board concludes that considerations relating to the financial and managerial resources and future prospects of the organizations involved in the proposal, as well as the records of effectiveness of M&F and Vernon in combatting money-laundering activities, are consistent with approval.

Convenience and Needs Considerations

In acting on a proposal under section 3 of the BHC Act, the Board must consider the effects of the proposal on the convenience and needs of the communities to be served and take into account the records of the relevant depository institutions under the Community Reinvestment Act ("CRA").[16] The CRA requires the federal financial supervisory agencies to encourage insured depository institutions to help meet the credit needs of the local communities in which they operate, consistent with their safe and sound operation,[17] and requires the appropriate federal financial supervisory agency to

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[15] The senior management of M&F and M&F Bank would remain the same after consummating the acquisition.

[16] 12 U.S.C. § 1842(c)(2); 12 U.S.C. § 2901 et seq.

[17] 12 U.S.C. § 2901(b).

take into account a relevant depository institution's record of meeting the credit needs of its entire community, including low- and moderate-income ("LMI") neighborhoods, in evaluating bank expansionary proposals.[18]

The Board has considered all the facts of record, including reports of examination of the CRA performance of M&F Bank and Vernon Bank, information provided by M&F, and confidential supervisory information.

A. Records of Performance Under the CRA

As provided in the CRA, the Board evaluates an institution's performance record in light of examinations by the appropriate federal supervisors of the CRA performance records of the relevant institutions.[19] The CRA requires that the appropriate federal financial supervisor for a depository institution prepare a written evaluation of the institution's record of meeting the credit needs of its entire community, including LMI neighborhoods.[20] An institution's most recent CRA performance evaluation is a particularly important consideration in the applications process because it represents a detailed, on-site evaluation of the institution's overall record of performance under the CRA by its appropriate federal supervisor.

CRA Performance of M&F Bank

M&F Bank was assigned an overall "satisfactory" rating at its most recent CRA performance evaluation by the FDIC as of June 2012 ("M&F Bank Evaluation").[21]

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[18] 12 U.S.C. § 2903.

[19] See Interagency Questions and Answers Regarding Community Reinvestment, 75 Federal Register 11642, 11665 (2010).

[20] 12 U.S.C. § 2906.

[21] The M&F Bank Evaluation was conducted using Small Institution CRA Examination Procedures, and examiners reviewed the bank's lending activity from April 23, 2007, through June 5, 2012. The M&F Bank Evaluation included a full-scope review of Vernon Parish and Calcasieu Parish, both of Louisiana. Examiners gave more weight to the Vernon Parish non-MSA (Metropolitan Statistical Area), based on the percentages of M&F Bank's total loans, deposits, and banking offices located in the Vernon Parish.

Examiners determined that the bank's average quarterly net loan-to-deposit ratio was reasonable given the bank's asset size, financial condition, and assessment area credit needs. In addition, examiners found that the bank exhibited a good record of lending within the assessment area, with a majority of bank's loans made within the assessment area. Examiners also noted that the bank's geographic distribution of lending reflected a satisfactory penetration and loan dispersion throughout the assessment area. Further, the bank's lending distribution to borrowers reflected good responsiveness to businesses of different sizes and individuals of different income levels, particularly LMI borrowers, as well as good performance in meeting the credit needs of small businesses in the assessment area.

CRA Performance of Vernon Bank

Vernon Bank was assigned an overall "satisfactory" rating at its most recent CRA performance evaluation by the FDIC in March 2011 ("Vernon Bank Evaluation").[22] Examiners determined that the bank's average quarterly net loan-to-deposit ratio was satisfactory given the bank's resources and assessment area credit needs. Examiners noted that a substantial majority of the bank's loans were made within its assessment area, demonstrating the bank's willingness to meet the credit needs of its assessment area. Further, examiners found that the bank's geographic distribution of loans throughout the assessment area was reasonable. Examiners also noted that the bank's distribution of loans reflected reasonable penetration among businesses of different sizes and individuals of different income levels, as well as reasonable performance in meeting the credit needs of small businesses in the assessment area.

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[22] The Vernon Bank Evaluation was conducted using Small Institution CRA Examination Procedures. Examiners reviewed the bank's lending activity from February 6, 2006, through March 7, 2011. The Vernon Bank Evaluation included an evaluation of Vernon Parish.

B. Additional Information on Convenience and Needs of Communities to Be Served by the Combined Organization

In assessing the effects of a proposal on the convenience and needs of the communities to be served, the Board also considers the extent to which the proposal would result in public benefits.

M&F represents that the proposal would provide customers of the combined organization access to an expanded branch network and would offer additional or expanded services to current Vernon Bank customers, including expanded access to more ATM locations and extended branch hours. M&F also states that the combined organization's larger lending limit would allow M&F to make larger commercial loans to its customers. Further, M&F represents that M&F Bank will continuously monitor the CRA performance of the combined entity in order to ensure that the organization's obligations thereunder are met.

C. Conclusion on Convenience and Needs Considerations

The Board has considered all the facts of record, including reports of examination of the CRA records of the institutions involved, information provided by M&F, and confidential supervisory information. Based on the Board's assessment of the CRA performance and consumer compliance programs of M&F Bank and Vernon Bank, review of examination reports, and consultations with other agencies, the Board concludes that the convenience and needs factor, including the CRA records of the insured depository institutions involved in this transaction, is consistent with approval of the application.

Financial Stability

The Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") amended section 3 of the BHC Act to require the Board to consider "the extent to which a proposed acquisition, merger, or consolidation would result in greater or more concentrated risk to the stability of the United States banking or financial system."[23]

To assess the likely effect of a proposed transaction on the stability of the U.S. banking or financial system, the Board considers a variety of metrics that capture the systemic "footprint" of the resulting firm and the incremental effect of the transaction on the systemic footprint of the acquiring firm. These metrics include measures of the size of the resulting firm, the availability of substitute providers for any critical products and services offered by the resulting firm, the interconnectedness of the resulting firm with the banking or financial system, the extent to which the resulting firm contributes to the complexity of the financial system, and the extent of the cross-border activities of the resulting firm.[24] These categories are not exhaustive, and additional categories could inform the Board's decision. In addition to these quantitative measures, the Board considers qualitative factors, such as the opaqueness and complexity of an institution's internal organization, that are indicative of the relative degree of difficulty of resolving the resulting firm. A financial institution that can be resolved in an orderly manner is less likely to inflict material damage to the broader economy.[25]

The Board has considered information relevant to risks to the stability of the U.S. banking or financial system. After consummation, M&F would have approximately $399.4 million in consolidated assets and would not be likely to pose systemic risks. The Board generally presumes that a merger that involves an acquisition of less than $2 billion in assets, or results in a firm with less than $25 billion in consolidated assets, will not pose significant risks to the financial stability of the United States absent evidence that the transaction would result in a significant increase in

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[23] Section 604(d) of the Dodd-Frank Act, Pub. L. No. 111-203, 123 Stat. 1376, 1601, codified at 12 U.S.C. § 1842(c)(7).

[24] Many of the metrics considered by the Board measure an institution's activities relative to the U.S. financial system.

[25] For further discussion of the financial stability standard, see Capital One Financial Corporation, FRB Order 2012-2 (February 14, 2012).

interconnectedness, complexity, cross-border activities, or other risk factors. Such additional risk factors are not present in this transaction.

In light of all the facts and circumstances, this transaction would not appear to result in meaningfully greater or more concentrated risks to the stability of the U.S. banking or financial system. Based on these and all other facts of record, the Board determines that considerations relating to financial stability are consistent with approval.

Conclusion

Based on the foregoing and all the facts of record, the Board determines that the application should be, and hereby is, approved. In reaching its conclusion, the Board has considered all the facts of record in light of the factors that it is required to consider under the BHC Act and other applicable statutes. The Board's approval is specifically conditioned on compliance by M&F with all the conditions imposed in this order, including receipt of all required regulatory approvals, and on the commitments made to the Board in connection with the application. For purposes of this action, the conditions and commitments are deemed to be conditions imposed in writing by the Board in connection with its findings and decision herein and, as such, may be enforced in proceedings under applicable law.

The proposal may not be consummated before the 15th calendar day after the effective date of this Order or later than three months thereafter, unless such period is extended for good cause by the Board or the Federal Reserve Bank of Atlanta acting under delegated authority.

By order of the Board of Governors,[26] effective June 15, 2015.

Margaret M. Shanks (signed)

Margaret McCloskey Shanks
Deputy Secretary of the Board

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[26] Voting for this action: Chair Yellen, Vice Chairman Fischer, and Governors Tarullo, Powell, and Brainard.