

FEDERAL RESERVE SYSTEM

C-B-G, Inc.  
West Liberty, Iowa

Order Approving the Acquisition of Shares  
of a Bank Holding Company

C-B-G, Inc. (“C-B-G”), a bank holding company within the meaning of the Bank Holding Company Act (“BHC Act”), has requested the Board’s approval under section 3 of the BHC Act<sup>1</sup> to acquire up to 24.35 percent of the voting shares of Washington Bancorp (“Washington”) and thereby indirectly acquire an interest in Washington’s subsidiary bank, Federation Bank, both of Washington, Iowa.

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published (69 Federal Register 78,028 (2004)). The time for filing 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.

C-B-G, with consolidated assets of approximately \$189 million, is the 63<sup>rd</sup> largest depository organization in Iowa, controlling deposits of \$160 million, which represent less than 1 percent of total deposits of insured depository institutions in Iowa (“state deposits”).<sup>2</sup> Washington, with total consolidated assets

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<sup>1</sup> 12 U.S.C. § 1842.

<sup>2</sup> Asset data are as of December 31, 2004. Statewide deposit and ranking data are as of June 30, 2004. Deposit data reflect the total of the deposits reported by each organization’s insured depository institutions in their Consolidated Reports of Condition and Income or Thrift Financial Reports. In this context, insured depository institutions include commercial banks, savings banks, and savings associations.

of \$106 million, is the 154<sup>th</sup> largest depository organization in Iowa, controlling \$75 million in deposits. If C-B-G were deemed to control Washington on consummation of the proposal, C-B-G would become the 43<sup>rd</sup> largest depository organization in Iowa, controlling approximately \$235 million in deposits, which represents 1 percent of state deposits.

The Board received comments from Washington and a local resident objecting to the proposal and expressing concern that the proposal would result in C-B-G controlling and potentially harming Washington.<sup>3</sup> The Board has considered carefully these comments in light of the factors that the Board must consider under section 3 of the BHC Act.

The Board previously has stated that the acquisition of less than a controlling interest in a bank or bank holding company is not a normal acquisition for a bank holding company.<sup>4</sup> However, the requirement in section 3(a)(3) of the BHC Act that the Board's approval be obtained before a bank holding company acquires more than 5 percent of the voting shares of a bank suggests that the Congress contemplated the acquisition by bank holding companies of between 5 and 25 percent of the voting shares of banks.<sup>5</sup> On this basis, the Board

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<sup>3</sup> Washington requested a private meeting with C-B-G about the proposal. Under the Board's Rules of Procedures, the Reserve Bank may arrange a private meeting between a protestant and the applicant for the purposes of clarifying and narrowing issues and resolving differences when both parties agree to such a meeting. 12 C.F.R. 262.25(c). The parties ultimately declined the invitation of the Federal Reserve Bank of Chicago to participate in a private meeting.

<sup>4</sup> See, e.g., Brookline Bancorp, MHC, 86 Federal Reserve Bulletin 52 (2000) ("Brookline"); North Fork Bancorporation, Inc., 81 Federal Reserve Bulletin 734, 735 (1995) ("North Fork"); First Piedmont Corp., 59 Federal Reserve Bulletin 456, 457 (1973).

<sup>5</sup> 12 U.S.C. § 1842(a)(3).

previously has approved the acquisition by a bank holding company of less than a controlling interest in a bank or bank holding company.<sup>6</sup>

C-B-G has indicated that it does not propose to control or exercise a controlling influence over Washington or Federation Bank. C-B-G has agreed to abide by certain commitments previously relied on by the Board in determining that an investing bank holding company would not be able to exercise a controlling influence over another bank holding company for purposes of the BHC Act.<sup>7</sup> For example, C-B-G has committed not to exercise or attempt to exercise a controlling influence over the management or policies of Washington or any of its subsidiaries; not to seek or accept representation on the board of directors of Washington or any of its subsidiaries; and not to have any director, officer, employee, or agent interlocks with Washington or any of its subsidiaries. C-B-G also has committed not to attempt to influence the dividend policies, loan decisions, or operations of Washington or any of its subsidiaries. The Board notes that the BHC Act prohibits C-B-G from acquiring additional shares of Washington or attempting to exercise a controlling influence over Washington without the Board's prior approval.

The Board has adequate supervisory authority to monitor compliance by C-B-G with its commitments and can take enforcement action against C-B-G if

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<sup>6</sup> S&T Bancorp, Inc., 91 Federal Reserve Bulletin 74 (2005) (acquisition of up to 24.9 percent of the voting shares of a bank holding company); Brookline (acquisition of up to 9.9 percent of the voting shares of a bank holding company); GB Bancorporation, 83 Federal Reserve Bulletin 115 (1997) (acquisition of up to 24.9 percent of the voting shares of a bank).

<sup>7</sup> See, e.g., S&T Bancorp; Brookline; FleetBoston Financial Corp., 86 Federal Reserve Bulletin 751, 766 (2000). The commitments are set forth in the Appendix. Washington also has expressed concern that C-B-G might in the future seek relief from some of these commitments. Any such request would be evaluated by the Board in light of all facts and circumstances at that time.

it violates any of the commitments.<sup>8</sup> The Board also has authority to initiate a control proceeding against C-B-G if facts presented later indicate that C-B-G or any of its subsidiaries or affiliates in fact controls Washington for purposes of the BHC Act.<sup>9</sup> Based on these considerations and all other facts of record, the Board has concluded that C-B-G would not acquire control of, or have the ability to exercise a controlling influence over, Washington through the proposed acquisition of voting shares.<sup>10</sup>

### Competitive and Convenience and Needs 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 any attempt to monopolize the business of banking in any relevant banking market.

Section 3 also prohibits the Board from approving a proposal that would substantially lessen competition in any relevant banking market, unless the Board finds that the anticompetitive effects of the proposal clearly are outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the community to be served.<sup>11</sup>

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<sup>8</sup> See 12 U.S.C. § 1818(b)(1).

<sup>9</sup> See 12 U.S.C. § 1841(a)(2)(C).

<sup>10</sup> Washington asserted that the proposal is inconsistent with the Board's source of strength doctrine. As explained above, the Board previously has permitted a bank holding company that meets the requirements of section 3 of the BHC Act to acquire shares of a bank or bank holding company in a transaction that does not trigger the Board's source of strength regulation.

Washington also expressed concern that the proposal could subject Federation Bank to liability under the cross-guarantee provision of the Federal Deposit Insurance Act, 12 U.S.C. § 1815(e) ("FDI Act"), if a subsidiary bank of C-B-G were to fail or require assistance from the Federal Deposit Insurance Corporation ("FDIC"). The Board notes that the application of this provision of the FDI Act is a matter for the FDIC to decide.

<sup>11</sup> 12 U.S.C. § 1842(c)(1).

The Board previously has stated that one company need not acquire control of another company to lessen competition between them substantially.<sup>12</sup> C-B-G and Washington, however, do not compete directly in any relevant banking market. Based on all the facts of record, the Board has concluded that consummation of the proposal would have no significant adverse effect on competition or on the concentration of banking resources in any relevant banking market and that competitive factors are consistent with approval of the proposal.

In addition, considerations relating to the convenience and needs of the communities to be served, including the records of performance of the institutions involved under the Community Reinvestment Act (“CRA”),<sup>13</sup> are consistent with approval. C-B-G’s subsidiary banks each received “satisfactory” ratings, and Federation Bank received an “outstanding” rating, at their most recent evaluations for CRA performance by the FDIC.<sup>14</sup>

#### Financial, Managerial, and Supervisory Considerations

Section 3 of the BHC Act requires the Board to consider the financial and managerial resources and future prospects of the companies and depository institutions involved in the proposal and certain other supervisory factors. The

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<sup>12</sup> The Board has found that noncontrolling interests in directly competing depository institutions may raise serious questions under the BHC Act and has concluded that the specific facts of each case will determine whether the minority investment in a company would be anticompetitive. See, e.g., BOK Financial Corp., 81 Federal Reserve Bulletin 1052, 1053-54 (1995); Mansura Bancshares, Inc., 79 Federal Reserve Bulletin 37, 38 (1993).

<sup>13</sup> 12 U.S.C. § 2901 et seq.

<sup>14</sup> The most recent CRA performance evaluations of Community Bank, Muscatine, Iowa, the larger of C-B-G’s subsidiary banks, and Wilton Savings Bank, Wilton, Iowa, C-B-G’s other subsidiary bank, were as of February 2004 and July 2003, respectively. Federation Bank’s most recent CRA performance evaluation was as of August 2004.

Board has considered carefully these factors in light of all the facts of record, including confidential reports of examination, other confidential supervisory information from the federal and state banking supervisors of the organizations involved, publicly reported and other financial information, information provided by C-B-G, and comments received.<sup>15</sup>

In evaluating financial factors in expansion proposals by banking organizations, the Board reviews the financial condition of the organizations involved on both a parent-only and consolidated basis, as well as the financial condition of the subsidiary depository institutions and significant nonbanking operations. In this evaluation, the Board considers a variety of areas, including capital adequacy, asset quality, and earnings performance. In assessing financial factors, the Board consistently has considered capital adequacy to be especially important. The Board also evaluates the financial condition of the combined organization on consummation, including its capital position, asset quality, and earnings prospects and the impact of the proposed funding of the transaction.<sup>16</sup>

Based on its review of these factors, the Board finds that C-B-G has sufficient financial resources to effect the proposal. C-B-G and its subsidiary banks currently are well capitalized and would remain so on consummation of this proposal. The proposed transaction is structured as a cash transaction, and

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<sup>15</sup> Washington also expressed concern that C-B-G could seek access to Washington's confidential records. The Board notes that Iowa law delineates the rights of shareholders to access an Iowa corporation's records. See Iowa Code § 490.1602.

<sup>16</sup> As previously noted, the current proposal provides that C-B-G would acquire only up to 24.35 percent of Washington. Under these circumstances, the financial statements of C-B-G and Washington would not be consolidated for purposes of Federal Reserve reporting requirements.

the consideration to be received by the Washington shareholders who are selling their shares to C-B-G would be funded from issuance of trust preferred securities.

The Board also has considered the managerial resources of the organizations involved. The Board has reviewed the examination records of C-B-G, Washington, and their subsidiary depository institutions, including assessments of their management, risk-management systems, and operations. In addition, the Board has considered its supervisory experiences and those of the other relevant banking agencies with the organizations and their records of compliance with applicable banking laws. C-B-G, Washington, and their subsidiary depository institutions are considered well managed.

Based on all the facts of record, the Board concludes that considerations relating to the financial and managerial resources and future prospects of the organizations involved in the proposal are consistent with approval, as are the other supervisory factors the Board must consider under the BHC Act.

#### Other Considerations

Washington has asserted that the proposal would violate an Iowa statute that requires a bank holding company making an offer to purchase, directly or indirectly, shares of an Iowa-chartered bank to extend the same offer to all shareholders of the bank.<sup>17</sup> If a bank is wholly owned by a bank holding company, as in this case, Washington argues that the same offer must be made to all the shareholders of the parent holding company. C-B-G, which made an offer only to some shareholders of Washington, has responded that the Iowa statute does not apply to the proposal because it is acquiring shares of a bank holding company, and not a bank, and that no additional shares of Federation Bank exist to purchase.

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<sup>17</sup> Iowa Code § 524.1803.

The Board may not approve a proposal that is prohibited by a valid state law.<sup>18</sup> The Board is not, however, the arbiter of disputes regarding the applicability or meaning of state corporate law.

The Board has reviewed the state law in this case and the submissions from C-B-G and Washington regarding the interpretation of the Iowa statute. In addition, the Board has consulted with the Iowa Superintendent of Banking and the Iowa Attorney General's Office.

Based on this review, it appears that the proposed acquisition of Washington shares is not prohibited under state law and can be consummated without violating state law. Under C-B-G's interpretation, the transaction would be permitted as structured. Even under Washington's interpretation, C-B-G would be permitted to acquire the shares at issue if it made a similar offer to all Washington shareholders. Accordingly, state law does not prohibit C-B-G from acquiring shares of Washington under either interpretation.

The Board conditions its action in this case on C-B-G's compliance with applicable state law.<sup>19</sup> If C-B-G must offer to purchase and then acquire additional shares of Washington, further review and approval by the Federal Reserve may be required under the BHC Act at that time.

### Conclusion

Based on the foregoing and all the facts of record, the Board has determined 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

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<sup>18</sup> Whitney National Bank in Jefferson Parish v. Bank of New Orleans and Trust Co., 379 U.S. 411 (1965).

<sup>19</sup> See also Central Pacific Financial Corp., 90 Federal Reserve Bulletin 93 (2004); Brookline Bancorp, MHC, 86 Federal Reserve Bulletin 52 (2000); Security Pecos Bancshares, Inc., 85 Federal Reserve Bulletin 640 (1999).

statutes. The Board's approval is specifically conditioned on compliance by C-B-G with the conditions imposed in this order and all the commitments made to the Board in connection with the application. For purposes of this transaction, those 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 acquisition of Washington's voting shares may not be consummated before the fifteenth calendar day after the effective date of this order, or later than three months after the effective date of this order, unless such period is extended for good cause by the Board or the Federal Reserve Bank of Chicago, acting pursuant to delegated authority.

By order of the Board of Governors,<sup>20</sup> effective April 26, 2005.

(signed)

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Robert deV. Frierson  
Deputy Secretary of the Board

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<sup>20</sup> Voting for this action: Chairman Greenspan, Vice Chairman Ferguson, and Governors Gramlich, Bies, Olson, Bernanke, and Kohn.

## APPENDIX

In connection with its application to acquire up to 24.35 percent of Washington, C-B-G commits that it will not, directly or indirectly:

- (1) take any action that would cause Washington<sup>21</sup> to become a subsidiary of C-B-G;
- (2) acquire or retain shares that would cause the combined interests of C-B-G and its officers, directors, and affiliates to equal or exceed 25 percent of the outstanding voting shares of Washington;
- (3) exercise or attempt to exercise a controlling influence over the management or policies of Washington;
- (4) seek or accept representation on the board of directors of Washington;
- (5) have or seek to have any representative serve as an officer, agent, or employee of Washington;
- (6) propose a director or slate of directors in opposition to a nominee or slate of nominees proposed by the management or board of directors of Washington;
- (7) solicit or participate in soliciting proxies with respect to any matter presented to the shareholders of Washington;
- (8) attempt to influence the dividend policies or practices; the loan, credit, or investment decisions or policies; the pricing of services; any personnel decisions; any operations activities, including the location of any offices or branches or their hours of operation; or any similar activities or decisions of Washington;
- (9) dispose or threaten to dispose of shares of Washington in any manner as a condition of specific action or nonaction by Washington; or
- (10) enter into any other banking or nonbanking transactions with Washington, except that C-B-G may establish and maintain deposit accounts with bank

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<sup>21</sup> All references to Washington in these commitments include any subsidiary of Washington.

subsidiaries of Washington, provided that the aggregate balances of all such accounts do not exceed \$500,000 and that the accounts are maintained on substantially the same terms as those prevailing for comparable accounts of persons unaffiliated with Washington.