FEDERAL RESERVE SYSTEM

Gateway Bank & Trust Co.
Elizabeth City, North Carolina

Order Approving the Acquisition and Establishment of Branches

Gateway Bank & Trust Co. ("Gateway"), a state member bank, has requested the Board's approval under section 18(c) of the Federal Deposit Insurance Act ("Bank Merger Act") to assume certain liabilities and acquire certain assets of three branches of Provident Bank of Maryland, Baltimore, Maryland ("Provident").[1] These branches are in Elizabeth City, North Carolina ("Elizabeth City Branch"), and Emporia and Suffolk, both in Virginia (collectively, "Virginia Branches").[2]

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published in accordance with the Bank Merger Act and the Board's Rules of Procedure (12 C.F.R. 262.3(b)). As required by the Bank Merger Act, reports on the competitive effects of the merger were requested from the United States Attorney General and the other federal banking agencies. 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 the Bank Merger Act.

Gateway, with total consolidated assets of $353 million, is the 43rd largest insured depository institution in North Carolina, controlling deposits of $184.2 million. The Elizabeth City Branch controls deposits of $52 million. On consummation of the proposal, Gateway would remain the 43rd largest insured

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[1] 12 U.S.C § 1828(c)).

[2] See 12 U.S.C. § 1831u. The branches are at 400 West Ehringhaus Street in Elizabeth City, 520 S. Main Street in Emporia, and 2825 Godwin Boulevard in Suffolk. Provident will continue to operate branches in Maryland, Virginia,

depository institution in North Carolina, controlling deposits of $236.2 million, which represent less than 1 percent of total deposits of insured depository institutions in the state.[3]

Gateway is the 119th largest insured depository institution in Virginia, controlling state deposits of approximately $48 million. The Virginia Branches control deposits of $90.8 million. On consummation of the proposal, Gateway would become the 81st largest insured depository institution in Virginia, controlling deposits of $139.6 million, which represent less than 1 percent of total deposits of insured depository institutions in the state.

Interstate Analysis

Gateway is in North Carolina and proposes to acquire two branches in Virginia, as well as a branch in North Carolina. Section 102 of the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 ("Riegle-Neal Act") authorizes a bank to merge with another bank under certain conditions unless, before June 1, 1997, the home state of one of the banks involved in the transaction adopted a law expressly prohibiting merger transactions involving out-of-state banks.[4] Virginia and North Carolina have enacted legislation allowing interstate mergers between banks in their states and out-of-state banks pursuant to the provisions of the Riegle-Neal Act.[5] Gateway has complied with state law

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Pennsylvania, and the District of Columbia.

[3] Asset data are as of March 31, 2004. Deposit data and ranking data are as of June 30, 2003, and reflect merger and acquisition activity through April 20, 2004.

[4] Pub. L. No 103-328, 108 Stat. 2338 (1994); see 12 U.S.C. § 1831u.

[5] See Va. Code Ann. 6.1-44.1 et seq. (effective March 16, 1995); 1999 N.C. Sess. Laws 53-224(11) (effective May 21, 1999).

requirements, and the proposal meets all other requirements of the Riegle-Neal Act.[6] Accordingly, the Riegle-Neal Act authorizes the proposed interstate branch acquisitions.

Competitive Considerations

The Bank Merger Act prohibits the Board from approving an application if the proposal would result in a monopoly or would be in furtherance of an attempt to monopolize the business of banking.[7] The Bank Merger Act also prohibits the Board from approving a proposal that would substantially lessen competition or tend to create a monopoly in any relevant market, unless the Board finds that the anticompetitive effects of the proposed transaction are clearly outweighed in the public interest by the probable effect of the transaction in meeting the convenience and needs of the community to be served.[8]

Gateway proposes to acquire a Provident branch in each of the following markets where Gateway and Provident compete directly: the Norfolk-Portsmouth, Virginia-North Carolina, banking market ("Norfolk-Portsmouth Market") and the Elizabeth City, North Carolina,[9] banking market

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6 Gateway is adequately capitalized and the resulting bank would continue to be adequately capitalized and adequately managed on consummation of this proposal. Gateway and its affiliates would control less than 10 percent of the total amount of deposits of insured depository institutions in the United States and less than 30 percent of the total amount of deposits of insured depository institutions in Virginia. See 12 U.S.C. § 1831u.

7 12 U.S.C. § 1828(c)(5)(A).

8 12 U.S.C. § 1828(c)(5)(A) and (B).

9 The Norfolk-Portsmouth Market is defined as the independent cities of Chesapeake, Norfolk, Portsmouth, Suffolk, and Virginia Beach in Virginia; and Currituck County, North Carolina. The Elizabeth City Market is defined as the counties of Camden, Pasquotank, and Perquimans in North Carolina.

("Elizabeth City Market"). The Board has carefully reviewed the competitive effects of the proposal in these banking markets in light of all the facts of record, including the number of competitors that would remain and the relative shares of total deposits in depository institutions in each market ("market deposits") they would control,[10] the concentration level of market deposits and the increase in this level as measured by the Herfindahl-Hirschman Index ("HHI") and the Department of Justice Merger Guidelines ("DOJ Guidelines"), [11] and other characteristics of the markets.

After consummation of the proposal, the Norfolk-Portsmouth Market would remain moderately concentrated, and the post-merger HHI would be consistent with the DOJ Guidelines and Board precedent. Numerous competitors would remain in the banking market.[12]

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[10] Market share data are based on calculations in which the deposits of thrift institutions are included at 50 percent before consummation. The Board has previously indicated that thrift institutions have become, or have the potential to become, significant competitors of commercial banks. See, e.g., Midwest Financial Group, 75 Federal Reserve Bulletin 386 (1989); National City Corporation, 70 Federal Reserve Bulletin 743 (1984). Thus, the Board regularly has included thrift deposits in the calculation of market share on a 50 percent weighted basis.

[11] 49 Federal Register 26,823 (1984). Under these guidelines, a market is considered moderately concentrated if the post-merger HHI is between 1000 and 1800 and highly concentrated if the post-merger HHI is more than 1800. The Department of Justice has informed the Board that a bank merger or acquisition generally will not be challenged (in the absence of other factors indicating anticompetitive effects) unless the post-merger HHI is at least 1800 and the merger increases the HHI by more than 200 points. The Department of Justice has stated that the higher than normal thresholds for an increase in the HHI when screening bank mergers and acquisitions for anticompetitive effects implicitly recognize the competitive effects of limited-purpose and other nondepository financial entities.

[12] Gateway operates the 14th largest depository institution in the market,

In the Elizabeth City Market, however, the HHI would exceed DOJ Guidelines on consummation. Gateway is the second largest insured depository institution in the market, controlling deposits of $143.3 million, which represent 21.9 percent of market deposits. Provident is the sixth largest depository institution with deposits of $52 million, which represent approximately 8 percent of market deposits. On consummation of the merger, Gateway would become the largest depository institution in the market, controlling deposits of $195.3 million, which represent approximately 29.9 percent of market deposits. The HHI would increase by 349 points to 2014.

Several factors indicate that the proposal is not likely to have a significant adverse effect on competition in the market. Nine commercial banking organizations would remain in the market after consummation. Four of Gateway's largest commercial bank competitors each would control more than 9 percent of market deposits and the two largest competitors would control more than 22 percent and 16 percent of market deposits, respectively. Although there has been no de novo entry in recent years, the Elizabeth City Market has economic characteristics that suggest it is modestly attractive for new entry. The market has experienced above-average population growth relative to the average of nonmetropolitan areas in North Carolina, and per capita income and deposits per banking office exceed the average for nonmetropolitan counties in the state. In addition, recent rates of increase in population and bank deposits in the market are

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controlling deposits of approximately $48 million or less than 1 percent of market deposits. Provident operates the 22nd largest depository institution in the market, controlling deposits of $42 million. On consummation of the proposal, Gateway would remain the 14th largest depository institution in the market, controlling deposits of $90 million or less than 1 percent of market deposits. The HHI would increase by 1 point to 1,325 and 21 institutions would remain in the market.

higher compared with national rates.

The Board also has considered that the market has a large and active credit union that offers a full range of retail banking products. North Carolina's State Employees' Credit Union ("SECU") is the second largest credit union in the United States, with more than $10 billion in total deposits. Approximately 75 percent of the residents in the market are eligible to become members of SECU. In addition, SECU operates street-level branches and multiple automated teller machines that are easily accessible to residents in the market. SECU controls approximately $68 million in deposits in the Elizabeth City Market. The Board concludes that this credit union exerts a competitive influence that mitigates, in part, the potential anticompetitive effects of the proposal.[13]

The Board concludes that the foregoing considerations, including the number and size of competitors that would remain in the Elizabeth City Market after consummation, the presence of a large, accessible credit union, the structure and attractiveness for entry of the market, and other factors, mitigate the transaction's potential anticompetitive effects. The Department of Justice has advised the Board that consummation of the proposal is not likely to have a significantly adverse competitive effect in the Elizabeth City Market. The Board also has received no objections to the proposal from the other federal banking agencies. Based on all the facts of record, the Board concludes that consummation of the proposed transaction would not likely result in a significantly adverse effect on competition or

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[13] With deposits of SECU included at 50 percent, Gateway would be the largest of eleven depository institutions in the market, with 20.8 percent of market deposits, and Provident would be the sixth largest depository institution in the market, controlling 7.6 percent of market deposits. On consummation of the proposal, Gateway would remain the largest depository institution in the market with deposits of $211.3 million or 28.4 percent of market deposits. The HHI would increase by 315 points to 1844.

on the concentration of banking resources in any relevant banking market and that competitive factors are consistent with approval.

Financial and Managerial Resources and Future Prospects

In reviewing the proposal under the Bank Merger Act, the Board has also carefully considered the financial and managerial resources and the future prospects of Gateway and the Provident branches to be acquired. The Board has reviewed these factors in light of all the facts of record, including confidential reports of examination assessing the financial and managerial resources of Gateway and information provided by Gateway. The Board notes that Gateway currently is well capitalized and is expected to remain so after consummation of the proposal. In addition, the Board has considered Gateway's plans to implement the proposal, including its available managerial resources. Gateway has sufficient financial and managerial resources to consummate the proposal. Based on all the facts of record, the Board concludes that the financial and managerial resources and future prospects of the institutions involved are consistent with approval of the proposal.

Convenience and Needs Considerations

In acting on the proposal, the Board also must consider its effects on the convenience and needs of the communities to be served and take into account the records of the relevant insured depository institutions under the CRA. 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.[14]

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[14] Interagency Questions and Answers Regarding Community Reinvestment, 66 Federal Register 36,620 and 36,639 (2001).

The Board has carefully considered the effects of the proposal on the convenience and needs of the communities to be served in light of all the facts of record, including Gateway's CRA performance record and other information from the bank. Gateway received an overall rating of "satisfactory" at its most recent CRA performance evaluation by the Federal Deposit Insurance Corporation ("FDIC"), as of April 1, 2001.[15] Provident also received a satisfactory overall rating at its most recent CRA performance evaluation by the FDIC, as of October 1, 2001. In addition, the Board notes that the three branches to be acquired are somewhat remote from Provident's main operations in Maryland and Northern Virginia. With their proximity to Gateway's branches, the bank plans for these branches to play a central role in expanding its community banking services in northeastern North Carolina and the Tidewater region of Virginia.

Based on these and all the facts of record, the Board has concluded that considerations relating to the convenience and needs of the communities to be served, including the CRA performance records of the institutions involved, are consistent with approval.

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 Bank Merger Act and other applicable statutes. The Board's approval is specifically conditioned on the commitments that Gateway made to the Board in connection with the application, including a commitment to comply with state law. These commitments are deemed to be conditions imposed in writing by the Board in connection with its findings and

[15] Gateway became a state member bank on October 1, 2001.

decisions and, as such, may be enforced in proceedings under applicable law.

The proposal 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 Richmond, acting pursuant to delegated authority.

By order of the Board of Governors,[16] effective August 3, 2004.

(signed)

Robert deV. Frierson
Deputy Secretary of the Board

[16] Voting for this action: Chairman Greenspan, Vice Chairman Ferguson, and Governors Gramlich, Bies, Olson, Bernanke, and Kohn.