

FEDERAL RESERVE SYSTEM

Five Star Bank
Warsaw, New York

Order Approving the Acquisition of Branches

Five Star Bank (“Five Star”), Warsaw, New York,¹ a state member bank, has applied under section 18(c) of the Federal Deposit Insurance Act² (“Bank Merger Act”) to acquire four branches of HSBC Bank USA, National Association (“HSBC”), McLean, Virginia (“New York Branches”), that First Niagara Bank, National Association (“First Niagara”), Buffalo, New York, contracted to purchase from HSBC.³ Five Star also has applied under section 9 of the Federal Reserve Act⁴ (“FRA”) to establish branches at the four branch locations.⁵

Notice of the proposal, affording interested persons an opportunity to submit comments, has been given in accordance with the Bank Merger Act and the Board’s Rules of Procedure.⁶ As required by the Bank Merger Act, a report on the competitive effects of the merger was requested from the United States Attorney General and a copy of that request was provided to the Federal Deposit Insurance Corporation (“FDIC”). The time for filing comments has expired, and the Board has considered the applications and all comments received in light of the factors set forth in the Bank Merger Act and the FRA.

¹ Five Star is a subsidiary of Financial Institutions, Inc., also of Warsaw, a financial holding company.

² 12 U.S.C. § 1828(c).

³ First Niagara acquired the right to purchase the New York Branches as part of its proposal to acquire 195 HSBC branches in New York and Connecticut. The Office of the Comptroller of the Currency (“OCC”) approved First Niagara’s proposal on April 19, 2012.

⁴ 12 U.S.C. § 321.

⁵ Those locations are listed in the appendix.

⁶ 12 CFR 262.3(b).

Five Star is the 40th largest insured depository institution in New York, controlling deposits of approximately \$2.2 billion, which represent less than 1 percent of the total amount of deposits in insured depository institutions in New York (“state deposits”).⁷ Five Star proposes to acquire \$217 million in total deposits from First Niagara, representing less than 1 percent of state deposits. On consummation of the proposal, Five Star would become the 37th largest insured depository institution in New York, controlling deposits of \$2.4 billion, representing less than 1 percent of state deposits.

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 any attempt to monopolize the business of banking.⁸ 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 effects of the transaction in meeting the convenience and needs of communities to be served.⁹

Five Star and the New York Branches compete directly in the New York banking markets of Elmira-Corning and Rochester.¹⁰ The Board has reviewed the

⁷ Data are as of June 30, 2011, and reflect the acquisition by Five Star of four other First Niagara branches on June 22, 2012. In this context, insured depository institutions include insured commercial banks, savings banks, and savings associations.

⁸ 12 U.S.C. § 1828(c)(5)(A).

⁹ 12 U.S.C. § 1828(c)(5)(B).

¹⁰ The Elmira-Corning banking market is defined as Chemung County; Cayuga, Dix, Montour, Orange, Reading, and Tyrone townships in Schuyler County; and Addison, Bath, Bradford, Cameron, Campbell, Caton, Corning, Erwin, Hornby, Jasper, Lindley, Rathbone, Thurston, Troupsburg, Tuscarora, Urbana, and Woodhulla townships in Steuben County, all in New York.

The Rochester banking market is defined as Genesee, Livingston, Monroe, Ontario, Seneca, Wayne, and Yates Counties; Alfred, Allen, Almond, Andover,

competitive effects of the proposal in those banking markets in light of all the facts of record. In particular, the Board has considered the number of competitors that would remain in the banking markets, the relative share of the total deposits in insured depository institutions in the market (“market deposits”) that Five Star would control,¹¹ the concentration levels of market deposits and the increase in those levels as measured by the Herfindahl-Hirschman Index (“HHI”) under the Department of Justice Bank Merger Competitive Review guidelines (“DOJ Bank Merger Guidelines”),¹² and other characteristics of the markets.

Angelica, Birdsall, Burns, Granger, Grove, Hume, Independence, and West Almond townships in Allegany County; Albion, Barre, Carlton, Clarendon, Gaines, Kendall, and Murray townships in Orleans County; Avoca, Canisteo, Cohocton, Dansville, Fremont, Greenwood, Hartsville, Hornellsville, Howard, Prattsburg, Pulteney, Wayland, Wayne, West Union, and Wheeler townships in Steuben County; and Castile, Covington, Gainesville, Genesee Falls, Middlebury, Perry, Pike, and Warsaw townships in Wyoming County, all in New York.

¹¹ In the Rochester banking market, deposit and market share data are based on data reported by insured depository institutions in the summary of deposits data as of June 30, 2011, 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 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 market share calculation on a 50 percent weighted basis. See, e.g., First Hawaiian, Inc., 77 Federal Reserve Bulletin 52 (1991). No savings associations operate in the Elmira-Corning banking market.

¹² 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 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 have issued revised Horizontal Merger Guidelines, the DOJ has confirmed that its Bank Merger Guidelines, which were issued in 1995, were not modified. Press Release, Department of Justice (August 19, 2010), available at www.justice.gov/opa/pr/2010/August/10-at-938.html.

In the Rochester banking market, consummation of the proposal would be consistent with Board precedent and within the thresholds in the DOJ Bank Merger Guidelines. On consummation of the proposal, the Rochester banking market would remain unconcentrated, as measured by the HHI, and numerous competitors would remain in the banking market.¹³

Five Star is the fifth largest insured depository institution in the Elmira-Corning banking market, controlling deposits of approximately \$191 million, which represent approximately 11 percent of market deposits.¹⁴ HSBC is the fourth largest insured depository institution in the market, controlling deposits of approximately \$246 million, which represent approximately 14.1 percent of market deposits. Five Star proposes to acquire \$173 million of those deposits, representing 9.9 percent of market deposits.¹⁵ On consummation of the proposal, Five Star would become the second largest depository institution in the Elmira-Corning banking market, controlling deposits of approximately \$364 million, which would represent 21.8 percent of market deposits. The HHI would increase 324 points, from 2188 to 2512.

¹³ In the Rochester banking market, Five Star operates the seventh largest insured depository institution, controlling deposits of approximately \$1.2 billion, which represent 7 percent of market deposits. The branch Five Star proposes to acquire currently controls \$61 million in deposits, but Five Star would acquire only \$44 million of the branch's deposits. After consummation, Five Star would remain the seventh largest insured depository institution in the market, controlling deposits of approximately \$1.3 billion, which represent 8.1 percent of market deposits. The HHI would decrease by 6 points, from 1079 to 1073, due to First Niagara's large presence in that banking market. On consummation of the proposal, 24 competitors would remain in the market.

¹⁴ Deposit and market share data are based on data reported by insured depository institutions in the summary of deposits data as of June 30, 2011, and reflect the acquisition by Community Bank, N.A., DeWitt, New York, of an HSBC branch in the Elmira-Corning banking market.

¹⁵ The proposed acquisition contemplates HSBC retaining \$73 million in deposits. HSBC would not retain an office in the Elmira-Corning market, and those deposits would be transferred out of the market.

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.¹⁶ In this market, there are several such factors. On consummation, eight other insured depository institutions, including three institutions that each control more than 10 percent of market deposits, would continue to operate in the market, including the market's largest competitor, Chemung Canal Trust Company, with 35.9 percent of market deposits.

Additionally, nine credit unions operate branches in the market. One credit union, First Heritage Federal Credit Union ("First Heritage"), exerts a significant competitive influence in the Elmira-Corning banking market.¹⁷ First Heritage offers a wide range of consumer products, operates street-level branches, and has membership open to almost all the residents in the market. First Heritage's activities in this banking market exert a sufficiently competitive influence to mitigate, in part, the potential competitive effects of the proposal. When First Heritage's deposits are considered on a 50 percent weighted basis, Five Star would control approximately 20 percent of the market deposits on consummation of the proposal, and the HHI would increase 267 points, from 1924 to 2191.

The Elmira-Corning banking market has other characteristics that also tend to mitigate potentially adverse competitive effects. Over the three year period ending in 2010, income in the market has grown faster than the state and national averages for metropolitan statistical areas and nonmetropolitan counties. The Elmira-Corning banking market also has experienced de novo entry in the last five years.

¹⁶ The number and strength of factors necessary to mitigate the competitive effects of a proposal depend on the size of the increase in, and resulting level of, concentration in a banking market. See NationsBank Corp., 84 Federal Reserve Bulletin 129 (1998).

¹⁷ The Board previously has considered competition from certain active credit unions as a mitigating factor. See, e.g., The Toronto-Dominion Bank, 96 Federal Reserve Bulletin B36 (2010); Regions Financial Corporation, 93 Federal Reserve Bulletin C16 (2007); Wachovia Corporation, 92 Federal Reserve Bulletin C183 (2006); F.N.B. Corporation, 90 Federal Reserve Bulletin 481 (2004).

The DOJ conducted a review of the potential competitive effects of the proposal 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 FDIC has been afforded an opportunity to comment and has 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 Elmira-Corning and Rochester banking markets, or in any other relevant banking market. Accordingly, the Board has determined that competitive considerations are consistent with approval.

Financial, Managerial, and Other Supervisory Factors

In reviewing this proposal under the Bank Merger Act and the FRA, the Board has considered the financial and managerial resources and future prospects of the institutions involved and the organization's nonbanking operations. In its evaluation, the Board considers a variety of information, including capital adequacy, asset quality, and earnings performance. The Board evaluates the financial condition of the pro forma organization, including its capital position, asset quality, and earnings prospects, and the impact of the proposed funding of the transaction. The Board also considers the ability of the organization to absorb the cost of the proposal and the proposed integration of the operations of the institutions. In assessing financial factors, the Board consistently has considered capital adequacy to be especially important.

Five Star is well capitalized and would remain so on consummation of the proposal. The proposed transaction is structured as a cash purchase of assets, and Five Star will fund the purchase from existing resources. The proposal would not negatively affect asset quality, and 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 Five Star and reviewed the examination records of Five Star, including assessments of its management, risk-management systems, and operations. In addition, the Board has considered its supervisory experiences and Five Star's records of compliance with applicable banking and anti-money-laundering laws. The Board also has considered Five Star's plans for implementing the proposal. Five Star is considered to be well managed and its board of directors and senior management have significant community banking experience. Five Star would operate the acquired branches under its existing policies and procedures, which are considered to be adequate.

Based on all the facts of record, the Board has concluded that considerations relating to the financial and managerial resources and future prospects of Five Star are consistent with approval, as are the other supervisory factors.

Convenience and Needs Considerations

The Bank Merger Act also requires the Board to consider the convenience and needs of the communities to be served and to take into account the records of the relevant depository institutions under the Community Reinvestment Act ("CRA").¹⁸ The CRA requires the federal financial supervisory agencies to encourage financial institutions to meet the credit needs of the local communities in which they operate, consistent with their safe and sound operation, and requires the appropriate federal financial supervisory agency to take into account an institution's record of meeting the credit needs of its entire community, including low- and moderate-income ("LMI") neighborhoods, in evaluating bank acquisition proposals. Accordingly, the Board has considered the convenience and needs factor and the CRA performance records of Five Star and HSBC in light of all the facts of record.

As provided in the CRA, the Board has evaluated the convenience and needs factor in light of the evaluations by the appropriate federal supervisors of the CRA

¹⁸ 12 U.S.C. § 2901 et seq.

performance records of the relevant insured depository institutions. 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.¹⁹

Five Star received an overall rating of "outstanding" at its most recent CRA performance examination by the Federal Reserve Bank of New York, as of August 2011. Examiners noted that 9 branches, representing 18 percent of Five Star's 49 existing branches, were in LMI areas. Examiners determined that this distribution of branches compared favorably with the percentage of the population in the bank's assessment area residing in LMI tracts (6 percent). As a result of this proposal, Five Star would operate 53 branches, of which 11 branches, or 20 percent, will be in LMI areas. Further, three of the branches will be in areas that are not currently part of Five Star's assessment area, and one of the three branches will be in an LMI area. HSBC received an overall rating of "outstanding" at its most recent CRA performance examination by the OCC, as of October 2009.

This proposal would result in customers of the four branches continuing to have access to banking services in their immediate communities. In three instances, existing Five Star branches will be consolidated with three New York Branches, and those consolidations will occur within the same census tract. In two of the consolidations, the distance between the branches involved is less than one mile. In the remaining consolidation, the branches are within 1.2 miles of each other.²⁰

¹⁹ See Interagency Questions and Answers Regarding Community Reinvestment, 75 Federal Register 11,642 at 11,665 (2010).

²⁰ The Board has considered that federal banking law provides a specific mechanism for addressing branch closings. Section 42 of the Federal Deposit Insurance Act, 12 U.S.C. § 1831r-1, as implemented by the Joint Policy Statement Regarding Branch Closings (64 Federal Register 34,844 (1999)), requires that a bank provide the public with at least 30 days' notice, and the appropriate federal supervisory agency and customers of the branch with at least 90 days' notice, before the date of the proposed branch closings. The bank also is required to provide reasons and other supporting

Based on all the facts of record and for the reasons discussed above, the Board concludes that considerations relating to convenience and needs, including the CRA performance records of the relevant depository institutions, are consistent with approval of the proposal.

Financial Stability

The Board has considered information relevant to risk to the stability of the United States banking or financial system. The proposed acquisition represents a de minimis transaction for financial stability purposes, and the proposed transaction would not materially increase the interconnectedness or complexity of Five Star. The Board, therefore, concludes that financial stability considerations in this proposal are consistent with approval.

Establishment of Branches

As noted, Five Star has applied under section 9 of the FRA to establish branches at the locations of the New York Branches, and the Board has considered the factors it is required to consider when reviewing an application under that section.²¹ Specifically, the Board has considered Five Star's financial condition, management, capital, actions in meeting the convenience and needs of the communities to be served, CRA performance, and investment in bank premises. For the reasons discussed in this order, the Board finds those factors to be consistent with approval.

Conclusion

Based on the foregoing and all the facts of record, the Board has determined that the applications should be, and hereby are, 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 the FRA. Approval of the

data for the closure, consistent with the institution's written policy for branch closings. Five Star has complied with those requirements.

²¹ See 12 U.S.C. § 322; 12 CFR 208.6.

applications is specifically conditioned on compliance by Five Star with all the commitments made in connection with this proposal and the conditions set forth in this order. The commitments and conditions are deemed to be conditions imposed in writing by the Board and, as such, may be enforced in proceedings under applicable law.

Acquisition of the branches 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 by the Federal Reserve Bank of New York, acting pursuant to delegated authority.

By order of the Board of Governors,²² effective July 27, 2012.

(signed)

Robert deV. Frierson
Deputy Secretary of the Board

²² Voting for this action: Chairman Bernanke, Vice Chair Yellen, and Governors Duke, Tarullo, Raskin, Stein, and Powell.

Appendix

New York Branches to be Acquired

1. 150 Lake Street, Elmira 14901
2. 309 S. Main Street, Horseheads 14845
3. 217 Prescott Avenue, Elmira Heights 14903
4. 102 N. Main Street, Albion 14411