

FEDERAL RESERVE SYSTEM

Midland States Bancorp, Inc.
Effingham, Illinois

Order Approving the Acquisition of a Savings and Loan Holding Company,
the Merger of Banks, and the Establishment of Branches

Midland States Bancorp, Inc. (“Midland”), Effingham, Illinois, a financial holding company within the meaning of the Bank Holding Company Act (“BHC Act”), has requested the Board’s approval under sections 4(c)(8) and 4(j) of the BHC Act¹ to acquire by merger Love Savings Holding Company (“LSHC”) and its wholly owned subsidiary, Heartland Bank, FSB (“Heartland Bank”), both of St. Louis, Missouri.²

In addition, Midland’s subsidiary state member bank, Midland States Bank (“Midland Bank”), Effingham, Illinois, has requested the Board’s approval to merge with Heartland Bank pursuant to section 18(c) of the Federal Deposit Insurance Act (“Bank Merger Act”), with Midland Bank as the surviving entity (the “Merger”).³ Midland Bank has also applied under section 9 of the Federal Reserve Act (“FRA”) to establish and operate branches at the locations of Heartland Bank’s main office and branches.⁴

Notice of the proposals, affording interested persons an opportunity to submit comments, has been published in the Federal Register (78 Fed. Reg. 61845 (October 4, 2013)) in accordance with the Bank Merger Act and the Board’s Rules of

¹ 12 U.S.C. §§ 1843(c)(8) and (j).

² LSHC is currently controlled by members of the Love family. The Love family controls Heartland Bank through direct ownership and controlled entities. Five of these vehicles are registered savings and loan holding companies: The Love Family 1941 Trust, The Love Family Charitable Trust, The Love Family Testamentary Trust, The Love Group Joint Venture, and The Love Real Estate Company.

³ 12 U.S.C. § 1828(c).

⁴ 12 U.S.C. § 321. These locations are listed in the appendix to this order.

Procedure.⁵ As required by the Bank Merger Act, a report on the competitive effects of the Merger was requested from the United States Attorney General. The time for filing comments has expired, and the Board has considered the proposals and all comments received in light of the factors set forth in section 4 of the BHC Act, the Bank Merger Act, and the FRA.

Midland, with total consolidated assets of approximately \$1.7 billion, is the 408th largest depository organization in the United States, controlling deposits of approximately \$1.4 billion, which represent less than 0.1 percent of the total amount of deposits of insured depository institutions in the United States (“national deposits”).⁶ Midland Bank operates branches in Illinois and Missouri. Midland Bank is the 32nd largest insured depository institution in Illinois, with deposits representing less than one percent of total deposits of insured depository institutions in that state. Midland Bank is the 296th largest insured depository institution in Missouri, with deposits representing less than 0.1 percent of total deposits of insured depository institutions in that state (“state deposits”).⁷

LSHC, with total consolidated assets of approximately \$845.0 million, controls deposits of approximately \$662.5 million. Heartland Bank operates branches in Missouri and Colorado and is the 33rd largest insured depository institution in Missouri, with deposits representing 0.4 percent of the total amount of state deposits.

On consummation of the proposed transactions, Midland would become the 281st largest depository organization in the United States and would become the 32nd largest depository organization in Missouri. Midland would control deposits of

⁵ 12 CFR 262.3(b).

⁶ Asset and nationwide deposit ranking data are as of December 31, 2013. In this context, insured depository institutions include insured commercial banks, savings banks, and savings associations.

⁷ State market share and ranking data are as of June 30, 2013.

approximately \$2.1 billion nationwide and approximately \$678.1 million in Missouri, representing less than 0.1 percent of national deposits and 0.5 percent of state deposits.

The Board previously has determined by regulation that the operation of a savings association by a bank holding company is closely related to banking for purposes of section 4(c)(8) of the BHC Act.⁸ The Board requires that savings associations acquired by bank holding companies conform their direct and indirect activities to those permissible for bank holding companies under section 4 of the BHC Act.⁹ Midland has represented that all activities of LSHC will, upon consummation, be permissible for a bank holding company to conduct.

Interstate and Deposit Cap Analyses

The Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”) amended section 4 of the BHC Act¹⁰ and the Bank Merger Act¹¹ to provide that, in general, the Board may not approve an application by a bank holding company to acquire an insured depository institution, or an application by one insured depository institution to acquire another insured depository institution, if the home state of the target insured depository institution is a state other than the home state of the applicant and the applicant controls or would control more than 10 percent of the total amount of deposits of insured depository institutions in the United States (collectively, “nationwide deposit caps”).¹² The intended purpose of the nationwide deposit caps was to help guard against undue concentrations of economic power.¹³ For purposes of the

⁸ 12 CFR 225.28(b)(4)(ii).

⁹ 12 CFR 225.28(b)(4)(ii).

¹⁰ Dodd-Frank Act § 623(b), codified at 12 U.S.C. § 1843(i)(8).

¹¹ Dodd-Frank Act § 623(a), codified at 12 U.S.C. § 1828(c)(13).

¹² For a detailed discussion of the nationwide deposit cap, see Bank of America Corporation/LaSalle, 93 Federal Reserve Bulletin C109, C109-C110 (2007); Bank of America Corporation/Fleet, 90 Federal Reserve Bulletin 217, 219-220 (2004) (“Fleet Order”).

¹³ Fleet Order at 219.

BHC Act and the Bank Merger Act, the home state of Midland is Illinois and the home state of Heartland Bank is Missouri.¹⁴

Based on the latest available data reported by all insured depository institutions in the United States, the total amount of deposits of insured depository institutions is \$11.0 trillion.¹⁵ On consummation of the proposed transaction, Midland would control less than 0.1 percent of the total amount of deposits in insured depository institutions in the United States. Accordingly, in light of all the facts of record, the Board is not required to deny the proposals under section 4(i) of the BHC Act or under the Bank Merger Act.

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.¹⁶ 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

¹⁴ A bank holding company's home state is the state in which the total deposits of all banking subsidiaries of such company were the largest on July 1, 1966, or the date on which the company became a bank holding company, whichever is later. 12 U.S.C. § 1841(o)(4)(C). For a state bank, the home state is the state by which the bank is chartered. 12 U.S.C. § 1828(c)(13)(C)(ii)(II). For a federal savings association, the home state is the state in which the home office of the savings association is located. 12 U.S.C. § 1828(c)(13)(C)(ii)(III); 12 U.S.C. § 1841(o) (4)(E).

¹⁵ See Fleet Order at 219. Deposit data are calculated based on reports filed by insured depository institutions and are as of December 31, 2013. Each bank and savings association insured by the Federal Deposit Insurance Corporation ("FDIC") in the United States must report data regarding its total deposits in accordance with the definition of "deposit" under the Federal Deposit Insurance Act, 12 U.S.C. § 1813(I), on the institution's Consolidated Report of Condition and Income. Deposit data for FDIC-insured U.S. branches of foreign banks and federal branches of foreign banks are obtained from the Report of Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks. These data are reported quarterly to the FDIC and are publicly available.

¹⁶ 12 U.S.C. § 1828(c)(5).

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.¹⁷ In addition, the Board must consider the competitive effects of a proposal to acquire a savings association under the public benefits factor of section 4(j) of the BHC Act.¹⁸

Midland Bank and Heartland Bank compete directly in the St. Louis, Missouri, banking market.¹⁹ The Board has reviewed the competitive effects of the proposals 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 shares of the total deposits in insured depository institutions in the market (“market deposits”) that Midland Bank would control,²⁰ 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

¹⁷ 12 U.S.C. § 1828(c)(5)(B).

¹⁸ 12 U.S.C. § 1843(j)(2)(A).

¹⁹ The St. Louis, Missouri, banking market consists of the city of Saint Louis; Franklin, Jefferson, Lincoln, Saint Charles, Saint Louis, Warren and Washington counties; Roark, Boeuf, Canaan and Brush Creek townships, including the cities of Hermann and Owensville, in Gasconade County; Boone township in Crawford County; Loutre township in Montgomery County, all in Missouri; also Bond, Calhoun, Clinton, Jersey, Macoupin, Madison, Monroe and St. Clair counties; the western part of Randolph County, defined by Route 3 on the east and the Kaskaskia River on the south, including the cities of Red Bud, Ruma and Evansville; Washington County (minus Ashley and Du Bois townships); and the entire city of Centralia, all in Illinois.

²⁰ Deposit and market share data are based on data reported by insured depository institutions in the summary of deposits data as of June 30, 2013, and are based on calculations in which the deposits of thrift institutions are included. 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 market share calculation on a 50 percent weighted basis. *See, e.g., First Hawaiian, Inc.*, 77 Federal Reserve Bulletin 53 (1991).

Review guidelines (“DOJ Bank Merger Guidelines”),²¹ and other characteristics of the market.

Consummation of the proposed transactions would be consistent with Board precedent and within the thresholds in the DOJ Bank Merger Guidelines in the banking market. On consummation of the proposal, the St. Louis, Missouri, banking market would remain unconcentrated, as measured by the HHI. The changes in the HHI’s measure of concentration would be minimal, and numerous competitors would remain in the banking market.²²

The DOJ has conducted a review of the potential competitive effects of the proposed transactions and has advised the Board that consummation of the transactions 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 proposals.

²¹ 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 the DOJ 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.

²² The HHI would decrease in the market by 5 points. This decrease results from a pre-merger weighting of Heartland Bank’s market deposits at 50 percent and a post-merger weighting at 100 percent. See Norwest Corporation, 78 Federal Reserve Bulletin 452 (1992); First Banks, Inc., 76 Federal Reserve Bulletin 669 (1990) (deposits of thrifts are included in pre-merger market share calculations on a 50 percent weighted basis but included at 100 percent in the calculation of pro forma market share because the deposits would be acquired by a commercial banking organization). The pro forma market share of Midland Bank would be 1.11 percent, and 142 competitors would remain.

Based on all the facts of record, the Board concludes that consummation of the proposed transactions would not have a significantly adverse effect on competition or on the concentration of resources in the St. Louis, Missouri banking market or any other relevant banking market. Accordingly, the Board has determined that competitive considerations are consistent with approval.

Financial, Managerial, and Other Supervisory Factors

In addition to assessing competitive effects of the merger, in every case under the Bank Merger Act, the Board must take into consideration the financial and managerial resources and future prospects of the existing and proposed institutions, the convenience and needs of the communities to be served, records of compliance with anti-money-laundering laws, and the risk to the stability of the United States banking or financial system.²³ The Board also considers these factors in weighing the possible adverse effects against the public benefits of the transaction, as required by section 4(j) of the BHC Act.²⁴

In evaluating financial condition and future prospects of the proposal, the Board considers a variety of information, including capital adequacy, asset quality, and

²³ 12 U.S.C. § 1828(c)(5).

²⁴ Section 4(j)(2)(A) of the BHC Act requires the Board to consider whether the proposed acquisition of LSHC “can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interests, unsound banking practices, or risk to the stability of the United States banking or financial system.” 12 U.S.C. § 1843(j)(2)(A). As part of its evaluation of these factors, the Board reviews the financial and managerial resources of the companies involved, the effect of the proposal on competition in the relevant markets, the risk to the stability of the United States banking or financial system, records of compliance with anti-money-laundering laws, and the public benefits of the proposal. See 12 CFR 225.26; see, e.g., Capital One Financial Corporation, FRB Order 2012-2 (February 14, 2012) (“Capital One Order”); Bank of America Corporation/Countrywide, 94 Federal Reserve Bulletin C81 (2008); Wachovia Corporation, 92 Federal Reserve Bulletin C138 (2006); BancOne Corporation, 83 Federal Reserve Bulletin 602 (1997). In acting on a notice to acquire a savings association, the Board

earnings performance. The Board evaluates the financial condition of the pro forma organization, including its capital position, asset quality, liquidity, and earnings prospects, and the impact of the proposed funding of the transactions. The Board considers the future prospects of the organizations involved in the proposals in light of their financial and managerial resources and the proposed business plan. The Board also considers the ability of the organization to absorb the costs of the proposals 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.

Midland and Midland Bank are well capitalized and would remain so on consummation of the proposed transactions. Midland would acquire LSHC in exchange for a combination of cash and Midland common shares.²⁵ Midland would fund the transaction through a combination of cash on hand and additional fundraising. The asset quality, earnings prospects, and liquidity of Midland are considered consistent with approval. Midland appears to have adequate resources to absorb the costs of the proposal and to complete the integration of Midland Bank's and Heartland Bank's operations. Future prospects also are considered consistent with approval. Based on its review of the record, the Board finds that Midland has sufficient financial resources to effect the proposed transactions.

The Board also has considered the managerial resources of the organizations involved and has reviewed supervisory information and the examination records of Midland and Midland Bank, including assessments of their management, risk-management systems, and operations. In addition, the Board has considered its supervisory experiences with the organizations and their records of compliance with

reviews the records of performance of the relevant insured depository institutions under the Community Reinvestment Act ("CRA"). 12 U.S.C. § 2901 *et seq.*

²⁵ Upon consummation, shareholders of LSHC would acquire a significant number of Midland common shares. The Love family has filed a notice under the Change in Bank Control Act of 1978, as amended, 12 U.S.C. 1817(j), with respect to this share acquisition. The Board is acting separately on this notice.

applicable banking and anti-money-laundering laws. The Board also has considered Midland's plans for implementing the proposed transactions. In addition, the Board has considered comments submitted as part of the public comment process. These comments allege weaknesses in Midland's compliance management as it relates to consumer protection practices. Commenters criticized Midland's consumer compliance practices, particularly related to fair lending laws and the CRA.

Midland and Midland Bank are considered to be well managed, and their boards of directors and senior management have significant banking experience. Midland has a demonstrated record of successfully integrating organizations into its operations and risk-management systems following acquisitions, having successfully completed several acquisitions of banking organizations since 2007. Midland would implement at the combined organization its existing policies, procedures, and controls, which are considered to be satisfactory. Midland's management has the experience and resources that should allow the combined organization to operate in a safe and sound manner. The Board expects that Midland will ensure that its risk-management framework and methodologies, including its compliance functions, are commensurate with its new size and complexity.

Based on all the facts of record, including a review of the comments received, the Board has concluded that considerations relating to the financial and managerial resources of the organizations involved, as well as the records of effectiveness of Midland and Midland Bank in combatting money-laundering activities, are consistent with approval.

Convenience and Needs Considerations

In acting on a proposal under the Bank Merger Act, the Board must consider the convenience and needs of the communities to be served and take into account the records of the relevant depository institutions under the CRA.²⁶ As noted,

²⁶ 12 U.S.C. § 2901 et seq.

the Board also must review the records of performance under the CRA of the relevant insured depository institutions when acting on a notice under section 4 of the BHC Act to acquire a savings association. 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,²⁷ and requires the appropriate federal financial supervisory agency to 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.²⁸

The Board has considered all the facts of record, including reports of examination of the CRA performance of Midland Bank and Heartland Bank, data reported by Midland Bank and Heartland Bank under the Home Mortgage Disclosure Act of 1975, as amended ("HMDA"),²⁹ other information provided by Midland, confidential supervisory information, and the public comments received on the proposals. Two commenters expressed concern over levels of lending based on data released under the HMDA or the CRA. They also asserted that the record failed to establish sufficient public benefit to warrant approval. Each commenter requested that the Board require specific commitments from Midland to improve services to underserved communities. A third commenter withdrew its initial opposition to the proposal and urged approval of the proposed transactions after an affiliate of the commenter reached an agreement with Midland to enhance its community development activities and services to predominantly minority communities in specific ways over the next few years.

²⁷ 12 U.S.C. § 2901(b).

²⁸ 12 U.S.C. § 2903.

²⁹ 12 U.S.C. 2801 et seq.

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 supervisor of the CRA performance of the relevant institution.³⁰ 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.³¹ 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 Midland Bank

Midland Bank was assigned an overall "satisfactory" rating at its most recent CRA performance evaluation by the Federal Reserve Bank of St. Louis ("Reserve Bank") following an examination that commenced in October 2013 and was delivered to Midland Bank in July 2014 ("Midland Bank Evaluation").³² This was the first CRA examination for Midland Bank conducted under the Interagency Procedures for Large Institutions; the previous CRA examination was conducted under procedures for intermediate small institutions. Because the operations of Midland Bank are concentrated in Illinois, with a relatively small presence in the St. Louis Metropolitan Statistical Area ("MSA"), examiners gave primary consideration to Midland Bank's performance in

³⁰ See Interagency Questions and Answers Regarding Community Reinvestment, 75 Federal Register 11642, 11665 (2010).

³¹ 12 U.S.C. § 2906.

³² The evaluation periods for the Midland Bank Evaluation were January 1, 2011, to December 31, 2012, for HMDA and small farm lending; June 4, 2011, to December 31, 2012, for small business lending; and August 22, 2011, to October 15, 2013, for community development loans, investment, and service activities.

Illinois. The CRA examination was conducted during the pendency of this application and was informed by the public comments on the proposal.

Examiners assigned Midland Bank overall component ratings of “high satisfactory” on the Lending Test, “low satisfactory” on the Investment Test, and “low satisfactory” on the Service Test. Examiners described Midland Bank’s record of lending as adequate but with opportunities for improvement in certain areas. Midland Bank was described as having a lending record that reflected good responsiveness to assessment area credit needs and a geographically adequate distribution of loans among customers of different income levels and among businesses of different sizes. Examiners identified Midland Bank as a leader in making community development loans in the St. Louis MSA assessment area, with an overall adequate level of community development lending due to low levels in Illinois. Examiners described the bank as maintaining a significant level of community development investments and grants, and making numerous grants to, community development organizations in certain assessment areas, but no community development investments in one assessment area in Illinois.

Examiners found that Midland Bank’s record of opening and closing branches in its assessment areas had not adversely affected the accessibility of its delivery systems, but noted that branch hours and services generally did not vary to accommodate customers with variable work schedules. Examiners praised Midland Bank’s community development services and systems accessibility in Illinois, while stating that its delivery systems, including branches, in the St. Louis MSA assessment area were located principally outside the St. Louis Missouri-Illinois urban area (as determined by the 2010 United States Census), making it difficult to serve the urban areas of the assessment area where the majority of LMI census tracts are located. Examiners also found that Midland Bank made use of innovative and/or flexible products in its assessment areas.

Thus, Midland Bank received a mixture of praise and suggestions for improvement from examiners in connection with the determination by examiners that its

overall performance was “satisfactory.” During the course of the Midland Bank Evaluation, examiners did not find any evidence that Midland Bank engaged in discriminatory or other illegal credit practices.

CRA Performance of Heartland Bank

Heartland Bank was assigned an overall “satisfactory” rating at its most recent CRA performance evaluation by the Office of the Comptroller of the Currency (“OCC”) following an examination that commenced in August 2013 (“Heartland Bank Evaluation”). Heartland Bank received a “satisfactory” rating for the Lending Test and an “outstanding” rating for the Community Development Test.³³ In evaluating the Lending Test in the St. Louis assessment area, OCC examiners concluded that Heartland Bank’s lending to individuals with different income levels was excellent and that lending to businesses of different sizes was reasonable. Examiners found that the geographic distribution of loans in the St. Louis assessment area reflected reasonable dispersion. Examiners also found that Heartland Bank made a high level of community development loans that reflected excellent responsiveness to the need for affordable housing in the assessment area. Examiners found that Heartland Bank’s community development investments reflected adequate responsiveness, while its community development services reflected reasonable responsiveness to the needs of the assessment area. In particular, examiners noted that Heartland Bank’s branch and ATM network, along with online and mobile banking, made it reasonably accessible to geographies and individuals with different income levels.

³³ The Heartland Bank Evaluation was conducted using Small Bank CRA evaluation procedures in Heartland Bank’s two assessment areas of St. Louis, Missouri, and Denver, Colorado. For the Lending Test, examiners reviewed data from January 1, 2011, to December 31, 2012. For the Community Development Test, examiners reviewed data from June 17, 2008, to August 29, 2013.

B. Fair Lending and Other Consumer Protection Laws

The Board has considered the records of Midland Bank and Heartland Bank in complying with fair lending and other consumer protection laws. As part of this consideration, the Board reviewed the Midland Bank Evaluation and the Heartland Bank Evaluation, assessed the records of Midland Bank and Heartland Bank in helping to meet the credit needs of their communities, and considered the comments received on the proposals as well as other agencies' views on the records of performance of Midland Bank and Heartland Bank under fair lending laws. The Board also considered Midland Bank's fair lending policies and procedures. As noted, the Midland Bank Evaluation was conducted during the pendency of this application and was informed by the public comments on the proposals. In addition, in response to the public comments on the proposal, the Reserve Bank conducted a fair lending examination during the pendency of this application, including a redlining review across Midland Bank's assessment areas. The Board has relied on the findings of that examination as part of its analysis.

HMDA Data and Fair Lending Analysis

The commenters criticized Midland Bank's record of mortgage lending to minority individuals based generally on their review of 2011 and 2012 HMDA data for the bank's five CRA assessment areas, with emphasis on the bank's St. Louis MSA assessment area.³⁴ The commenters asserted that Midland Bank's volume of mortgage loans to African American, Hispanic, and Asian individuals and to minority communities has been extremely low compared to the volume of loans originated to these populations and communities by the aggregate of all lenders and compared to the demographics of those areas.³⁵

³⁴ One commenter's discussion of Midland Bank's HMDA data covered the years 2009 through 2012.

³⁵ Aggregate lending is defined as the number of loans originated and purchased by all reporting lenders as a percentage of the aggregate number of loans originated and purchased by all reporting lenders in the metropolitan or assessment area. In this context,

Midland Bank's branches in the St. Louis MSA assessment area are in suburban or rural areas on the outskirts of the MSA. Midland Bank argued that its lending activities in the St. Louis MSA assessment area were appropriate given its relatively small economic presence in the market. Midland Bank identified community development organizations and projects with which it was involved, as well as organizations and projects with which Heartland was involved. Midland has stated that it expects to continue Heartland Bank's participation in community-based programs.

The Board analyzed Midland Bank's HMDA data for 2011, 2012, and 2013 in the St. Louis MSA, Champaign-Urbana MSA, Chicago-Naperville-Michigan City CSA, Central Illinois, and Northern Illinois assessment areas. The Board analyzed data related to HMDA-reportable loans to develop a view of Midland Bank's overall lending patterns, as well as the subsets of those data related specifically to the public comments received on the proposed transactions. The Board analyzed each bank's combined assessment areas and the specific market areas addressed in the public comments. Within those data sets, the Board focused its review on data related to concerns highlighted by the public comments, including lending to minority individuals and communities and to LMI individuals and communities.

The Board is concerned when HMDA data for an institution indicate lending disparities and believes that all lending institutions are obligated to ensure that their lending practices are based on criteria that are consistent with safe and sound lending but also provide equal access to credit by creditworthy applicants, regardless of their race or ethnicity. Although the HMDA data may reflect certain disparities in the rates of loan applications, originations, and denials among members of different racial or ethnic groups in certain local areas, HMDA data alone do not provide a sufficient basis on which to conclude whether the bank excluded or denied credit to any group on a

aggregate lending is considered an indicator of the lending opportunities in the geographic area in which the bank is located.

prohibited basis.³⁶ Fully evaluating a bank's compliance with fair lending laws and regulations would require a thorough review of the bank's application and underwriting policies and procedures, as well as access to information contained in the application files, to determine whether the observed lending disparities persist after taking into account legitimate underwriting factors.

The Board's review generally confirmed the levels of lending by Midland Bank to African American, Hispanic, Asian, and LMI borrowers and the denial disparity ratios noted by the commenters. The Board notes that Midland Bank's record of lending to LMI tracts and to majority-minority tracts generally exceeds that of the aggregate, but that the volume of applications is low compared to the aggregate. As part of the Midland Bank Evaluation, examiners found that Midland Bank had good lending activity and a high percentage of loans in its assessment areas, and that it makes use of innovative and/or flexible products throughout its assessment areas. Midland Bank's percentage of applications from and loans to LMI borrowers for these loan types generally exceeded the aggregate in the St. Louis MSA assessment area. However, with respect to conventional home purchase, refinancing, and home improvement loans, Midland Bank's lending data in the St. Louis MSA assessment area showed low levels of applications from minority individuals, as well as a low level of loans to those in predominantly minority and LMI census tracts.³⁷

³⁶ The data, for example, do not account for the possibility that an institution's outreach efforts may attract a larger proportion of marginally qualified applicants than other institutions attract and do not provide a basis for an independent assessment of any applicant's creditworthiness. In addition, information on credit history problems, excessive debt levels relative to income, and high loan amounts relative to the value of the real estate collateral (the reasons most frequently cited for a credit denial or higher credit cost) is not always available from HMDA data.

³⁷ The Board analyzed Heartland Bank's 2011, 2012, and 2013 HMDA data in its primary market, the St. Louis MSA assessment area. Commenters focused on the St. Louis MSA assessment area and were generally favorable when discussing Heartland Bank's mortgage lending record relative to the aggregate. Commenters expressed concern that the acquisition of Heartland Bank by Midland would remove an above

The Board considered and placed great emphasis on information collected by, and on the assessment of, the Reserve Bank's fair lending examiners. As noted, contemporaneously with the Midland Bank Evaluation, Reserve Bank examiners conducted a fair lending and redlining review at Midland Bank, including a review of matters related to the concerns raised by the commenters. While examiners noted a low volume of applications from minority individuals, examiners found no significant disparities in denials in areas with high minority populations.

Examiners focused their review on Midland Bank's branching and marketing practices in each of Midland Bank's assessment areas. Commenters expressed concerns over Midland Bank's branch locations, currently and when combined with Heartland Bank's branches. Specifically, commenters stated that none of Midland Bank's 32 branches is in a majority-minority tract or a low-income tract, while two are in moderate-income tracts. For the St. Louis MSA assessment area, commenters observed that none of Midland Bank's 11 current branches is located in the city of St. Louis, which contains a high percentage of the assessment area's LMI tracts and majority-minority tracts, and that none of Heartland Bank's 11 Missouri branches is located in majority-minority tracts. Examiners generally observed that Midland Bank has expanded its geographic reach outward from a small core presence in Illinois, primarily through a series of acquisitions. Examiners found that the geographic expansion appeared to have been undertaken without deliberate avoidance of majority-minority census tracts.

For instance, in the St. Louis MSA, most of Midland Bank's branches are located in southwestern Illinois, technically within the MSA but on its suburban and rural

average lender from the market while increasing the presence of a lender with an inferior record of serving the needs of the community. The Board reviewed Heartland Bank's HMDA data and confirmed that in 2011, 2012, and 2013, Heartland Bank's percentages of loans to African Americans exceeded those of the aggregate and, for Hispanics, generally exceeded those of the aggregate. In addition, Heartland Bank's percentages of loans to LMI borrowers consistently exceeded those of the aggregate. As discussed above, Midland Bank has stated that it will continue Heartland Bank's participation in community-based programs.

outskirts. The acquisition of these branches was part of an outward accretion of Midland's presence in that area. One branch currently within the St. Louis MSA was not in the MSA when Midland Bank acquired the branch, but the MSA was later expanded. Midland Bank's two branches within the urban portions of the St. Louis MSA are on the outer edges of the urban area. Examiners further noted that, although its branches were generally in rural or suburban areas, Midland Bank's pattern of branching suggests movement towards the majority-minority census tracts at the core of the St. Louis MSA. Branching patterns in Midland Bank's other assessment areas, including the Joliet-Kankakee and Champaign MSAs, were similar to Midland Bank's expansion in the St. Louis MSA.

Examiners concluded that Midland Bank's policies and procedures to address fair lending risks, and the implementation of those policies and procedures, were satisfactory. Examiners identified several areas for improvement, including opportunities to expand marketing; to enhance fair lending compliance management and monitoring; and to evaluate its marketing, outreach, and branching practices to ensure that majority-minority areas and customers are being adequately served.

Midland Bank is addressing the identified areas for improvement and, in connection with this transaction, has committed to continue doing so. For example, Midland Bank recently hired a Community Development and CRA Officer with experience in the St. Louis area, has begun working more closely with community groups in its assessment areas, and has enhanced its fair lending policies and procedures as directed. Midland Bank has also developed a community development plan and begun its implementation, including updating products and services to better serve low- and moderate-income borrowers and preparing to open a branch in a majority-minority, low-income census tract in Joliet, Illinois.

Midland Bank's Small Business Lending Record

Commenters generally noted that Midland Bank's record of originating small business loans in LMI tracts improved significantly from 2011 to 2012. However, commenters argued that the bank's lending volume could be improved in LMI areas, particularly in the St. Louis MSA assessment area. The Midland Bank Evaluation found Midland Bank's record of lending to businesses of different sizes to be adequate or good in its assessment areas. In addition, Midland Bank's volume of loans to LMI tracts generally met or exceeded the aggregate for the periods reviewed.

Midland Bank's Fair Lending Program

Midland Bank has established policies and procedures to help ensure compliance with all fair lending and other consumer protection laws and regulations, and these are considered satisfactory from a supervisory perspective. Midland Bank's compliance program is included as part of its overall risk management and involves participation of the compliance department, committees of the board of directors, senior management, and employees. Midland Bank's public community development plan states that it will continue to maintain fair lending policies and practices that meet all legal requirements, including continuing to conduct a second review of all loans initially denied, continuing to require all employees and directors involved in lending to complete annual fair lending training, and seeking to ensure that third-party agents involved in Midland Bank's lending activities receive appropriate fair lending training.

Senior staff at Midland Bank conduct quarterly compliance testing, and Midland Bank has retained an independent third-party vendor to conduct annual compliance testing. Midland Bank also periodically retains third parties to conduct comprehensive reviews of its loan operations. As noted, Midland Bank has hired a new Community Development and CRA Officer and is in the process of adding personnel to its compliance staff and considering enhancements to its compliance systems.

Certain lines of business have enhanced compliance oversight. Underwriting, pricing, and policy exceptions for residential mortgages are reviewed by senior staff, with

denials subjected to a second review. Midland Bank's Loan Committee receives reports on exceptions on a monthly basis. Similarly, Midland Bank has taken steps to more closely monitor dealers involved in its indirect auto lending program. Midland Bank's risk-management systems and its policies and procedures for assuring compliance with fair lending laws would be implemented at the combined organization, with modifications Midland Bank has been making in anticipation of the proposed transactions.

C. 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. As noted, commenters asserted that the proposed transactions would not product sufficient public benefits to warrant approval of the proposed transactions.

The Board has considered that the proposed transactions would allow Midland to expand the range of financial products and services available to existing customers of Heartland Bank. Following consummation of the proposed transactions, Heartland Bank's customers would gain access to additional services provided by Midland Bank, such as investment management, trust services, private banking, brokerage services, and expanded card products. In addition, customers of both institutions would benefit from a more expansive branch and ATM network. The proposed transactions would provide the opportunity for operational efficiencies, cost savings, and revenue enhancement for the combined organization.

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 Midland, confidential supervisory information, the public comments on the proposals, and commitments made by Midland. Based on the Board's assessment of the CRA

performance and consumer compliance programs of Midland Bank and Heartland Bank, its review of examination reports, its analysis of the HMDA data, and its consultations with other agencies, the Board concludes that the convenience and needs factor, including the CRA records of the insured depository institutions involved in the proposed transactions, is consistent with approval of the proposals.

The Board expects Midland to continue to make progress in addressing areas identified for improvement. In order to ensure that Midland continues to do so, Midland has committed to the Board that it will make specific enhancements related to its marketing and outreach, compliance management and monitoring, and branching before undertaking any future expansion.

Financial Stability

The Dodd-Frank Act added “risk to the stability of the United States banking or financial system” to the list of possible adverse effects that the Board must weigh against any expected public benefits in considering proposals under section 4(j) of the BHC Act, and as a factor that must be considered under the Bank Merger Act.³⁸

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 merged 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

³⁸ Dodd-Frank Act, § 604(e) and (f), codified at 12 U.S.C. §§ 1843(j)(2)(A) and 1828(c)(5). Other provisions of the Dodd-Frank Act impose a similar requirement that the Board consider or weigh the risks to financial stability posed by a merger, acquisition, or expansion proposal by a financial institution. See sections 163, 173, and 604(d) of the Dodd-Frank Act.

resulting firm.³⁹ 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.⁴⁰

The Board has considered information relevant to risks to the stability of the United States banking or financial system. After consummation of the proposed transactions, Midland would have approximately \$2.6 billion in consolidated assets and would be outside the largest 100 financial institutions in the United States. 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 total 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 interconnectedness, complexity, cross-border activities, or other risk factors. Such additional risk factors are not present in the proposed transactions. The companies engage, and Midland would continue to engage, in traditional banking activities. The resulting organization would experience small increases in the metrics that the Board considers to measure an institution's complexity and interconnectedness, with the resulting firm generally ranking outside of the top 100 U.S. financial institutions in terms of those metrics. For example, Midland's intrafinancial assets and liabilities would constitute a negligible share of the system-wide total, both before and after the transaction. The resulting organization would not engage in complex activities or provide critical services in such volume that disruption in those services would have a significant impact on the macroeconomic condition of the United States by disrupting trade or resulting in increased resolution difficulties.

³⁹ Many of the metrics considered by the Board measure an institution's activities relative to the U.S. financial system.

⁴⁰ For further discussion of the financial stability standard, see Capital One Order at 28.

In light of all the facts and circumstances, the proposed transactions 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 has determined that considerations relating to financial stability are consistent with approval.

Additional Public Benefits of the Proposals

As noted above, in connection with a notice under section 4(c)(8) of the BHC Act, section 4(j) of the Act requires the Board to “consider whether performance of the activity by a bank holding company or a subsidiary of such company can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interests, unsound banking practices, or risk to the stability of the United States banking or financial system.”⁴¹ As noted, commenters asserted that the proposed transactions would not produce sufficient public benefits to warrant approval of the proposed transactions. As discussed above, the Board has considered that the proposed transactions would allow Midland Bank to expand the range of financial products and services available to existing customers of Heartland Bank. The Board has determined that the conduct of the proposed nonbanking activities within the framework of Regulation Y, Board precedent, and this order is not likely to result in significant adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interests, unsound banking practices, or risk to the stability of the United States banking or financial system.

On the basis of the entire record, including commitments made in this case and conditions noted in this order, and for the reasons discussed above, the Board believes that the balance of benefits and potential adverse effects related to competition,

⁴¹ 12 U.S.C. § 1843(j)(2).

financial and managerial resources, convenience and needs, financial stability, and other factors weigh in favor of approval of these proposals. Accordingly, the Board has determined that the balance of the public benefits under the standard of section 4(j)(2) of the BHC Act is consistent with approval.

Establishment of Branches

As noted, Midland Bank has applied under section 9 of the FRA to establish branches at the current locations of Heartland Bank, and the Board has considered the factors it is required to consider when reviewing an application under that section.⁴² Specifically, the Board has considered Midland Bank'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.⁴³

Conclusion

Based on the foregoing and all the facts of record, the Board has determined that the proposals should be, and hereby are, approved.⁴⁴ In reaching its

⁴² 12 U.S.C. § 322; 12 CFR 208.6.

⁴³ Under section 9 of the Federal Reserve Act, state member banks are subject to the branching restrictions that apply to national banks. Thus, state member banks are permitted to establish branches at locations acquired through acquisition if the branches are located in states where the state member bank had a presence prior to the acquisition. 12 U.S.C. § 36(e). In addition, Dodd-Frank Act section 341 provides authority for savings associations that become banks to continue to operate branches that they operated immediately before becoming banks. Dodd-Frank Act § 341, codified at 12 U.S.C. § 5451.

⁴⁴ Several commenters requested that the Board hold a public hearing on the proposed transactions. The Board's regulations provide for a hearing on a notice filed under section 4 of the BHC Act if there are disputed issues of material fact that cannot be resolved in some other manner. 12 CFR 225.25(a)(2). Under its rules, the Board also may, in its discretion, hold a public hearing if appropriate to allow interested persons an opportunity to provide relevant testimony when written comments would not adequately present their views. The Board has considered the commenters' requests in light of all the facts of record. In the Board's view, the commenters have had ample opportunity to submit comments on the proposals and, in fact, submitted written comments that the

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, the Bank Merger Act, the FRA, and other applicable statutes. Approval of the proposals is specifically conditioned on compliance by Midland with all commitments made in connection with these proposals 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.

The proposed transactions may not be consummated before the fifteenth calendar day after the effective date of this order or later than three months after the date of this order unless such period is extended for good cause by the Board or by the Reserve Bank, acting pursuant to delegated authority.

By order of the Board of Governors,⁴⁵ effective December 11, 2014.

Margaret McCloskey Shanks (signed)

Margaret McCloskey Shanks
Deputy Secretary of the Board

Board has considered in acting on the proposals. The commenters' requests fail to identify disputed issues of fact that are material to the Board's decision and would be clarified by a public hearing. In addition, the requests fail to demonstrate why the written comments do not present the commenters' views adequately or why a hearing otherwise would be necessary or appropriate. For these reasons, and based on all the facts of record, the Board has determined that a public hearing is not required or warranted in this case. Accordingly, the requests for a public hearing on the proposals are denied.

⁴⁵ Voting for this action: Chair Yellen and Vice Chairman Fischer, Governors Tarullo, Powell, and Brainard.

Appendix

Branches in Missouri to be Established by Midland Bank

St. Louis

7818 Bonhomme Avenue

1 McKnight Place

9925 Clayton Road

9877 Manchester and Berry Roads

11670 Gravois Road

13402 Clayton Road

212 South Central Avenue

Arnold

1920 Richardson Road

Chesterfield

14125 Clayton Road

O'Fallon

2341 Highway K

St. Charles

5991 South Highway 94

St. Clair

815 North Commercial Avenue

Branch in Colorado to be Established by Midland Bank

Denver

100 Garfield Street, Suite 100