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Preface

The *Federal Reserve Bulletin* was introduced in 1914 as a vehicle to present policy issues developed by the Federal Reserve Board. Throughout the years, the *Bulletin* has been viewed as a journal of record, serving to provide the public with data and research results generated by the Board.

Authors from the Board's Research and Statistics, Monetary Affairs, International Finance, Banking Supervision and Regulation, Consumer and Community Affairs, Reserve Bank Operations, and Legal divisions contribute to the content published in the *Bulletin,* which includes topical research and analysis and quarterly "Legal Developments."

Starting in 2004, the *Bulletin* was published quarterly rather than monthly. In 2006, in response to the increased use of the Internet—and in order to release articles and reports in a more timely fashion—the Board discontinued the quarterly print version of the *Bulletin* and began to publish the contents of the *Bulletin* on its public website as the information became available. All articles, orders on banking applications, and enforcement actions that were published in the online *Bulletin* in 2010 are included in this print compilation.

The tables that appeared in the Financial and Business Statistics section of the *Bulletin* from 1914 through 2003 were removed and published monthly as a separate print and online publication, the *Statistical Supplement to the Federal Reserve Bulletin,* from 2004 to 2008. Effective with the publication of the December 2008 issue, the Federal Reserve Board discontinued both the print and online versions.

The majority of data published in the *Statistical Supplement* are available elsewhere on the Federal Reserve Board's website at www.federalreserve.gov/econresdata/statisticsdata.htm. The Board has created a webpage that provides a detailed list of links to the most recent data on its site and links to other data provided by the Federal Reserve Bank of New York, the U.S. Treasury, and the Federal Financial Institutions Examination Council.

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Improving the Measurement of Cross-Border Securities Holdings: The Treasury International Capital SLT

Erika Brandner, Fang Cai, and Ruth Judson, of the Board's Division of International Finance, prepared this article. Hugh Montag provided research assistance.

Understanding and accurately measuring cross-border financial flows and positions has long been important for analysis of portfolio exposures, but the significance of these measures has intensified since the onset of the financial crisis in late 2007, when patterns of cross-border flows changed dramatically.[1] In the United States, the system for measuring cross-border security investment has to this point consisted of annual surveys that measure securities *positions* and monthly reports that measure *transactions* in securities collected through the Treasury International Capital (TIC) reporting system.[2] During the crisis, estimated cross-border positions based on the more timely transactions data collected on the TIC S form were imperfect and in some cases misleading; in these cases, the more comprehensive survey data later revealed different patterns that would have improved understanding of vulnerabilities had they been known sooner. In the wake of the crisis, interest in improving the measurement of cross-border securities positions and flows was a chief motivation for the introduction of a new TIC reporting form for collecting monthly aggregate cross-border securities position data, the TIC SLT, for which the first wave of data was released on May 15, 2012.[3] This article reviews the general structure of cross-border position and flow data, the benefits that the new SLT can provide, and the incoming information from the first two reporting months of SLT data, September and December 2011. While some patterns and characteristics of the SLT data will only become clear over time, the SLT data have already begun to provide insights on U.S. and foreign cross-border investment flows that are different from the monthly estimates based on existing flow data.

Cross-border financial flows are the other side of current account transactions, or trade in goods and services: When goods or services are bought by one country, the cost of the items acquired must, on net, be covered either by a corresponding sale of goods or services or by financial inflows, or sales of financial assets. For the United States, which has run a current account deficit for about two decades, measurements and analysis of cross-border financial flows and positions is vital for understanding the sustainability of the U.S. current account deficit.

Cross-border financial flows occur mainly in the form of purchases and sales of securities, lending to banks and firms, and direct investment. The first two types of activity are monitored through the TIC reporting system; the third, direct investment, which we will not

1 See Bertaut and Pounder (2009).

2 TIC data, documentation, and forms are available at www.treas.gov/tic.

3 SLT is an abbreviation for "Securities Long Term." The form's title is "Aggregate Holdings of Long-Term Securities by U.S. and Foreign Residents."

review here, is collected and administered by the Bureau of Economic Analysis (BEA).[4] The TIC reporting system comprises several monthly forms as well as annual surveys and more-extensive periodic benchmark surveys of securities holdings; Appendix A: The TIC Reporting System provides an overview. Monthly TIC estimates of cross-border securities positions between surveys suffer from several shortcomings; because of these shortcomings, as well as interest in more-comprehensive, timely, and internationally comparable data, the SLT was developed and was first used in September 2011. The TIC SLT brings U.S. data collection into better alignment with updated international reporting standards, allows for quarterly publication of the U.S. International Investment Position, provides significantly timelier measurements of cross-border securities positions, and should ameliorate some, though not all, of the shortcomings of the current estimates based on the monthly transactions data.

This article reviews four topics. First, we review the data collection and compilation methodology in place prior to the debut of the SLT, including a review of the shortcomings and pitfalls of those reports and methods. Second, we review the SLT methodology and its ability to improve upon the existing system. We also discuss ongoing challenges to reporting and corresponding cautions that apply to interpretation of the data. We then review, based on the initial data received, the additional coverage provided by the SLT and the differences between the SLT data and the previous estimates based on cross-border flows. Finally, we compare the changes in cross-border holdings reported on the TIC SLT for the fourth quarter of 2011 with the estimates of the same changes based on the previous methodology. In general, the SLT data confirm trends indicated by the existing transactions-based position estimates: Cross-border positions in both claims and liabilities have largely recovered from the pullbacks that occurred during the financial crisis.

Although the initial SLT data for September and December should still be regarded as somewhat preliminary, the SLT readings nonetheless indicate changes in patterns of securities holdings that are in some ways quite different from the movements estimated using other available data. First, the new data indicate that U.S. investors shed rather than augmented their holdings of European long-term bonds late last year, a time that saw unusual strains in European financial markets. Second, these data indicate two trends in foreign holdings of U.S. Treasury securities in late 2011: a stronger overall foreign appetite for U.S. Treasury securities but a considerably larger decline in Chinese holdings of U.S. Treasury securities during late 2011 than had been estimated earlier. This data revision for China was not surprising: Data for China are typically revised when the annual TIC survey data become available. However, the magnitude and direction of the revision were surprising relative to earlier years, and with the SLT, we are able to see that change much sooner than we have in the past.[5]

Measuring Securities Positions and Flows Prior to the SLT: The Annual Surveys and the TIC S

The TIC SLT will be a complement to the two older TIC system elements that focus on collecting securities data: the annual surveys, which collect detailed data on cross-border secu-

[4] The BEA compiles the most comprehensive measures of cross-border financial flows and positions in the quarterly balance of payments accounts and in the annual net international investment position. The BEA's data on international accounts, including the balance of payments accounts and the international investment position, are published in both the BEA's Survey of Current Business (www.bea.gov/scb/index.htm) and on its International Economic Accounts webpage (www.bea.gov/bea/di1.htm).

[5] These data were reported in late February as part of the Major Foreign Holders of U.S. Treasury Securities table at www.treasury.gov/resource-center/data-chart-center/tic/Documents/mfh.txt.

rities positions; and the TIC S, which collects cross-border securities transactions data. (See appendix A for a review of all of the TIC forms.) Prior to the introduction of the TIC SLT, accurate estimates of cross-border securities positions were available from the surveys only with a substantial lag. In the months after the release of TIC S transactions data and prior to the release of the next survey, cross-border positions could be estimated using TIC S transactions and valuation adjustments. These position estimates, which we call Survey-S estimates, are useful but have significant limitations. The methodology for calculating these Survey-S estimates and its limitations are described more fully in the section Estimating Monthly Positions from Survey and TIC S Data, following a review of the features of the survey data and of the TIC S data.

Measuring Cross-Border Securities Positions: The Annual TIC Surveys

Annual surveys of cross-border security holdings provide the most accurate and detailed information on cross-border securities holdings by the United States and the rest of the world.[6] The TIC system currently conducts two sets of comprehensive position surveys annually for both long- and short-term securities.[7] First, the liabilities survey measures foreign holdings of U.S. securities at the end of June each year. Data are collected at the individual security level by country of holder, and by type of holder (official or private). Second, the claims survey measures U.S. holdings of foreign securities at the end of December each year. Data are collected at the individual security level and by broad type of holder. For both surveys, data are collected at the market value. Staff members at the Federal Reserve Bank of New York and at the Federal Reserve Board conduct extensive reviews of the data, including reporters' valuations of each security and reporters' designation of each security's characteristics, most importantly the security issuer's country of incorporation. In addition to any corrections, the raw aggregated data are also adjusted for securities that are reported by both issuers and custodians, and to make reporting samples comparable across annual and benchmark years.[8]

The Annual Liabilities Survey

Figure 1, panel A, shows foreign holdings of U.S. securities by asset type for the years 2003 to 2011. Most foreign holdings of U.S. securities are in debt (almost 70 percent as of June 2011), especially in long-term debt. Treasury securities and corporate bonds are the two largest categories of debt that foreigners hold. The share of long-term Treasury securities in total foreign holdings of U.S. securities has increased from about 20 percent in 2007 to more than 30 percent in 2011, mainly due to investment of substantial foreign exchange accumulations by foreign official investors. Foreign official investors are the largest foreign investors in U.S. Treasury securities; their share in total foreign holdings of U.S. long-term Treasury securities has grown from 62 percent in June 2002 to 77 percent in June 2011. Short-term debt holdings (not shown) have been small, generally less than 10 percent of total foreign holdings since 2002.

Figure 1, panel B, reports the geographic distribution of foreign holdings of U.S. securities. China and Japan are currently the two largest foreign holders of U.S. securities, but hold-

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[6] For additional background information on the surveys, see Griever, Lee, and Warnock (2001); Bertaut, Griever, and Tryon (2006); and the annual survey reports released by the Treasury Department available at www.treasury.gov/resource-center/data-chart-center/tic/Pages/fpis.aspx.

[7] In addition, benchmark surveys from a more comprehensive panel of reporters have been conducted periodically; currently, they are conducted every five years. The most recent benchmark claims survey was conducted in December 2011 and the most recent benchmark liabilities survey was conducted in June 2009.

[8] See chapter 2 of the annual survey reports for more details on the survey methodology. Annual survey reports are available at www.treasury.gov/resource-center/data-chart-center/tic/Pages/fpis.aspx.

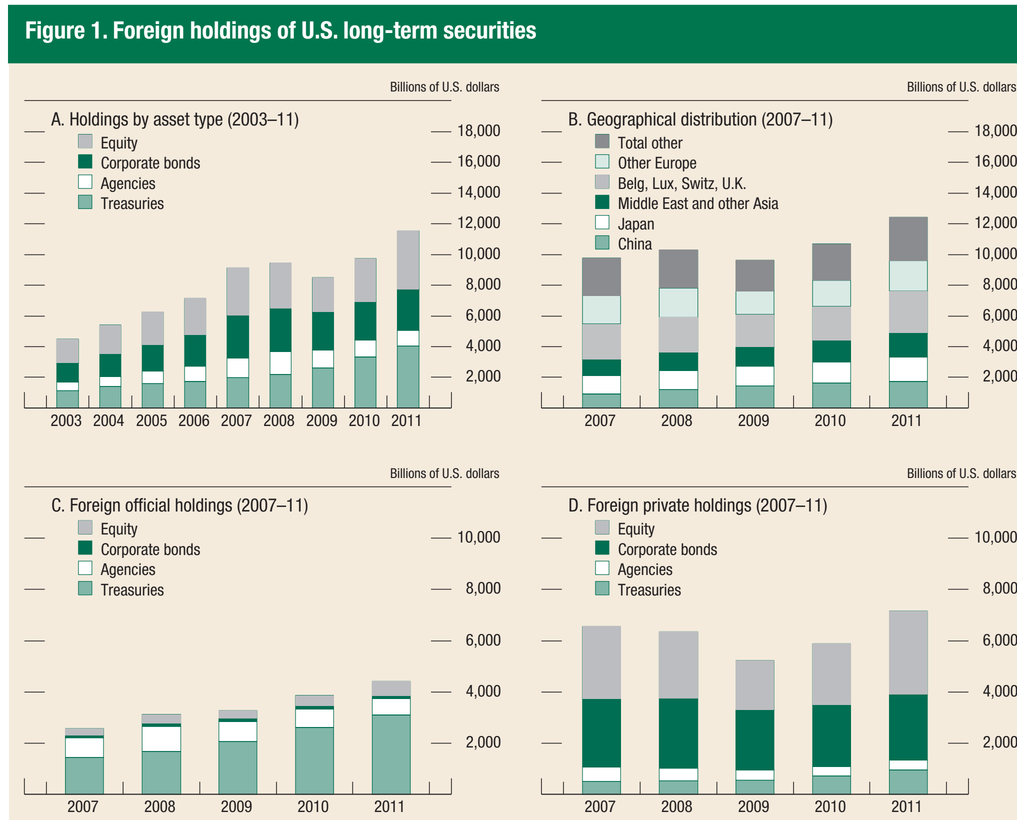


Figure 1. Foreign holdings of U.S. long-term securities

ings by other Asian countries and Mideast countries have also grown rapidly in the past few years. Belgium, Luxembourg, Switzerland, and the United Kingdom collectively have large foreign holdings of U.S. securities; of this group, the United Kingdom is the largest holder, and the third-largest holder of U.S. long-term securities overall. The large volume of holdings in this group of countries highlights the main pitfall in the liabilities survey—"custodial bias." The country attribution of foreign holdings of U.S. securities as reported in the liabilities surveys is imperfect because many foreign owners entrust the safekeeping of their securities to institutions that are neither in the United States nor in the owner's country of residence. For example, a German investor may buy a U.S. security and place it in the custody of a Swiss bank. In the surveys of foreign holdings of U.S. securities, such a holding typically is recorded against Switzerland rather than Germany. This custodial bias contributes to the large recorded foreign holdings of U.S. securities in major financial centers, such as Belgium, Luxembourg, Switzerland, the United Kingdom, and the Caribbean banking centers.[9]

The large holdings of U.S. securities by entities in offshore financial centers—especially those in the Caribbean—pose additional obstacles to interpreting foreign investors' cross-border financial activity because these holdings largely reflect the securities portfolios of the numerous investment funds that have been established in such offshore locations rather than the portfolio preferences of residents of those countries. Moreover, because many

[9] In addition, the country attribution in the liabilities survey is complicated by bearer, or unregistered, securities. Bearer securities generally cannot be issued in the United States, but U.S. firms can and do issue such securities abroad, and typically little or no information is available about the owners of these securities because they need not make themselves known. The vast majority of the debt securities attributed to owners whose country of residence is unknown in the liabilities surveys are bearer securities.

Caribbean banking centers include the Bahamas, Bermuda, the Cayman Islands, the Netherlands Antilles, Panama, and the British Virgin Islands.

financial institutions have affiliated banking and nonbanking offices in these offshore locations, analyzing securities transactions through these centers can be difficult without knowing whether offsetting transactions are occurring through other parts of the financial accounts. For example, when entities located in financial centers buy U.S. securities from U.S. broker–dealers, those transactions are recorded as financial inflows to the United States. However, such transactions could well be offset by equally sizable net outflows to the same financial centers but reported in other parts of the financial accounts, such as the TIC banking data.

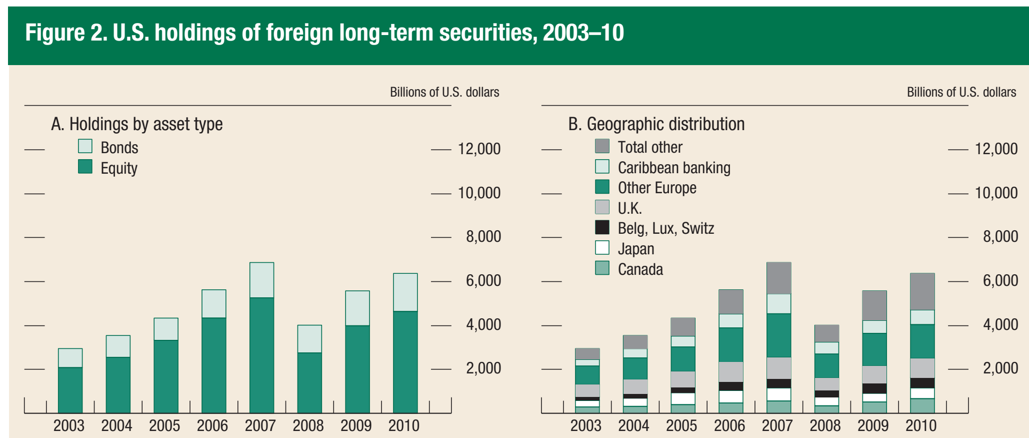
Foreign official and private investors have very different portfolios of U.S. long-term securities, as seen in panels C and D of figure 1. Foreign official holdings of U.S. securities are dominated by Treasury securities and U.S. agency securities, which together account for about 85 percent of such holdings. In contrast, foreign private investors' holdings of U.S. long-term securities are dominated by equity and corporate bonds, each of which account for about 40 percent of such holdings.

The Annual Claims Survey

The claims survey measures U.S. holdings of foreign securities at the end of December each year. These data are collected at the individual security level by country of issuer for U.S. holdings of foreign bonds, equities, and short-term debt. Figure 2, panel A, shows U.S. holdings of foreign securities by asset type from 2003 to 2010. Most U.S. holdings of foreign securities are in foreign equities (about two-thirds as of December 2010), followed by long-term debt. As with foreign holdings of U.S. securities, U.S. investment in short-term foreign debt (not shown) is small, generally less than 10 percent of total U.S. cross-border portfolio holdings.

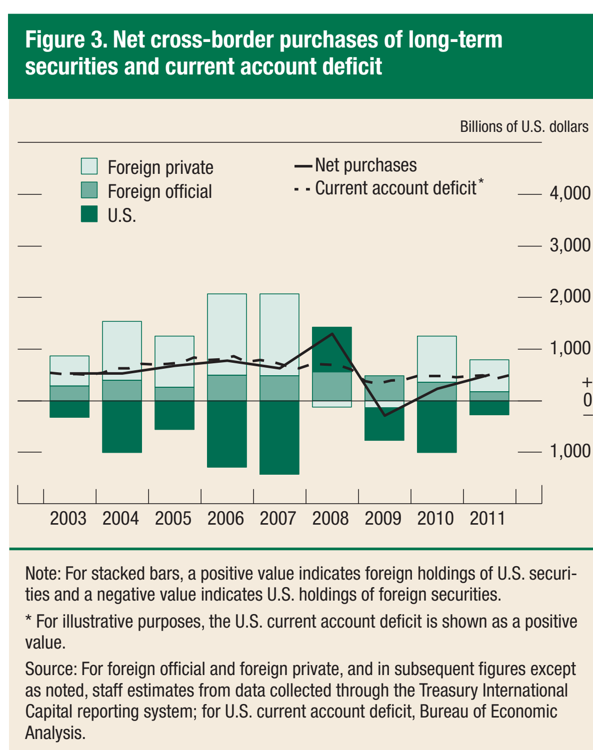
Panel B of figure 2 shows the United Kingdom, Canada, and Japan as some of the countries with the largest U.S. securities investments. Besides Europe, Caribbean banking centers are also a significant destination of U.S. investment overseas, which reflects the main shortcoming in the claims survey—that is, the claims survey identifies the country of issue of securities based on their country of legal incorporation, which may not be the center of the security issuer's activity. For example, equity of a U.S. multinational firm reincorporated in Bermuda or the Cayman Islands is officially identified with Bermuda or the Cayman Islands even though its center of activity is still in the United States and its equity trades on U.S. exchanges. Thus, TIC survey data based on where the issuer is incorporated can cause odd patterns of U.S. holdings that can be hard to reconcile with measures of foreign country market capitalization. For example, U.S. holdings of equities registered in Bermuda and Ireland in 2010 exceeded 100 percent of those countries' domestic market capi-

Figure 2. U.S. holdings of foreign long-term securities, 2003–10



talization.[10] Likewise, growth in special purpose vehicles (SPVs) in offshore financial centers can pose a challenge to measuring and interpreting U.S. investors' portfolios.[11] Although securities issued by multinational corporations reincorporated in the Caribbean or through offshore SPVs fit the definition of foreign securities, U.S. investors may not regard them as such because they trade in U.S. dollars on U.S. exchanges and are often issued by firms that conduct their market activity largely in the United States and otherwise behave like U.S. firms. In addition, since most Caribbean banking center debt is dollar denominated, growth in dollar-denominated debt securities issued in Caribbean banking centers obscures other important developments in the currency composition of U.S. holdings of foreign bonds.

Figure 3. Net cross-border purchases of long-term securities and current account deficit



Note: For stacked bars, a positive value indicates foreign holdings of U.S. securities and a negative value indicates U.S. holdings of foreign securities.

* For illustrative purposes, the U.S. current account deficit is shown as a positive value.

Source: For foreign official and foreign private, and in subsequent figures except as noted, staff estimates from data collected through the Treasury International Capital reporting system; for U.S. current account deficit, Bureau of Economic Analysis.

Overall, both U.S. cross-border liabilities and claims are substantial. However, as shown in figure 3, net purchases of U.S. long-term securities by foreigners have exceeded flows in the opposite direction, net purchases of foreign long-term securities by U.S. residents. This difference generally coincides with net foreign official purchases of U.S. long-term securities. Overall net cross-border purchases of long-term securities—foreign purchases of U.S. securities less U.S. purchases of foreign securities—the solid line, roughly balance the current account deficit, shown with a positive value as the dashed line in figure 3.

Shortcomings of the Survey Data

Both liabilities and claims survey data are collected primarily from large U.S. custodian banks and U.S. broker–dealers, but also from issuers of U.S. securities directly issued in the foreign markets and from large U.S.-resident end investors who do not use U.S. custodians for holdings of foreign securities (for example some pension funds, foundations, and endowments).[12]

Despite the richness of the TIC survey data at the security level, major shortcomings of the survey data are that these data are only available annually, are collected at different times for liabilities and claims, and are only usable with a substantial lag: Preliminary data from each survey are typically released eight months after the survey date. For example, the preliminary data from the June 2011 liabilities survey were released at the end of Febru-

[10] See table A14 in U.S. Department of the Treasury, Federal Reserve Bank of New York, and Board of Governors of the Federal Reserve System (2010).

[11] See Bertaut, Griever, and Tryon (2006).

[12] All U.S.-resident entities that have been contacted by the Federal Reserve Bank of New York must report, regardless of the size of their consolidated holdings.

ary 2012, and the preliminary data from the December 2011 claims survey are due to be released at the end of August 2012.

Measuring Cross-Border Transactions: The TIC S Data

In addition to the survey data, which measure positions in securities at a certain point in time in a year, the TIC system also collects financial flow data on the S form. The TIC S form collects monthly transactions data on cross-border purchases and sales of U.S. Treasury and agency securities, U.S. corporate bonds and other bonds, U.S. equities, and foreign stocks and bonds. These data are collected primarily from U.S.-resident broker–dealers responsible for securities transactions with nonresidents, but are also collected from some issuers, end investors, and money managers.[13] Unlike the survey data, TIC S data are collected only in aggregate by security type but become available with a much shorter lag—about 45 days. Thus, TIC S data provide us with a timely and useful tool to gauge cross-border investment at a monthly frequency. For example, are U.S. investors investing abroad, in equities or debt? Are foreign investors buying U.S. securities? Are they mainly official or private investors? The TIC S data can help to answer these questions between surveys, but it is important to note three pitfalls of the TIC S data that can cause misleading interpretations of cross-border flows.

First, by design, the TIC S data are recorded according to country of the first cross-border counterparty, not the country of the ultimate buyer or actual seller or issuer of the security. By recording direct transactions with foreign residents, who are often broker–dealer counterparties, the TIC S data record financial transactions between the two countries, information that is important for the U.S. balance of payments statistics. As a result, the geographical distribution of transactions is distorted by activity through financial centers, or suffers from a "transactions bias."[14] For example, when a German resident buys a U.S. Treasury bond through a London broker, the TIC S will record a sale to the United Kingdom rather than Germany. As a result, the reported monthly transactions data are concentrated in major international financial centers. In contrast, position data collected by the surveys and the SLT record the holder and so do not suffer from this transactions bias.

Second, measured transactions do not fully account for transactions made on behalf of official foreign investors. For example, if the Chinese government buys U.S. agency bonds through an intermediary in Hong Kong, the TIC S (correctly) will report a purchase of U.S. agency bonds by a private Hong Kong counterparty. The TIC S does not capture the foreign-to-foreign transaction showing the final owner to be an official mainland China counterparty; these distinctions can be important when trying to assess, for example, official and private demand for U.S. assets.

Third, the TIC S data do not record important cross-border flows in securities that do not pass through standard broker–dealer channels. In particular, the TIC S cannot account for principal repayment flows of asset-backed securities (ABS). Thus, the large holdings of U.S. asset-backed agency and corporate bonds result in overestimates of foreign net acquisitions of these securities. Similarly, the TIC S does not collect data on cross-border acquisitions of stocks through merger-related stock swaps or re-incorporations because these transactions are considered direct investment transactions, for which data are collected by the BEA. For example, when a U.S. firm buys a foreign firm and the transaction is financed through a stock swap, or when a foreign firm relocates to the United States,

[13] Reporting is legally required for these entities if their monthly cross-border transactions are above the $50 million threshold during the reporting month.

[14] See Griever, Lee, and Warnock (2001) and Warnock and Cleaver (2002).

U.S. residents' holdings of the foreign firm's stock are no longer considered foreign securities, but the change in ownership is not reported on the TIC S.[15] To assist users in obtaining more-comprehensive net transactions data, Federal Reserve Bank of New York and Federal Reserve Board staff construct estimates of ABS repayment flows and stock swaps, and these estimates are published on the TIC website.[16]

A final complication that can affect both the TIC S data and the annual survey data, and that also affects the SLT data, arises from the activities of U.S. investors who entrust their securities holdings to foreign investment managers or foreign custodians. Typically, a U.S. investor who keeps foreign securities abroad will use a domestic investment manager who will report the investor's holdings on the annual claims survey on behalf of the U.S. investor. However, if the U.S. investor uses a foreign investment manager, these holdings and associated securities transactions may be missed because the TIC reporting system can collect data only from U.S.-resident entities and cannot collect information from individual U.S. persons. As a result, U.S. holdings of foreign securities may be somewhat underreported in the TIC system. On the other hand, if a U.S. resident holds U.S. securities with a custodian abroad, it is possible that these holdings will be counted as foreign holdings of U.S. securities because the U.S. custodian who has subcustodian responsibilities may not know that they are held on behalf of a U.S. investor. This particular form of custodial bias can lead to overreporting of foreign holdings of U.S. securities.

Estimating Monthly Positions from Survey and TIC S Data: The Survey-S Estimates

In order to obtain timelier information on cross-border securities positions between surveys, we can estimate monthly time series of positions to date by combining the annual survey data with the TIC S data.[17] The monthly estimated positions between surveys are constructed in three steps for each asset type in the liabilities and claims surveys, as indicated in the following equation:

$$x_t = x_{t-1}(1+V_t) + S_t + A_t$$

First, beginning with data from the survey month, x_{t-1}, the next month's position, x_t is adjusted for valuation changes, V_t, using a combination of standard price indexes of U.S. or foreign securities. The combination of price indexes is chosen to approximate the portfolios held by foreign and U.S. investors as indicated by earlier surveys. Next, the current month's net transactions, S_t, are added. Finally, adjustments, A_t, are included to account for repayment flows of principal on asset-backed agency securities, acquisitions of equity through stock swaps, and transactions in nonmarketable Treasury bonds. We refer to these monthly position estimates as the Survey-S estimates.

As noted in Bertaut and Tryon (2007), however, there are often considerable discrepancies between the reported survey positions and position estimates derived from the monthly transactions data as published by the Treasury. At the individual country level, such discrepancies are largely due to the transactions bias in TIC S reporting. Constructing estimated positions based on the country-level monthly transactions data tends to generate estimates of holdings by residents of such financial center locations that considerably over-

[15] For more details, see Bertaut and Tryon (2007).

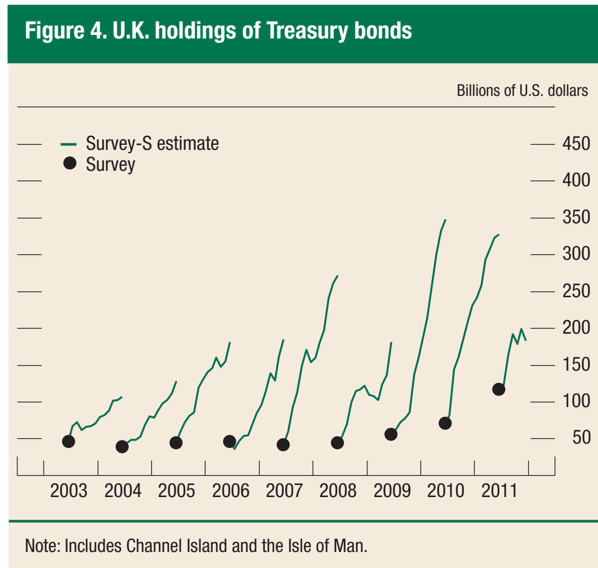
[16] See www.treasury.gov/resource-center/data-chart-center/tic/Pages/ticsec2.aspx, sections 4a and 4b.

[17] Monthly transaction data and annual survey data are integral to the BEA's estimate of holdings in the annual International Investment Positions (IIP) publication. The BEA also uses the information obtained from TIC S and survey data in calculating investment income and financial flows in the U.S. Balance of Payments statement.

state actual holdings as reported in the next survey, and will tend to underestimate holdings by residents of other countries.

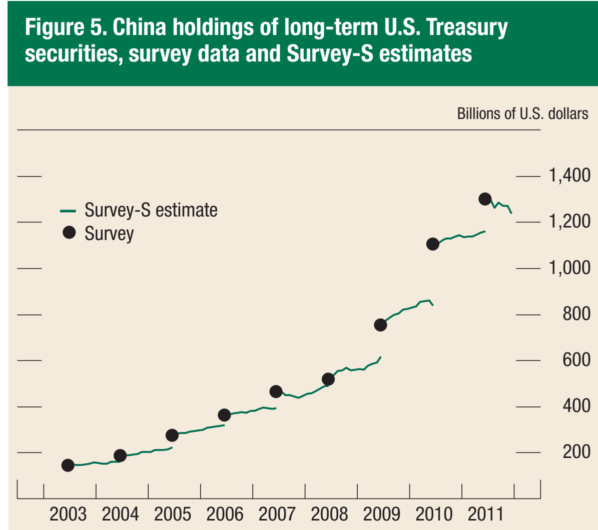
Figure 4 and figure 5 illustrate both sides of this problem for holdings of U.S. Treasury bonds by the United Kingdom, a transactions center, and holdings of U.S. Treasury securities by China, whose transactions are apparently often executed offshore. The solid lines indicate estimated positions based on the previous year's survey, cumulated transactions from the TIC S, and adjustments for valuation changes. The dots indicate reported survey positions. For the United Kingdom, estimated positions, even after adjusting for valuation changes, are consistently much higher than the survey results, presumably representing transactions in U.S. securities made in the United Kingdom on behalf of third parties. Conversely, estimated positions for China are much lower than reported positions, which reflect transactions conducted via overseas accounts. More generally, because of the transactions bias, our position estimates could give a misleading impression about which country is buying U.S. securities, and how U.S. and foreign investors are adjusting their portfolios.

Figure 4. U.K. holdings of Treasury bonds



Note: Includes Channel Island and the Isle of Man.

Figure 5. China holdings of long-term U.S. Treasury securities, survey data and Survey-S estimates

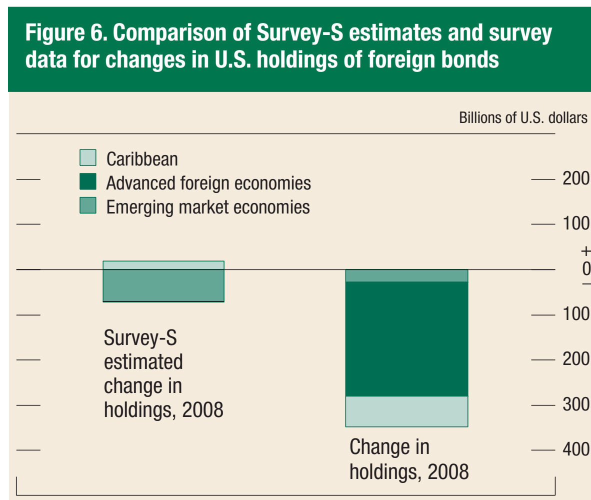


Conflicting Signals: Readings from the TIC S and Survey during and after the Crisis

Under the existing system, although the TIC S reporting provides us with a way to estimate positions data between surveys, misleading interpretations caused by the transactions bias are not revealed until the next annual survey. Given such limitations, there has been a growing demand for more-accurate and timely positions data by market participants and policymakers, especially in light of the recent financial crisis.

Figure 6 provides an example of what the existing system indicated about U.S. investment in foreign bonds in 2008, and what we could have learned earlier had a more-accurate and timely data source been available. As the crisis was unfolding, the TIC S indicated that, on net, U.S. investors were sharply reducing their holdings of foreign government and corporate bonds, especially those issued from emerging market economies (EMEs). These movements suggested that the EMEs might face difficulty obtaining funding in interna-

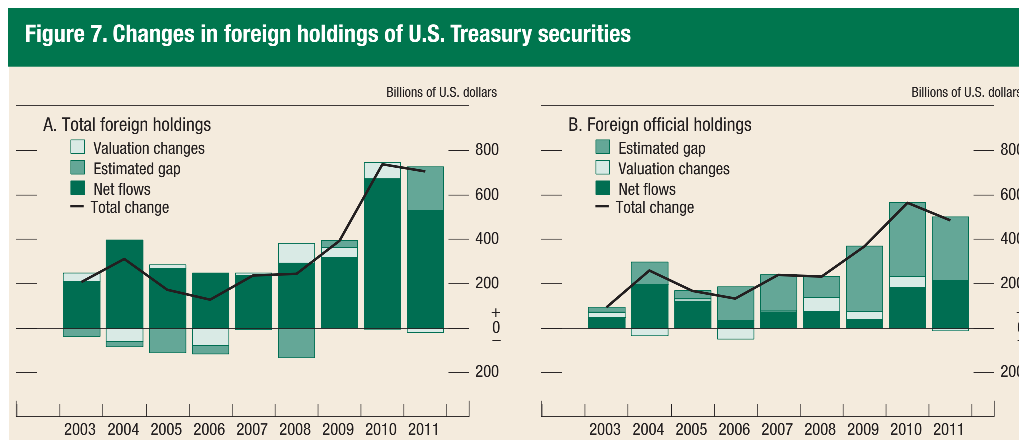
Figure 6. Comparison of Survey-S estimates and survey data for changes in U.S. holdings of foreign bonds



tional markets. In fact, these data were somewhat misleading: Survey data received much later, in the summer of 2009, indicated that the situation for EMEs was less severe than had been indicated by the TIC S but that the situation for other countries was more severe. The value of foreign bonds held by U.S. investors fell by considerably more than the TIC S had indicated, and the reductions had been concentrated not in the EMEs but rather in advanced economies. The difference between the country attribution of the Survey-S estimates and that of the survey data is likely due to the transactions bias in this instance. Purchases of EME securities, especially those issued in international markets, could have been recorded as purchases of securities issued by the country in which the sale occurred while redemptions of the same bonds would have been correctly attributed to the issuing country. In addition, the survey data revealed that actual U.S. sales of foreign bonds were apparently larger than were reported on the TIC S.

A more recent example is movements in foreign holdings of U.S. Treasury securities, a topic of interest given the large issuance of debt by the Treasury, large purchases of Treasury securities by the Federal Reserve, and the announcements by some large holders of U.S. Treasury securities, most notably China, of intentions to diversify their reserve asset holdings, presumably away from Treasury securities. The Survey-S estimates, shown in panel A of figure 7 by the sum of the pale green and dark green bars, indicate that total foreign holdings of U.S. Treasury securities rose about $500 billion in 2011—substantially less than the $750 billion increase over the previous 12-month period. However, the survey data from June 2011, released in late April 2012 and shown by the black line, indicate that foreign holdings of U.S. Treasury securities from mid-2010 to mid-2011 increased nearly as much as they had in the previous year—about $700 billion. The discrepancy between the actual change in holdings and the Survey-S estimates is shown by the positive medium green bar. Because valuation changes for Treasury securities are typically fairly small relative to the total change in holdings, this positive "gap" indicates the extent to which reported net purchases of Treasury securities likely understated actual foreign acquisitions. There are several possible explanations for this gap and investigation is ongoing. First, it is possible that

Figure 7. Changes in foreign holdings of U.S. Treasury securities



some cross-border transactions in the huge Treasury securities market are missed in the TIC S reporting: In 2011, average *daily* trading volume in Treasury bonds was on the order of $500 billion or more than twice the amount of the gap for the *year* of 2011.[18] Alternatively, custodial bias could be a complicating factor: If U.S. residents purchase Treasury securities in the U.S. market but then entrust them to foreign custodians, the TIC S would (correctly) not record the purchases but the survey could count the securities as held by foreigners.

Foreign official purchases of Treasury securities were subject to a larger but more typical revision: As shown in panel B of figure 7, the Survey-S estimate for mid-2010 to mid-2011 indicated an increase in foreign official holdings of about $200 billion, but the survey revealed a change of about $500 billion. Foreign official purchases are typically subject to such revisions, as shown by the positive medium green bars, because foreign official entities often execute their transactions through foreign private intermediaries. In this case, the gap between the Survey-S estimates and the survey data suggest that foreign official acquisitions of Treasury securities over this period were likely quite a bit larger than reported on the TIC S, which by design attributes such transactions to the foreign private parties that conduct the transactions. Thus, it is important to note that gaps may arise from reporting errors but can also result from the reporting structure.

The TIC SLT: Building on the TIC S and the Survey

Background

Analysis of the financial crisis that began in late 2007 highlighted the importance of collecting timely information on cross-border securities positions: As noted above, as the crisis unfolded, accurate and timely position information was not available, and the survey data released in 2009 indicated some different trends than the earlier TIC S had provided. The differences between the TIC S estimates and the survey data received later were due to the measurement and estimation problems mentioned above: Transactions bias likely resulted in underreporting of purchases of EME securities, especially those issued in international markets, while redemptions of the same bonds would have been correctly attributed to the issuing country. In addition, transactions that resulted in changes in U.S. residents' holdings of foreign securities appear to have been conducted by financial intermediaries that were not part of the reporting panel of the TIC S.

Additional securities reporting to address the shortcomings of the TIC survey and TIC S had been under consideration prior to the crisis, but the crisis accelerated the development and introduction of the TIC SLT "Aggregate Holdings of Long-Term Securities by U.S. and Foreign Residents," which addresses many, though by no means all, of these shortcomings. Relative to the survey, the SLT will provide much more timely and frequent reporting; relative to the TIC S, the TIC SLT will provide market-value reports of actual holdings rather than flows. During the process of developing and introducing the SLT, considerable efforts were made to ensure that all reporters meeting the reporting threshold, especially hedge funds, private equity firms, and other types of managed funds, understand how to report correctly.

Despite these improvements, the SLT will still not be perfect, and custodial bias in particular will remain a challenge. In addition, the older elements of the TIC reporting system—the TIC S and the annual surveys—will remain important as complements to the TIC SLT. The TICS will remain the timeliest indicator available of cross-border securities flows—

[18] See Securities Industry and Financial Markets Association, www.sifma.org/research/statistics.aspx.

actual cross-border securities acquisitions or sales—and will, along with the SLT, allow us to decompose position movements into recorded transactions, valuation changes, and "gaps" that reflect unrecorded transactions or errors in valuation estimates.[19] It also remains to be seen how closely the SLT data will anticipate the corresponding survey data. In principle, the SLT and survey data for the same dates should be nearly identical, but experience to date suggests that reporting differences can and do emerge. As a result, the detailed information provided by the survey will remain valuable as a complement to the SLT.

The recent financial crisis offers at least three examples of the added usefulness of survey data, even though it arrives with such a long lag. First, the survey provides the most detailed information available about the distribution of investment flows between valuation changes, or "passive" changes, and purchases or sales, or "active" changes. Over the course of 2008, the survey confirmed that U.S. investors' holdings of foreign equity declined $2.5 trillion, or nearly 50 percent. In isolation, this figure might indicate that U.S. investors were abandoning foreign equities. However, analysis of price changes and position changes at the security level revealed that the change was nearly all due to declines in valuation: After adjusting for price changes, U.S. net sales of foreign equity amounted to only about $10 billion, or less than 1 percent of the overall change. Second, the security-level reporting on the survey also can illuminate trends in cross-border portfolio composition that are difficult to identify otherwise. For example, the survey data allow analysis of exposures, by country and sector, to securities whose values are changing rapidly, such as ABS.[20] Finally, the survey will allow for confirmation that positions reported in aggregate on the SLT are calculated correctly. For example, it can sometimes be difficult for reporters to distinguish between securities issued in the U.S. market by foreign entities (considered to be foreign securities by the TIC system) and similar securities issued by the U.S. branches or subsidiaries of such foreign entities (considered to be U.S. securities by the TIC system). By examining the detailed security-level data reported in the annual surveys, proper guidance can be provided to reporters regarding classifications of such securities holdings.

Taken together, the combination of the more-frequent positions data from the SLT, the monthly transactions data, and the annual surveys should together result in a more complete and accurate system for recording cross-border flows and positions. Although the exercise of reconciling changes in cross-border holdings of securities between recorded transactions, valuation changes, and sources of "gaps" has long been conducted for the annual surveys, with resulting improvements in valuation estimates and clarification of reporting responsibilities to collect missed TIC S transactions, the more timely SLT holdings data will allow for this type of analysis to be conducted more frequently.

Data Collected on the SLT

The SLT requires monthly reporting on own and custodial cross-border positions in long-term securities at market value by country of holder for U.S. liabilities to foreigners and by country of issuer for U.S. claims on foreigners.[21] In addition, for liabilities, holdings must be divided into official and private holdings. Finally, for total positions across all countries, reporters must provide information on several memo items, including ABS positions, fund-

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[19] Beginning with the December 2011 report, the TIC SLT collects data monthly just as the TIC S does. However, the filing deadline for the TIC SLT is a bit later and, at least in the short run, the more intensive data review process required for a new form will result in later release of the TIC SLT data than the TIC S data.

[20] See Beltran, Pounder, and Thomas (2008).

[21] Position information for short-term securities is already collected on the TIC B forms. See appendix A and www.treasury.gov/resource-center/data-chart-center/tic/Pages/forms-b.aspx.

share positions, and the sector of the holder (for liabilities) or issuer (for claims).[22] The SLT form has two parts, A and B, for reporting of custodial and issuer or end-investor holdings, respectively. Although the structure of the SLT form parallels the TIC S in many respects, the differences reflect efforts to bring TIC reporting in line with recent initiatives to improve and harmonize data on this topic as described in box 1, "The TIC SLT and New Data Initiatives." In particular, the categories for the sectoral breakdowns were selected to meet the standards established in the sixth edition of the *Balance of Payments and International Investment Position Manual*, 6th edition (BPM6), and the separation of holdings into own and custodial holdings parallels reporting on the annual TIC surveys.

The SLT will provide considerably timelier position data, though initially not quite as timely as the estimates now available by cumulating adjusted TIC S data. The first two SLT report dates were September 30 and December 31, 2011; beginning with January 31, 2012, report dates will be monthly for the last business day of the month, with reports due to Federal Reserve Banks by the 23rd calendar day of the following month. As with any new report form, the lag for data releases will initially be somewhat longer as more extensive validation checks are conducted and reporting consistency is reviewed. Therefore, the current release includes full security type and country data from the two initial filings of the TIC SLT, for September and December 2011. As reporters become more accustomed to the form's requirements and procedures, we anticipate that the review and validation process will be quicker and data release will occur more promptly. In the longer run, publication is anticipated with an additional one-month to two-month lag, or a total of two to three months after the report date. We expect that SLT data will be available for use in quarterly international investment position calculations with a lag of less than one quarter, as specified in BPM6, by the end of 2012.

In addition to the new items collected on the TIC SLT, two factors have resulted in a significant expansion of the SLT reporting panel relative to the TIC annual survey panel. First, the reporting threshold is a bit different, and is generally lower. Second, significant outreach efforts were made in order to inform managers of hedge funds, private equity funds, and other types of managed funds of potential reporting responsibilities. As part of these efforts, instructions and other materials to clarify the reporting responsibilities of such entities were developed.[23] These factors resulted in an increase in the number of reporters from about 100 on each of the annual survey panels to over 300 on the SLT.

A First Look at the SLT Data

New Reporting

As noted above, substantial efforts were made to ensure that all eligible reporters were familiar with the TIC SLT form and its instructions, and the reporting panel expanded by over 200 reporters, or more than double the number of recent survey reporters. The first few reporting dates indicate that these efforts resulted in increased reporting on the order of 2½ percent—about $300 billion—for liabilities, and 6 percent—or about $400 billion—for claims. Table 1 presents SLT totals for two sets of reporters: all reporters, and only those who reported on the SLT but not on the annual surveys. As shown in the upper panel, these new reporters' positions were concentrated in equities and, to a lesser extent, in corporate

[22] Forms and instructions are available at www.treasury.gov/resource-center/data-chart-center/tic/Pages/forms-slt.aspx.

[23] These materials, which include FAQs and flowcharts, are available at www.treasury.gov/resource-center/data-chart-center/tic/Documents/slt_faqs.pdf and www.treasury.gov/resource-center/data-chart-center/tic/Documents/slt_flowcharts.pdf.

Box 1. The TIC SLT and New Data Initiatives

Although researchers have long been aware of the informational gaps in the monthly TIC S and the disparities between the TIC S estimates and annual survey data, concerns about reporting burden and costs to data compilers were sufficient to prevent the introduction of a new, improved TIC report. Instead, efforts were largely devoted to incremental enhancements to the existing data collection system. For example, reporters were required to identify transactions in asset-backed securities (ABS) on the TIC S, estimates of repayment flows on foreign holdings of ABS were made available to data users, and additional tabulations of the survey data were added to the annual survey reports.

However, the financial crisis of 2008 altered the balance of priorities between concerns over reporting burden and the need for more complete financial information, and highlighted the importance of moving the TIC forms into closer compliance with the Group of Twenty (G–20) data initiatives, especially those stressing the collection of more complete global financial data. In particular, the crisis revealed the value of a form such as the SLT. The crisis showed the importance of understanding, on a *timely* basis, how cross-border portfolio investors are responding to changes and how exposures are building in the global financial environment.

In November 2009, in the aftermath of the global financial crisis, the G–20 Data Gaps Initiatives were developed by the Financial Stability Board Secretariat and International Monetary Fund (IMF) staff.[1] These initiatives were endorsed by the G–20 Finance Ministers and Central Bank Governors and by the International Monetary and Financial Committee. The G–20 meetings that occurred as part of the Data Gaps Initiatives emphasized the importance of international collaboration and coordination to better assess current versus desired data collection, risks posed to institutions, especially global systemically important financial institutions, and how to optimally allocate resources to close existing data gaps. These key components are reflected in the 20 recommendations that were generated by the meetings. The recommendations balanced the desire to close gaps in financial data reporting against various constraints to data collection, including reporting burden, confidentiality concerns, and legal constraints.

In general, the recommendations focused on obtaining more-specific data in several dimensions. In particular, it was argued that data reported on a residence basis, disaggregated by country, sector, instrument, maturity, and currency denomination should facilitate the identification of interest rate and exchange rate risks, maturity mismatches or funding gaps, and the potential for spillovers.

In order to move the TIC reporting system into closer compliance with the G–20 data initiatives, the new form SLT was introduced in September 2011.

SLT's Link to Recommendations

The new SLT form addresses 3 of the 20 recommendations of the G–20 finance ministers and central bank governors in the May 2010 report *The Financial Crisis and Information Gaps* that pertain to cross-border securities positions.

First, central banks and statistical offices are to participate in the Bank for International Settlements (BIS) data collection on securities.[2] This recommendation is quite general. As noted elsewhere, the SLT will provide more timely, frequent, and reliable estimates of securities holdings, and thus will contribute to more-complete global cross-border data sets. Because the SLT collects holdings of securities at market value, the SLT in combination with the monthly transactions data will also provide a better approximation of valuation changes.

Second, countries are to work toward reporting their international investment positions (IIPs) quarterly and, to the extent possible, reporting their IIPs in accordance with the standards established in the *Balance of Payments and International Investment Position Manual,* 6th edition (BPM6).[3] The United States is already in partial compliance with the IIP "pipeline project," which aims to increase the number of countries reporting annual and

continued on next page

Box 1.—*continued*

quarterly IIP data to the IMF. The SLT will move the United States into full compliance with the BPM6 reporting timeline of quarterly reporting with a maximum lag of one quarter. BPM6 also emphasizes sector of issuer (for U.S. portfolio liabilities) and sector of holder (for U.S. portfolio assets). The "of which" memo lines on the SLT will move the United States into closer compliance with the BPM6 sector requirements.

Third, the report more generally recommended improved sectoral breakdowns in order to narrow financial data gaps.[4] The key recommendation from the early reports emphasizes the importance of improving data on international financial network connections and monitoring the vulnerability of domestic economies to shocks. In addition to satisfying BPM6 sector requirements, the "of which" items from the SLT allows for analysis of exposures to, for example, financial or nonfinancial or municipal issuers, and the more timely measures of cross-border securities holdings will strengthen coverage of the "rest of the world" sector of the U.S. national balance sheet and flow of funds data.

[1] See IMF and Financial Stability Board Secretariat (2009, 2010) and IMF (2011).
[2] This recommendation is number 7 in the report.
[3] This recommendation is number 12 in the report.
[4] This recommendation is number 15 in the report.

bonds; holdings of agency and Treasury securities were little affected by the increased outreach and clarification of reporting responsibilities. Likewise, the new reporting is geographically concentrated: Of the $293 billion in new reporting on foreign holdings of U.S. securities, about $225 billion, or nearly 75 percent, is in Europe and the Caribbean, which

Table 1. TIC SLT reporting by reporter group, security type, and residence of owner or issuer
Billions of dollars except as noted, December 2011

	Total reporting	Reporting by new SLT reporters	Reporting by new reporters as share of total reporting
Total liabilities	**11,910**	**293**	**2.5%**
Treasury securities: Official	3,257	0	0.0%
Treasury securities: Private	1,091	6	0.6%
Agency securities: Official	615	0	0.0%
Agency securities: Private	436	2	0.5%
Corporate bonds: Official	98	0	0.0%
Corporate bonds: Private	2,562	30	1.2%
Corporate stocks: Official	594	31	5.2%
Corporate stocks: Private	3,258	223	6.8%
Total claims	**6,575**	**390**	**5.9%**
Government bonds	363	8	2.2%
Corporate bonds	1,732	70	4.0%
Corporate stocks	4,480	312	7.0%
By residence of owner or issuer			
Total liabilities	**11,910**	**293**	**2.5%**
Europe	4,339	99	2.3%
Canada	547	21	3.8%
Latin America	451	4	0.9%
Caribbean	1,448	125	8.6%
Asia	4,729	29	0.6%
All other	396	14	3.5%
Total claims	**6,575**	**390**	**5.9%**
Europe	2,876	89	3.1%
Canada	693	37	5.3%
Latin America	394	5	1.3%
Caribbean	1,032	227	22.0%
Asia	1,153	16	1.4%
All other	428	16	3.7%

together account for slightly less than half of total holdings. Of the nearly $400 billion in new reporting on U.S. positions abroad, about $225 billion—over half—comes from new reporters' Caribbean positions, which account for about 15 percent of such positions overall.

Aggregate Data in Comparison with Recent Survey Data

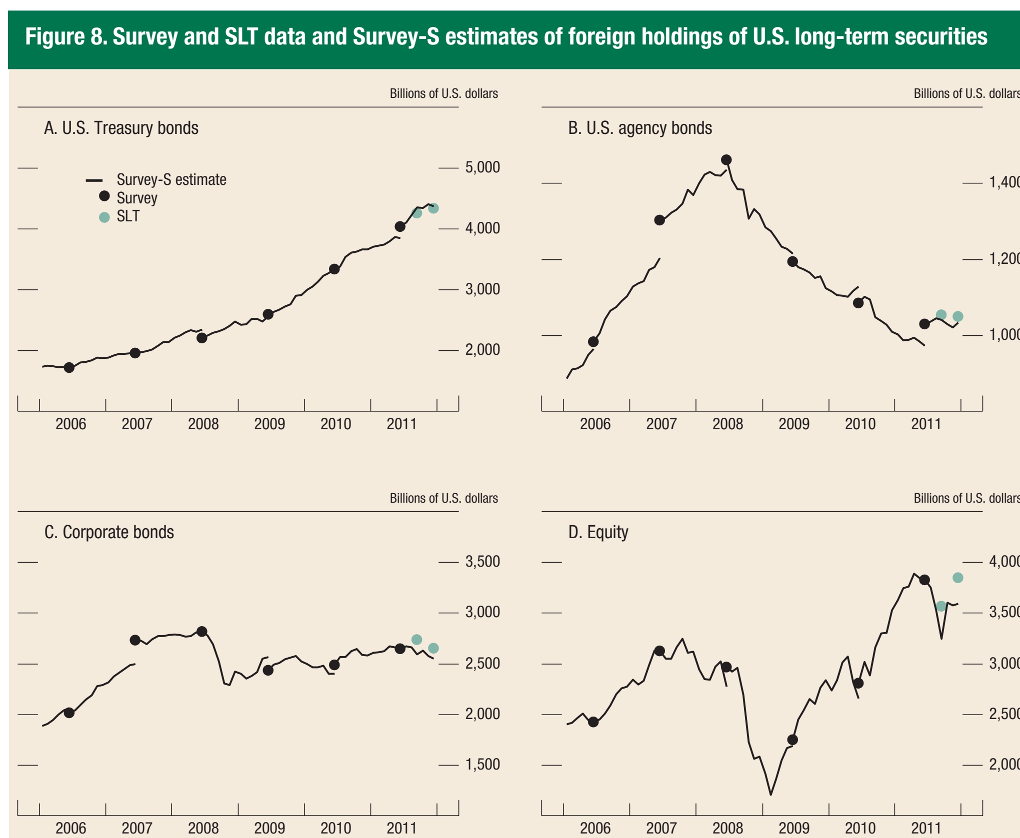
Holdings of U.S. Securities by Foreign Investors

The September and December 2011 SLT data, in terms of level, or position, are broadly in line with the most recent available survey data, from June 2011 for liabilities and from December 2010 for claims.

Figure 8 displays survey data and Survey-S estimates of U.S. liabilities for foreign residents through September 2011 and SLT data for September and December 2011. The lines indicate Survey-S estimates for total foreign holdings. The black and green circles indicate survey and SLT readings, respectively.[24] Thus, the vertical distance between the green circles and the black lines indicates the differences between SLT data and our Survey-S estimates based on the June 2011 liabilities survey.

For Treasury bonds, the SLT data indicate holdings that are a bit below the Survey-S estimates, but, like the estimates, indicate that foreign holders continue to increase their holdings. For U.S. government agency bonds, the SLT data are a bit above the Survey-S esti-

Figure 8. Survey and SLT data and Survey-S estimates of foreign holdings of U.S. long-term securities



24 As in the earlier figures, the position estimates are calculated as the valuation-adjusted level from the previous period plus TIC S transactions adjusted for ABS repayments and stock swaps.

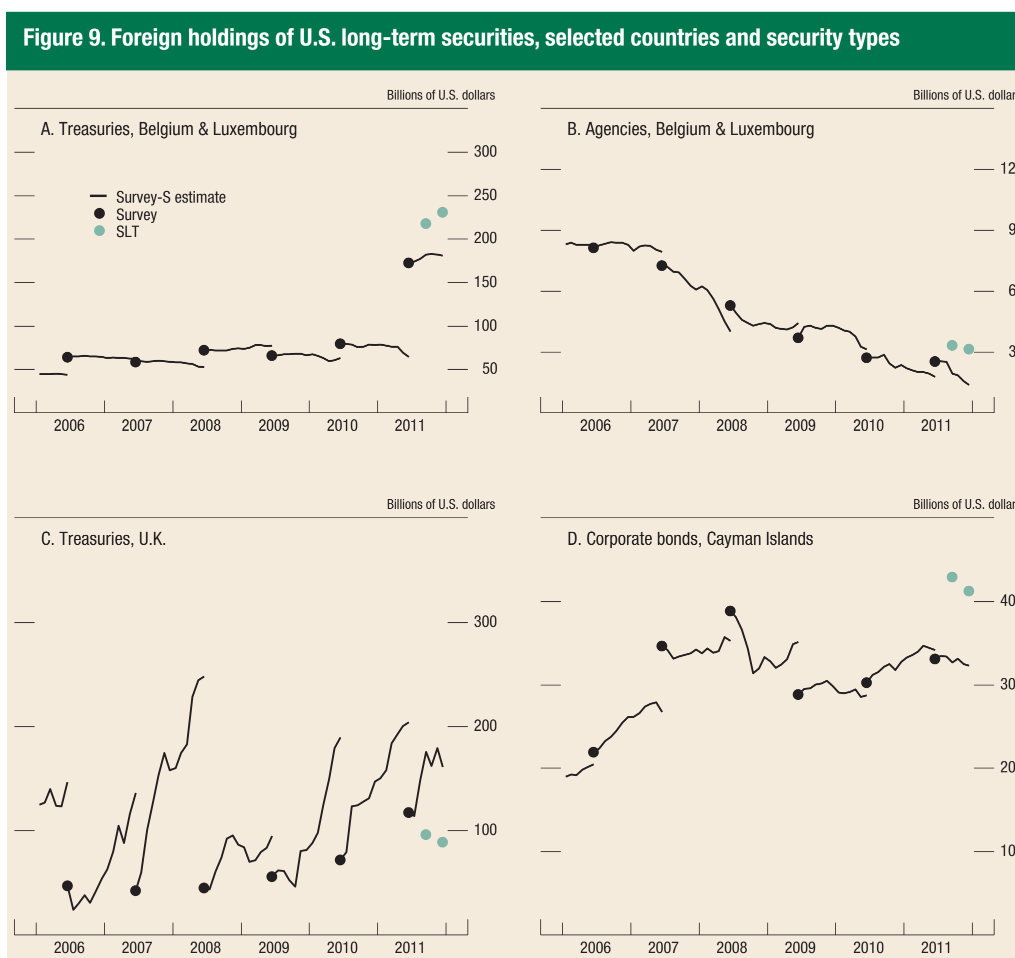


Figure 9. Foreign holdings of U.S. long-term securities, selected countries and security types

mates, suggesting that foreign positions in U.S. agencies might be recovering a bit more quickly than the earlier estimates indicate. For corporate bonds and equity, the SLT shows slightly higher positions than the Survey-S estimates; in large part, these higher positions are due to new reporting, as shown in table 1. In addition, unlike the Survey-S estimates, the SLT data do not include an adjustment for overreporting of securities, which can occur if an issuer reports securities issued directly into foreign markets as fully foreign held, while U.S. custodians simultaneously report foreign holdings of those securities.[25] As a result, the SLT data for existing reporters will typically exceed amounts reported in the liabilities surveys. Even with this expanded reporting coverage, though, the SLT data show that foreign holdings of U.S. corporate debt remain well below their pre-crisis levels.

For specific countries, however, the SLT data show some unexpected developments (figure 9). For example, Treasury bonds held in Belgium and Luxembourg on the SLT are considerably higher than the Survey-S estimates would indicate (panel A). This pattern has appeared in previous years and is likely due to transactions bias, where the purchases are recorded through other financial centers such as the United Kingdom. Agency debt holdings also appear to be moving up, contrary to earlier patterns (panel B). However, the concentration of these holdings—especially of Treasury securities—in such known custodial centers also serves as a reminder that, for U.S. securities, the SLT data are subject to the

[25] This adjustment can only be made at the security level with the annual surveys (the SLT is collected at the aggregate level). In recent years, this adjustment has been around $70 billion.

same custodial bias as the annual liabilities survey, and that these increased holdings in Belgium and Luxembourg are not necessarily on behalf of residents of those countries. Thus, these movements might point to changes in custodial or transactions behavior by investors outside Belgium and Luxembourg.

SLT data on Treasury holdings by the United Kingdom are considerably lower than the Survey-S estimates; such a discrepancy is to be expected given transactions bias (panel C). The SLT data indicate lower U.K. holdings in late 2011 than was indicated by the June 2011 survey; this movement could likewise indicate changes in custodial patterns.

Finally, U.S. corporate bond holdings by residents of the Cayman Islands as reported on the SLT are well above S-based estimates (panel D). Although the expanded reporting panel overall accounts for much of the higher foreign holdings of U.S. corporate bonds, in this instance, it is contributing relatively little—less than $10 billion. More thorough reporting by existing reporters contributes another significant piece—as much as $30 billion—of the approximately $80 billion increase. A more complete explanation for this difference will likely only be possible through comparison with the data from the next annual survey for June 2012.

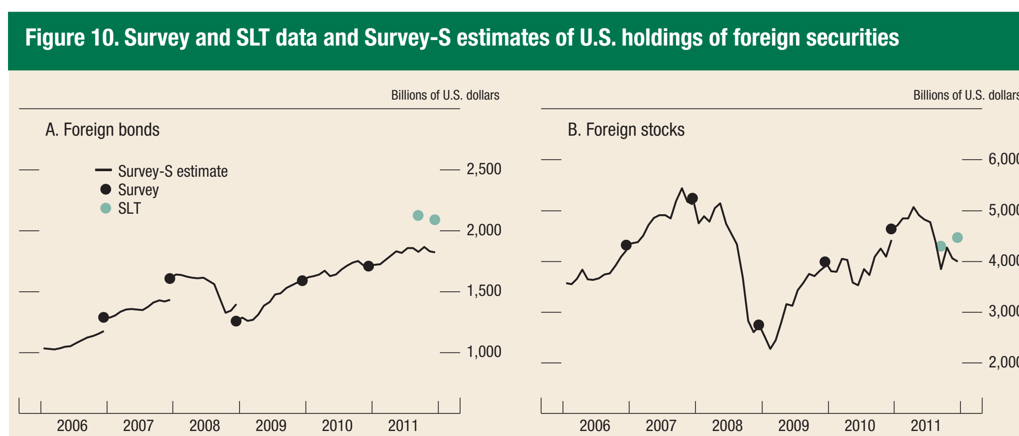
Holdings of Foreign Securities by U.S. Investors

In contrast to the TIC SLT data on U.S. liabilities to foreign residents, which are broadly in line with Survey-S estimates, the TIC SLT data for U.S. holdings of foreign bonds and equity in September and December were significantly higher than Survey-S estimates.

The December SLT data for U.S. holdings of foreign bonds (figure 10, panel A) point to a fairly sharp run-up over 2011, about $300 billion above the Survey-S estimates—the vertical distance between the green dot and the black line and about $400 billion up from the end of 2010—the vertical distance between the last black dot and the latter green dot.

These increases are only partially explained by the new reporters on the TIC SLT. As noted in table 1, new SLT reporters accounted for only about $80 billion of U.S. holdings of foreign bonds in December; about $10 billion in additional reporting came from entities that had been reporting on the liabilities survey but not on the claims survey. Aside from the new reporting, the remaining difference of about $200 billion is likely due to some combination of missing transactions on the TIC S, incorrectly estimated valuation changes, and, possibly, incorrect reporting or valuation on the SLT. We will be looking for further clarification from the December 2011 survey data.

Figure 10. Survey and SLT data and Survey-S estimates of U.S. holdings of foreign securities



U.S. holdings of foreign equity (figure 10, panel B) were about $4.7 trillion at the end of 2010. Using the Survey-S estimation approach discussed above, these holdings dropped about $700 billion, to around $4 trillion, by the end of 2011. Of the estimated $700 billion decline, cumulative valuation losses totaled about $725 billion, which was partially offset by roughly $25 billion in purchases, as recorded by the TIC S. The December 2011 SLT measurement of about $4.5 trillion is considerably higher, largely due to expanded reporting. As noted in table 1, new SLT reporters accounted for a total of about $300 billion in newly reported holdings of foreign equity. Of this $300 billion, nearly $200 billion was in the Cayman Islands, reflecting the efforts to incorporate reporting from hedge funds, private equity funds, and other managed funds. In addition to the increase in reporting from new reporters, as with bonds, the SLT collected data from reporters who had been reporting on the liabilities survey but not the claims survey: this group of reporters accounted for a total of about $130 billion in U.S. holdings of foreign equity on the December 2011 SLT.

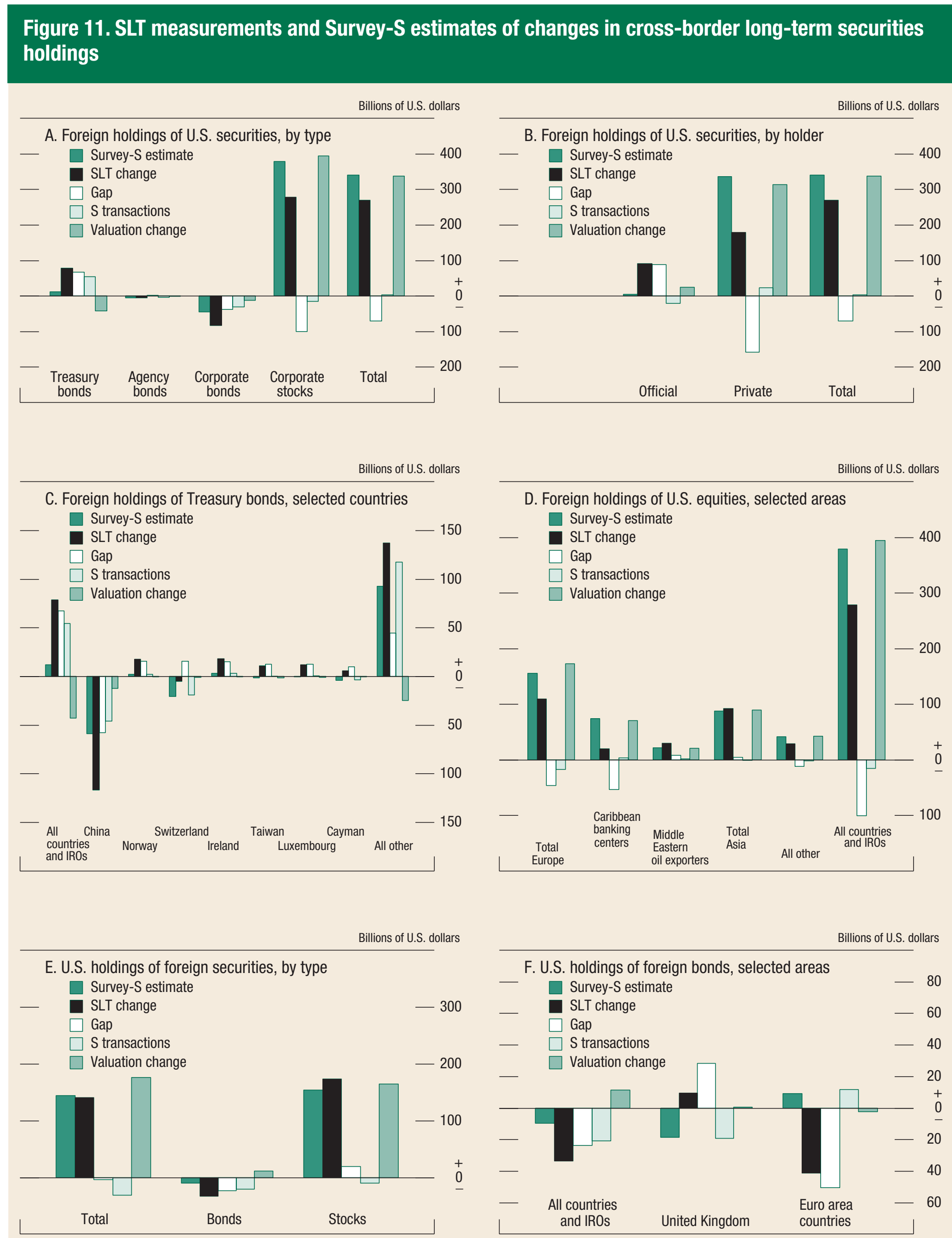
Assuming that the SLT data turn out to be consistent with the December 2011 claims survey data, this first look at the SLT suggests that U.S. residents' holdings of foreign bonds have increased more rapidly than previous estimates suggest. As did the annual survey, the SLT confirmed that U.S. investors' holdings of foreign bonds are concentrated in corporate debt securities. Holdings of government bonds account for roughly 20 percent of foreign bond holdings; this proportion is about the same as in the survey. Thus, the SLT data indicate that foreign bond holdings—most likely holdings of foreign corporate bonds—now exceed their 2007 peak by a substantial margin, perhaps suggesting that U.S. investors are increasingly interested in overseas investments. The SLT data also suggest that U.S. residents' holdings of foreign equity, while well below earlier peaks, seem to have declined less than earlier estimates indicated.

Fourth-Quarter Changes in Positions: SLT and Survey-S Estimates

As discussed above, the SLT data for September and December generally indicate higher cross-border positions than the Survey-S estimates would suggest. With the release of the September and December 2011 SLT data, it is possible to examine fourth-quarter changes in holdings from the SLT data with changes from the Survey-S estimates. (In previous years, such comparisons were only possible with the release of survey data nearly a year after the reporting date.) The differences between the SLT movements and those implied by the Survey-S estimates result from several factors: custodial and transactions bias, the effects of applying price index values to all holdings of U.S. securities by foreigners in construction of the Survey-S estimates, possible misreporting of the market value of securities on the TIC SLT, and gaps that arise from cross-border acquisitions or sales of securities that are not reported on the TIC S. These transactions may not be reported because they are conducted through intermediaries that fall outside of the TIC reporting system or because of missed reporting.

As seen in figure 11, large portions of the estimated movements, especially for equity, come from estimated valuation changes, the medium green bars. Precisely estimating valuation changes can be challenging. In the Survey-S estimates, we assume that valuation changes can be approximated by standard indexes of equity prices such as the MSCI. However, with much of the new reporting coming from a variety of managed funds, it is difficult to know how well valuation gains or losses on these funds can be approximated by standard broad equity indexes. For example, cross-border holdings of all types of funds—including funds that invest in foreign bonds, U.S. Treasury securities, or commodities, as well as money market funds—are classified as "equity" in the surveys and the SLT. Thus, the securities portfolios of these diverse types of funds might have price movements that differ from those of standard indexes. In the coming year, the incoming December 2011 claims survey and the June 2012 liabilities survey data should allow us to better assess the actual returns

Figure 11. SLT measurements and Survey-S estimates of changes in cross-border long-term securities holdings



earned on cross-border investments over this period as well as to assess the potential magnitude of missed transactions.[26]

Although there are only two observations to compare, the SLT is already signaling movements in some asset categories that suggest different trends in cross-border portfolios than the Survey-S estimates. Overall, as shown in the rightmost set of bars in figure 11, panel A,

[26] Initial indications are that reporting errors are minor. The data screening and evaluation process for the new SLT data included analysis of each reporter's filings at the country and SLT item level compared to the analogous data from the most recent survey. These data reviews indicated that valuations as reported on the SLT were generally consistent with reporters' survey filings, which in turn generally provided accurate valuations.

the SLT shows an increase in foreign residents' holdings of U.S. securities of nearly $300 billion, the rightmost black bar, in the fourth quarter of 2011, a smaller increase than the nearly $350 billion increase indicated by the change in the Survey-S estimates, the rightmost dark green bar. The difference between these two measures—the estimation gap (shown in white)—however, is not evenly distributed across security types, as indicated by the other sets of bars. The TIC SLT indicated that foreign holdings of Treasury securities increased nearly $80 billion between September and December, the leftmost black bar. This increase is substantially larger than suggested by the Survey-S estimates: TIC S transactions, the leftmost pale green bar, indicated that foreign investors purchased on net roughly $50 billion in Treasury securities over the quarter. But because Treasury prices declined roughly 1 percent over the period, valuation changes, the leftmost medium green bar, are estimated to have reduced the market value of foreign holdings about $40 billion, generating a combined Survey-S increase of only about $10 billion, the leftmost dark green bar. With the SLT indicating that foreign holdings of U.S. Treasury securities rose about $80 billion, this difference suggests that foreign net purchases could have been larger than recorded in the TIC S.

The SLT shows small declines in foreign holdings of U.S. agency bonds and corporate debt securities, broadly consistent with the Survey-S estimates. In contrast, the SLT indicated that foreign investors' holdings of U.S. equity increased about $280 billion, the fourth black bar, considerably less than the Survey-S estimate of $380 billion, the fourth dark green bar; we discuss these differences in more detail in the following section.

The SLT also indicated a different breakdown of such changes by type of holder (figure 11, panel B): Foreign official positions increased more than earlier estimates indicated while private positions increased by less; as discussed above, these differences are likely due to transactions bias that does not classify purchases of U.S. securities as foreign official purchases if they occur through third-party countries.

The SLT data also show some surprising changes by country for foreign holdings of Treasury securities (panel C). The SLT showed that holdings attributed to China declined by more in the fourth quarter of 2011—about $120 billion—than suggested by the Survey-S estimates—about $60 billion. The larger-than-estimated decline in holdings could indicate that Chinese official investors sold more Treasury securities than recorded, or that they have shifted some of their Treasury holdings and transactions to custodians and financial intermediaries abroad. Such shifts are not recorded as sales because the ownership of the security is unchanged—only the location of ownership is changed.[27] In contrast, Treasury holdings for several countries, including Norway, Switzerland, Ireland, Taiwan, Luxembourg, and the Cayman Islands increased considerably more than the estimates indicated.

Foreign Holdings of U.S. Equity

As displayed in panel D of figure 11, the fourth-quarter change in foreign holdings of U.S. equity as measured by the SLT was about $100 billion less than the change implied by the Survey-S estimate, showing that foreign investors' holdings of U.S. equity increased about $280 billion rather than $380 billion. This category of securities is heavily affected by measures of valuation changes. Indeed, nearly all of the Survey-S estimated changes are due to valuation changes, as shown by the medium green bars. The differences between the SLT and estimated Survey-S changes were dominated by gaps in Europe and the Caribbean,

[27] See FAQ A.5, "How are TIC data used by BEA and the Federal Reserve? Where else are TIC data reported or used?" on the Treasury's webpage, "Frequently Asked Questions Regarding the TIC System and TIC Data," www.treasury.gov/resource-center/data-chart-center/tic/Pages/ticfaq1.aspx at the TIC website, www.treasury-.gov/resource-center/faqs/Treasury-International-Capital/Pages/tic-faqs.aspx.

regions known to be subject to substantial transactions bias. In addition, these regions are centers of incorporation for many foreign investment funds, and as discussed above, returns earned on fund holdings may not be well approximated by the standard equity price indexes applied in the estimated Survey-S changes. Overall, the SLT indicates lower foreign holdings of U.S. equity in Europe and the Caribbean, but larger-than-estimated holdings by investors in the Middle East and in Asia.

SLT Data on Changes in U.S. Holdings of Foreign Securities

The SLT indicates slightly smaller increases in total U.S. holdings of foreign securities in the final quarter of 2011 than indicated by the Survey-S estimates (panel E)—about $170 billion rather than about $150 billion.[28] The Survey-S estimates for equity were reasonably close to those for the SLT, but the estimates for bonds were quite different. The SLT indicates that U.S. holdings of foreign bonds declined by about $30 billion (the first black bar)—compared with the $10 billion decrease suggested by the Survey-S estimates (the first dark green bar). Within Europe, though, there are large and offsetting gaps (panel F): The SLT indicates an increase in U.S. residents' holdings of U.K. bonds (the second black bar) whereas the Survey-S estimate points to a decrease (the second dark green bar). In contrast, for euro area countries, which suffered from severe financial strains during the latter half of 2011, the SLT indicates a decline in U.S. bond holdings of over $40 billion (the third black bar), a sharp contrast to the Survey-S's increase of about $10 billion (the third dark green bar). These differences likely reflect the transactions bias in the Survey-S estimates, with sales of euro area bonds that occurred through U.K. intermediaries recorded as "U.K. sales" and misinterpreted as decreases in holdings of U.K. bonds. In this case, the SLT provides much different information than would have been available otherwise about an area of ongoing concern.

Memo Items

As noted in box 1, the SLT incorporates reporting for memo items indicating the type of issuer of U.S. corporate securities, the type of U.S. holder of foreign securities, and two categories of securities: ABS and fund shares. These groupings were selected to conform to BPM6 guidelines. Feedback from respondents indicated that categorizing this information was a challenge, but nonetheless reporting in the first few months of the SLT was fairly complete and broadly consistent with analogous survey data. Respondents were able to categorize roughly 95 percent of both claims and corporate liabilities.

U.S. Issuers of Long-Term Securities Held by Foreign Residents

SLT reporting on the breakdown of cross-border holdings of U.S. long-term securities by issuer for December 2011 indicate that the largest share—about 60 percent—of U.S. long-term corporate debt and equity held by foreign investors was issued by nonfinancial firms, with the next substantial portion—just under 30 percent—issued by financial firms other than depository institutions, such as mutual funds, investment banks, issuers of corporate ABS, and insurance companies. Of the remaining 10 percent, about 8 percent was issued by depository institutions and the residual was issued by state and local governments. These shares are roughly in line with the industry classifications derived from the 2010 and 2011 liabilities surveys.[29]

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[28] Although the SLT collects data on U.S. holdings of foreign bonds separately for government and corporate bonds, the TIC S collects data only for bonds, and so comparisons to Survey-S estimates must be calculated at the higher level of aggregation.

[29] See table 18 in U.S. Department of the Treasury, Federal Reserve Bank of New York, and Board of Governors of the Federal Reserve System (2011).

Table 2. Comparison of Survey and SLT data on cross-border holdings of asset-backed securities
Billions of dollars except as noted

	U.S. government agency securities[1]		U.S. corporate bonds[1]		Foreign corporate bonds[2]	
	Total	Share	Total	Share	Total	Share
SLT	730	70%	487	18%	266	16%
Survey	712	69%	428	16%	193	11%

[1] Survey data from June 2011 liabilities survey.
[2] Survey data from December 2010 claims survey.

U.S. Holders of Foreign Long-Term Securities

The SLT also collects data on U.S. holders of foreign securities. Reporting coverage was reasonably good for these items as well. This breakdown shows that, for debt as well as equity, U.S. holders were largely financial firms other than depository institutions, such as investment banks, securities broker–dealers, managed funds, and insurance companies. Although the TIC claims survey collects some broad categories on type of owner for foreign securities, there is currently only limited overlap in these categories and those collected on the SLT, and it is therefore difficult to make comparisons between the SLT and survey data.

Fund Shares and ABS

SLT and survey data on foreign holdings of U.S. ABS and equity fund shares are broadly comparable (table 2). Both data sources indicate that foreign holdings of U.S. government agency securities were dominated by ABS (nearly all mortgage-backed securities), which accounted for about 70 percent of all cross-border holdings of agency debt securities. Both data sources report a considerably lower ABS share for foreign holdings of U.S. corporate bonds, around 15 to 20 percent.

However, on the claims side, U.S. holdings of foreign securities, the survey and SLT figures for cross-border holdings of ABS differ by a substantial margin. The survey figure for U.S. holdings of foreign corporate ABS as a share of all such holdings is 11 percent while the corresponding SLT figure is 16 percent. While this difference could indicate that U.S. acquisitions of foreign ABS picked up markedly since December 2010, it seems likely that at least part of this difference might be due to changes or differences in valuation methods adopted by reporters in the SLT compared with those in the claims survey data; as noted in Bertaut and Pounder (2009), valuation is especially challenging for ABS. For such differences, the detailed survey data will be critical. We expect that comparison of the December 2011 SLT and claims survey data will reveal whether this difference reflects movements in ABS holdings or difficulties with ABS valuation.

SLT and survey data for U.S. holdings of foreign equity fund shares are likewise fairly comparable (table 3) though comparisons are somewhat more challenging in this category because reporting requirements are slightly different for the survey and the SLT. Both sources indicate that common stock (as reported on the survey) or all equity less fund shares (as reported on the SLT) account for about 80 percent of cross-border holdings of domestic equity and about 90 percent of such holdings of foreign equity.

Table 3. Comparison of Survey and SLT data on cross-border holdings of equity fund shares and common stock
Billions of dollars except as noted

	Domestic equity: Common stock		Foreign equity: Common stock	
	Total	Share	Total	Share
SLT	3,056	80%	3,965	89%
Survey	3,070	79%	4,327	93%

Note: SLT common stock totals estimated as total equity less fund shares.

Conclusion

The new TIC SLT is designed to provide readings on cross-border positions in long-term securities that are much timelier than the existing annual surveys and more accurate than estimates based on the TIC S transactions. Movements in ownership of these securities are an important barometer of cross-border investor sentiment; in times of financial strain and crisis, more timely and accurate measurements of cross-border financial movements can indicate where strains might be more or less acute, and can point to near-term and longer-term prospects for asset prices and for the financing of current account imbalances.

The SLT data are subject to the same custodial bias present in the liabilities surveys, which means that the SLT also cannot fully attribute foreign holdings of U.S. securities by country of ultimate investor. Moreover, despite ongoing efforts to reconcile holdings reported on the SLT with data reported on the annual surveys and through the TIC S, some degree of reporting error likely remains. We anticipate that fuller analysis and comparisons with annual survey data from months when the SLT was also being compiled (December 2011 for claims and June 2012 for liabilities) will allow for more-expansive analysis of SLT data quality and trends.

The initial TIC SLT data for September and December 2011 are generally consistent with the more comprehensive measures of securities holdings collected in the annual surveys and with the intermediate estimates, which are based on subsequent transactions and adjustments for valuation changes in securities holdings, providing considerable comfort that this new data initiative will be able to provide reliable measures of U.S. cross-border securities positions on a timely basis. Nonetheless, the first two data collections for September and December 2011 reveal some important developments. First, the SLT data, partially due to expanded reporting, are showing somewhat higher foreign holdings of U.S. securities and U.S. holdings of foreign securities than expected, based on the most recent surveys and intermediate transactions-based estimates. For the final quarter of 2011, the first period for which a time-series comparison is possible, the SLT data point to smaller changes in holdings in both foreign holdings of U.S. securities and U.S. holdings of foreign securities than the Survey-S estimates. More specifically, contrary to earlier estimates based on TIC S and survey data which indicated that U.S. investors slightly increased their holdings of euro area bonds, the SLT indicates the reverse: U.S. investors reduced their holdings of these assets by about 10 percent during this difficult time for European financial markets. The SLT also points to stronger foreign demand for U.S. Treasury securities overall but a steeper decline in China's holdings of Treasury securities than had been estimated earlier. Going forward, the SLT will allow for much more timely and accurate tracking of these and other developments—up to a year earlier than had been possible—and, as circumstances warrant, correspondingly more timely policy responses.

Appendix A: The TIC Reporting System

Under the current Treasury International Capital (TIC) reporting system, an assortment of monthly and quarterly reports are filed with district Federal Reserve Banks by commercial banks, securities dealers, other financial institutions, and nonbanking enterprises in the United States (table A.1). These data are centrally processed and maintained at the Federal

Table A.1. Summary of TIC reporting forms

TIC form	Position or flow	Item	Valuation method	Frequency	Reporter type	Magnitude** (Billions of U.S. dollars as of last reporting date in 2011)
BC: Report of U.S. Dollar Claims on Foreigners	Position	Deposit accounts, loans, short-term securities, and other claims	Face	Monthly	U.S.-resident entities	$3,177
BL-1: Report of U.S. Dollar Liabilities to Foreign Residents	Position	Deposits, short-term securities, and other own liabilities	Face	Monthly	U.S.-resident entities	$3,628
BL-2: Report of Customers' U.S. Dollar Liabilities to Foreigners	Position	Short-term securities and other custody liabilities	Face	Monthly	U.S.-resident entities	$1,022
BQ-1: Report of Customers' U.S. Dollar Claims on Foreigners	Position	Deposit accounts, short-term securities, and other custody claims	Face	Quarterly	U.S.-resident entities	$676
BQ-2: **Part 1** – Report of Foreign Currency Liabilities and Claims on Foreigners **Part 2** – Report of Customers' Foreign Currency Liabilities to Foreigners	Position	Deposits, short-term securities, and other liabilities in foreign currency	Face	Quarterly	U.S.-resident entities	$655
BQ-3: Report of Maturities of Selected Liabilities to Foreigners	Position	Deposits, short-term securities, and other liabilities	Face	Quarterly	U.S.-resident entities	Not published*
CQ-1: Report of Financial Liabilities to, and Financial Claims on, Unaffiliated Foreign-Residents	Position	Deposits, short-term securities, and other liabilities and claims	Face	Quarterly	U.S.-resident entities	$61
CQ-2: Report of Commercial Liabilities to, and Commercial Claims on, Unaffiliated Foreign-Residents	Position	Trade payables, advance receipts, and other liabilities; trade receivables, advance payments, and other claims	Face	Quarterly	U.S.-resident entities	$118
D: Report of Holdings of, and Transactions in, Financial Derivatives Contracts	Position and net flows	Derivatives contracts	Fair value	Quarterly	U.S.-resident entities with derivatives contracts	Gross pos. FV: $4,705 Gross neg. FV: $4,578 Net settlements: $33
S: Purchases and Sales of Long-Term Securities by Foreign-Residents	Flow	Long-term securities	Market	Monthly	Brokers and dealers, security underwriters, issuers of securities, end investors	U.S. securities: • For. purch.: $1,650 • For. sales: $1,669 • For. official purch: $101 • For. official sales: $111 Foreign securities: • U.S. purch.: $505 • U.S. sales: $543
SHCA: Report of U.S. Ownership of Foreign Securities, Including Selected Money Market Instruments	Position	Long- and short-term securities	Market	Annual: December	Large custodial banks, security broker–dealers, end investors	$6,763
SHLA: Foreign-Residents' Holdings of U.S. Securities, Including Selected Money Market Instruments	Position	Long- and short-term securities	Market	Annual: June	Large custodial banks, issuers, security broker–dealers	$12,440
SLT: Aggregate Holdings of Long-Term Securities by U.S. and Foreign Residents	Position	Long-term securities	Market	Monthly	Large custodial banks, issuers, end investors, managed funds	U.S. liabilities: $11,910 Foreign claims: $6,575

Note: U.S.-resident entities include depository institutions, bank holding companies, financial holding companies, and securities broker–dealers.

** Totals as of end-December 2011.

* The BQ-3 data include maturity breakdowns used for supplemental calculations.

Reserve Bank of New York, which, along with the district banks, acts as fiscal agent for the U.S. Treasury. Since late 1998, the Federal Reserve Board also has supported the TIC data collection system by providing final review and dissemination of TIC data to the Treasury as well as to other agencies, including the Bureau of Economic Analysis and the Bank for International Settlements. The TIC reports of individual respondents are treated as confidential and access to the respondent-level data is strictly limited to specific staff of the Treasury and the Federal Reserve System.

Data derived from Treasury reports are posted monthly on the TIC website, www.ustreas.gov/tic. TIC data aggregates are also published monthly at the Federal Reserve's website, www.federalreserve.gov/econresdata/releases/secholdtrans/current.htm, and are used in the U.S. international transactions and investment position compilations published by the Department of Commerce in the *Survey of Current Business.*

Report Forms

TIC BC (for U.S. claims) collects data on U.S.-resident banks' claims on foreigners, including deposit accounts, loans, and foreign short-term securities held by U.S. residents as reported by banks, other depository institutions, and securities brokers and dealers in the United States. Bank holding companies (BHCs) and financial holding companies (FHCs) also report for their domestic nonbank and nonsecurities firm affiliates, other than their insurance affiliates, who report separately on the C-series forms. Data on respondents' own dollar claims are collected monthly on Form BC. Data on claims held for domestic customers as well as on claims denominated in foreign currencies is collected on a quarterly basis only on forms BQ-1 and BQ-2, respectively.

TIC BL forms (for U.S. liabilities) cover U.S.-resident banks' liabilities to foreigners, including deposits, U.S. short-term securities held by foreigners, and other liabilities as reported by banks, other depository institutions, and securities brokers and dealers in the United States. BHCs and FHCs also report for all domestic nonbank, nonsecurities firm affiliates, other than their insurance affiliates, who report separately on the C-series forms. Banks' own dollar-denominated liabilities are reported monthly on form BL-1, and customers' dollar-denominated liabilities are reported monthly on form BL-2. Liabilities denominated in foreign currencies are reported quarterly on form BQ-2.

TIC CQ forms collect quarterly data on the liabilities to, and claims on, unaffiliated foreigners of exporters, importers, industrial and commercial concerns, financial institutions (other than banks, other depository institutions, and securities brokers and dealers), and other nonbanking enterprises in the United States. Financial claims and liabilities, such as deposits and short-term securities, are reported on the CQ-1. Commercial claims and liabilities, such as trade receivables and payables, are reported on the CQ2. Data exclude claims on foreigners held in custody by banks in the United States.

TIC D collects quarterly data on holdings and net cash settlements of cross-border derivatives contracts reported by banks, securities brokers, dealers, and nonfinancial companies in the United States with sizable holdings of derivatives contracts. Total holdings are divided between those contracts with positive fair values and those contracts with negative fair values from the perspective of the reporter. The fair (market) value is generally defined as the amount for which a derivative contract could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

TIC S collects monthly data on gross purchases and gross sales between U.S. residents and foreign residents in long-term domestic and foreign securities as reported by banks, securities brokers and dealers, and other financial intermediaries in the United States. A memo-

randum section reports the transactions in U.S. securities that represent purchases or sales by foreign official institutions.

TIC SHCA and SHC forms collect the annual and benchmark TIC survey data on U.S. holdings of foreign long- and short-term securities at the individual security level.

TIC SHLA and SHL forms collect the annual and benchmark TIC survey data on foreign residents' holdings of U.S. long- and short-term securities at the individual security level.

TIC SLT collects monthly data at the aggregate level on foreign holdings of U.S. long-term securities and on U.S. holdings of foreign long-term securities by broad security type.

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Changes in U.S. Family Finances from 2007 to 2010: Evidence from the Survey of Consumer Finances

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The Federal Reserve Board's Survey of Consumer Finances (SCF) for 2010 provides insights into changes in family income and net worth since the 2007 survey.[1] The survey shows that, over the 2007–10 period, the median value of real (inflation-adjusted) family income before taxes fell 7.7 percent; median income had also fallen slightly in the preceding three-year period (figure 1). The decline in median income was widespread across demographic groups, with only a few groups experiencing stable or rising incomes. Most noticeably, median incomes moved higher for retirees and other nonworking families. The decline in median income was most pronounced among more highly educated families, families headed by persons aged less than 55, and families living in the South and West regions. Real mean income fell even more than median income in the recent period, by 11.1 percent across all families. The decline in mean income was even more widespread than the decline in median income, with virtually all demographic groups experiencing a decline between 2007 and 2010; the decline in the mean was most pronounced in the top 10 percent of the income distribution and for higher education or wealth groups. Over the preceding three years, mean income had risen, especially for high-net-worth families and families headed by a person who was self-employed.

The decreases in family income over the 2007–10 period were substantially smaller than the declines in both median and mean net worth; overall, median net worth fell 38.8 percent, and the mean fell 14.7 percent (figure 2). Median net worth fell for most groups between 2007 and 2010, and the decline in the median was almost always larger than the decline in the mean. The exceptions to this pattern in the medians and means are seen in the highest 10 percent of the distributions of income and net worth, where changes in the median were relatively muted. Although declines in the values of financial assets or business were important factors for some families, the decreases in median net worth appear to have been driven most strongly by a broad collapse in house prices.[2] This collapse is reflected in the patterns of change in net worth across demographic groups to varying degrees, depending

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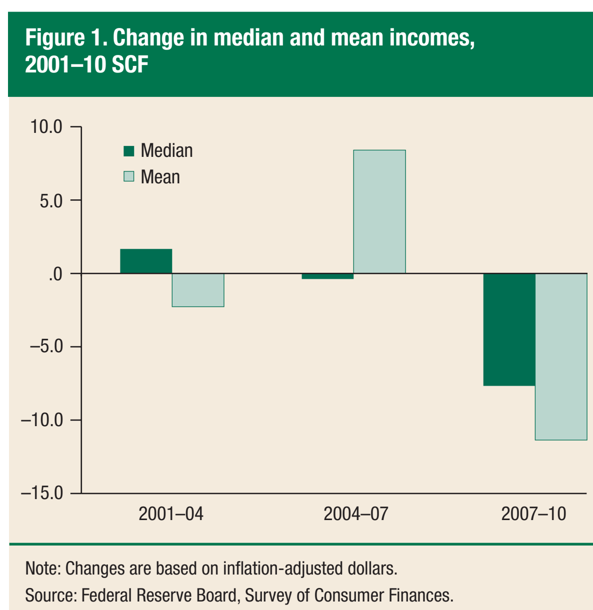
[1] For a detailed discussion of the 2004 and 2007 surveys as well as references to earlier surveys, see Brian K. Bucks, Arthur B. Kennickell, Traci L. Mach, and Kevin B. Moore (2009), "Changes in U.S. Family Finances from 2004 to 2007: Evidence from the Survey of Consumer Finances," *Federal Reserve Bulletin*, vol. 95, pp. A1–A55, www.federalreserve.gov/pubs/bulletin/default.htm. Information about changes in family finances between 2007 and 2009 based on a re-interview of 2007 SCF families can be found in Jesse Bricker, Brian Bucks, Arthur Kennickell, Traci Mach, and Kevin Moore (2011), "Surveying the Aftermath of the Storm: Changes in Family Finances from 2007 to 2009," Finance and Economics Discussion Series 2011-17 (Washington: Board of Governors of the Federal Reserve System, March), www.federalreserve.gov/pubs/feds/2011/201117/index.html

[2] If primary residences and the associated mortgage debt are excluded, the median of families' net worth is reduced from $126,400 to $42,300 in 2007 and from $77,300 to $29,800 in 2010. Although the adjusted wealth measure declined proportionately by only a somewhat smaller amount than the unadjusted measure—29.7 percent—the

Figure 1. Change in median and mean incomes, 2001–10 SCF



Note: Changes are based on inflation-adjusted dollars.
Source: Federal Reserve Board, Survey of Consumer Finances.

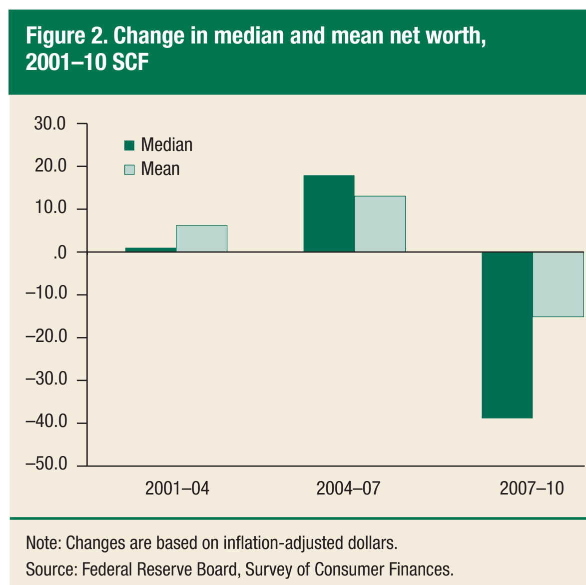
on the rate of homeownership and the proportion of assets invested in housing. The decline in median net worth was especially large for families in groups where housing was a larger share of assets, such as families headed by someone 35 to 44 years old (median net worth fell 54.4 percent) and families in the West region (median net worth fell 55.3 percent).

A substantial part of the declines observed in net worth over the 2007–10 period can be associated with decreases in the level of unrealized capital gains on families' assets. The share of total assets of all families attributable to unrealized capital gains from real estate, businesses, stocks, or mutual funds fell 11.6 percentage points, to 24.5 percent in 2010. Although the overall level of debt owed by families was basically unchanged, debt as a percentage of assets rose because the value of the underlying assets (especially housing) decreased faster.

With overall median and mean debt basically unchanged or falling less than income, measures of debt payments relative to income might have been expected to increase. In fact, total payments relative to total income increased only slightly, and the median of payments relative to income among families with debt fell after having risen between 2004 and 2007. The share of families with high payments relative to their incomes also fell after rising substantially between 2001 and 2007.

This article reviews these and other changes in the financial condition of U.S. families between 2007 and 2010.[3] The discussion draws on data from the Federal Reserve Board's SCF for those years; it also uses evidence from other years of the survey and a special panel SCF conducted from 2007 to 2009 to place the 2007–10 changes in a broader context.

Figure 2. Change in median and mean net worth, 2001–10 SCF



Note: Changes are based on inflation-adjusted dollars.
Source: Federal Reserve Board, Survey of Consumer Finances.

amount of the change is, obviously, much smaller; median adjusted wealth declined $12,600, while the unadjusted measure fell $49,100.

[3] See box 1, "The Data Used in This Article," for a general description of the data. The appendix to this article provides a summary of key technical aspects of the survey. See also Bucks, Kennickell, Mach, and Moore, "Changes in U.S. Family Finances from 2004 to 2007," and Bricker, Bucks, Kennickell, Mach, and Moore, "Surveying the Aftermath of the Storm."

Box 1. The Data Used in This Article

Data from the Survey of Consumer Finances (SCF) are the basis of the analysis presented in this article. The SCF is normally a triennial interview survey of U.S. families sponsored by the Board of Governors of the Federal Reserve System with the cooperation of the U.S. Department of the Treasury. Since 1992, data for the SCF have been collected by NORC, a research organization at the University of Chicago, roughly between May and December of each survey year.

The majority of statistics included in this article are related to characteristics of "families." As used here, this term is more comparable with the U.S. Census Bureau definition of "households" than with its use of "families," which excludes the possibility of one-person families. The appendix provides full definitions of "family" for the SCF and the associated family "head." The survey collects information on families' total income before taxes for the calendar year preceding the survey. But the bulk of the data cover the status of families as of the time of the interview, including detailed information on their balance sheets and use of financial services as well as on their pensions, labor force participation, and demographic characteristics. Except in a small number of instances (see the appendix and the text for details), the survey questionnaire has changed in only minor ways relevant to this article since 1989, and every effort has been made to ensure the maximum degree of comparability of the data over time.

The need to measure financial characteristics imposes special requirements on the sample design for the survey. The SCF is expected to provide reliable information both on attributes that are broadly distributed in the population (such as homeownership) and on those that are highly concentrated in a relatively small part of the population (such as closely held businesses). To address this requirement, the SCF employs a sample design, essentially unchanged since 1989, consisting of two parts: a standard, geographically based random sample and a special oversample of relatively wealthy families. Weights are used to combine information from the two samples to make estimates for the full population. In the 2010 survey, 6,492 families were interviewed, and in the 2007 survey, 4,421 were interviewed.

This article draws principally upon the final data from the 2010 and 2007 surveys. To provide a larger context, some information is also included from the final versions of earlier surveys, as well as a panel interview in 2009 with respondents to the 2007 survey.[1] Differences between estimates from earlier surveys as reported here and as reported in earlier *Federal Reserve Bulletin* articles are attributable to additional statistical processing, correction of minor data errors, revisions to the survey weights, conceptual changes in the definitions of variables used in the articles, and adjustments for inflation. In this article, all dollar amounts from the SCF are adjusted to 2010 dollars using the "current methods" version of the consumer price index for all urban consumers (CPI-U-RS). The appendix provides additional detail on the adjustments.

The principal detailed tables describing asset and debt holdings focus on the percentage of various groups that have such items and the median holding for those who have them.[2] This conditional median is chosen to give a sense of the "typical" holding. Generally, when one deals with data that exhibit very large values for a relatively small part of the population—as is the case for many of the items considered in this article—estimates of the median are often statistically less sensitive to such outliers than are estimates of the mean.

One liability of using the median as a descriptive device is that medians are not additive; that is, the sum of the medians of two items for the same population is not generally equal to the median of the sum (for example, median assets less median liabilities does not equal median net worth). In contrast, means for a common population are additive. Where a comparable median and mean are given, the gain or loss of the mean relative to the median may usually be taken as indicative of the relative change at the top of the distribution; for example, when the mean decreases more rapidly than the median, it is typically taken to indicate that the values in the top of the distribution fell more than those in the lower part of the distribution.

continued on next page

Box 1—*continued*

To provide a measure of the significance of the developments discussed in this article, standard errors due to sampling and imputation for missing data are given for selected estimates. Space limits prevent the inclusion of the standard errors for all estimates. Although we do not directly address the statistical significance of the results, the article highlights findings that are significant or are interesting in a broader context.

[1] Additional information about the survey is available at www.federalreserve.gov/econresdata/scf/scf_2010.htm.

[2] The median of a distribution is defined as the value at which equal parts of the population considered have values larger or smaller.

Economic Background

Families' finances are affected by both their own decisions and the state of the broader economy. Over the 2007–10 period, the U.S. economy experienced its most substantial downturn since the Great Depression. Real gross domestic product (GDP) fell nearly 5.1 percent between the third quarter of 2007 and the second quarter of 2009, the official period of recession as determined by the National Bureau of Economic Research. During the same period, the unemployment rate rose from 5.0 percent to 9.5 percent, the highest level since 1983. Recovery from the so-called Great Recession has also been particularly slow; real GDP did not return to pre-recession levels until the third quarter of 2011. The unemployment rate continued to rise through the third quarter of 2009 and remained over 9.4 percent during 2010. The rate of inflation, as measured by the consumer price index for all urban consumers (CPI-U-RS), decreased somewhat over the period from an annual average of 2.8 percent in 2007 to 1.6 percent in 2010.

Financial markets moved dramatically over the three-year period. Major stock market indexes fell nearly 50 percent between September 2007 and March 2009, but about one-half of the losses in indexes such as the Dow Jones industrial average, the Standard & Poor's 500, and the Wilshire 5000 had been recouped by September 2010. Interest rates on new consumer loans generally fell; for example, the interest rate on a new 30-year fixed-rate mortgage averaged 6.38 percent in September 2007, when about one-half of the interviews for the 2007 survey had been completed, and the average rate was 4.35 percent three years later in September 2010. Yields fell dramatically on liquid deposits, time deposits, and bonds; for example, the rate on a three-month certificate of deposit (CD) fell from an average of 5.46 percent in September 2007 to 0.28 percent in September 2010.

Housing was of greater importance than financial assets for the wealth position of most families. The national purchase-only LoanPerformance Home Price Index produced by First American CoreLogic fell 22.4 percent between September 2007 and September 2010, by which point house prices were fully 27.5 percent below the peak achieved in April 2006. The decline in house prices was most rapid in the states where the boom had been greatest. For example, California, Nevada, Arizona, and Florida saw declines of 40 to 50 percent, while Iowa saw a decline of only about 1 percent. Homeownership rates fell over the period, in part because some families found it impossible to continue to afford their homes. By 2010, the homeownership rate was back down to a level last seen in the 2001 SCF, although that was still higher than in any previous SCF since at least 1989.

The Congress and the President responded to the economic situation with several legislative measures, some of which had an immediate effect on family finances, and some of which were intended to help prevent future crises. For example, in order to boost family after-tax incomes, the 2001 and 2003 income tax reductions originally scheduled to expire in 2010 were extended. In addition, employee payroll taxes earmarked for Social Security were reduced. In another move aimed at offsetting the decline in economic activity, the Troubled

Asset Relief Program allowed government infusion of equity into stressed financial institutions. Lawmakers also responded to the economic crisis by attempting to curtail practices that disproportionately affected vulnerable consumers, practices that some argued had contributed to the crisis. Most notably, the Dodd–Frank Wall Street Reform and Consumer Protection Act, passed in July 2010, contained prohibitions on certain lending practices and created the Consumer Financial Protection Bureau.

Several demographic shifts had important consequences for the structure of the population. The aging of the baby-boom population from 2007 to 2010 drove an 11.0 percent increase in the population aged 55 to 64. Overall population growth was about 2.7 percent, and, according to figures from the U.S. Census Bureau, 21.5 percent of that growth was due to net immigration. Also according to Census Bureau estimates, the number of households increased 1.2 percent—below the 2.3 percent rate of household formation between 2004 and 2007. With the population growing more rapidly than household formation, the average number of persons per household rose slightly from 2.59 people in 2007 to 2.63 in 2010.

The vast majority of interviews for the 2010 SCF were completed in 2010, but some were completed in early 2011. Thus, the survey data are largely unaffected by changes in economic activity since 2011—in particular, the rise in the market price of corporate equities, the relative stabilization of house prices, and the start of a decline in the unemployment rate.

Income

The change in real before-tax family income between 2007 and 2010 diverged sharply from the patterns seen in recent surveys.[4] Both median and mean income fell sharply, though the drop in the median (7.7 percent) was smaller than the drop in the mean (11.1 percent) (table 1).[5] Over the preceding three-year period, the median had been basically unchanged, and the mean had risen 8.5 percent. The changes for both periods stand in stark contrast to a pattern of substantial increases in both the median and the mean dating to the early 1990s.

Underlying the recent change was a shift in the composition of income between 2007 and 2010 (table 2). The share of family income attributable to realized capital gains fell from 6.7 percent in 2007 to only 0.9 percent in 2010; income from businesses, farms, and self-employment accounted for only 12.2 percent of income in 2010, down from 13.6 percent in 2007. Offsetting these declines in shares, the share of income from wages and salaries rose 3.6 percentage points; that of Social Security, pension, or other retirement income rose

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[4] To measure income, the interviewers request information on the family's cash income, before taxes, for the full calendar year preceding the survey. The components of income in the SCF are wages; self-employment and business income; taxable and tax-exempt interest; dividends; realized capital gains; food stamps and other, related support programs provided by government; pensions and withdrawals from retirement accounts; Social Security; alimony and other support payments; and miscellaneous sources of income for all members of the primary economic unit in the household.

[5] Over the 2007–10 period, estimates of inflation-adjusted household income for the previous year from the Current Population Survey (CPS) of the Census Bureau show a decrease in both the median (negative 2.2 percent) and the mean (negative 3.6 percent); both of these changes are smaller in absolute terms than the corresponding declines in the SCF. The medians for 2010 are similar in the SCF ($45,800) and the CPS ($50,600). Typically, the SCF shows a higher level of mean income than does the CPS; for 2010, the SCF yields an estimate of $78,500, while the CPS yields an estimate of $69,100. As discussed in more detail in the appendix, the two surveys differ in their definitions of the units of observation and in other aspects of their methodologies. Most relevant here is the fact that a CPS household can contain more people than a corresponding SCF family. If the SCF measure is expanded to include the income of household members not included in the SCF definition of a family, the median falls 5.6 percent over the period (from $51,700 in 2007 to $48,800 in 2010), and the mean falls 10.8 percent (from $90,800 in 2007 to $81,000 in 2010). The substantial difference in mean levels is likely the result of the truncation of large values in the CPS data above a certain amount, which is done with the intent of minimizing the possibility that participants in that survey might be identifiable.

Table 1. Before-tax family income, percentage of families that saved, and distribution of families, by selected characteristics of families, 2001–10 surveys

Thousands of 2010 dollars except as noted

Family characteristic	2001				2004			
	Income		Percentage of families that saved	Percentage of families	Income		Percentage of families that saved	Percentage of families
	Median	Mean			Median	Mean		
All families	**48.9**	**83.3**	**59.2**	**100.0**	**49.8**	**81.4**	**56.1**	**100.0**
	(1.0)	(2.4)			(1.0)	(1.4)		
Percentile of income								
Less than 20	12.6	12.3	30.0	20.0	12.8	12.4	34.0	20.0
20–39.9	29.9	29.6	53.4	20.0	29.5	30.0	43.3	20.0
40–59.9	48.9	49.4	61.3	20.0	49.8	50.0	54.5	20.0
60–79.9	79.4	79.9	72.0	20.0	78.5	79.6	69.3	20.0
80–89.9	120.9	120.2	74.9	10.0	120.5	122.6	77.8	10.0
90–100	207.8	371.0	84.3	10.0	212.7	347.7	80.6	10.0
Age of head (years)								
Less than 35	40.9	54.2	52.9	22.7	37.8	51.9	55.0	22.2
35–44	63.0	94.5	62.3	22.3	57.5	85.0	58.0	20.6
45–54	66.8	114.2	61.7	20.6	70.3	108.6	58.5	20.8
55–64	55.4	106.5	62.0	13.2	62.6	115.5	58.5	15.2
65–74	34.0	71.3	61.8	10.7	38.4	68.7	57.1	10.5
75 or more	27.4	45.0	55.5	10.4	27.3	47.1	45.7	10.7
Family structure								
Single with child(ren)	27.7	36.0	45.2	11.4	29.5	37.7	39.8	12.1
Single, no child, age less than 55	35.3	49.4	55.8	15.1	33.3	45.2	52.8	15.3
Single, no child, age 55 or more	20.8	39.9	49.5	13.2	24.5	39.2	45.9	14.6
Couple with child(ren)	76.5	115.0	61.9	31.1	75.6	113.9	61.7	31.7
Couple, no child	63.0	105.3	68.1	29.2	67.4	107.0	64.4	26.3
Education of head								
No high school diploma	20.8	30.8	38.7	16.0	22.3	29.8	35.9	14.4
High school diploma	41.6	54.9	56.7	31.7	41.1	51.5	54.0	30.6
Some college	50.1	68.0	61.7	18.3	47.3	64.5	51.0	18.4
College degree	83.1	142.9	70.0	34.0	84.4	135.3	68.3	36.6

Note: For questions on income, respondents were asked to base their answers on the calendar year preceding the interview. For questions on saving, respondents were asked to base their answers on the 12 months preceding the interview.

Percentage distributions may not sum to 100 because of rounding. Dollars have been converted to 2010 values with the current-methods consumer price index for all urban consumers (see the box "The Data Used in This Article"). See the appendix for details on standard errors (shown in parentheses below the first row of data for the means and medians here and in table 4) and for definitions of family and family head.

2.4 percentage points; and that of transfers or other income rose 1.3 percentage points. The share of income from interest or dividends was little changed. The decline in the share of capital gains was largest among the wealthiest 10 percent of families. As shown in the table, wage income tends to be a smaller factor for the highest wealth group.

Some patterns of income distribution hold generally across the years of SCF data shown in table 1.[6] Across age classes, median and mean incomes show a life-cycle pattern, rising to a peak in the middle age groups and then declining for groups that are older and increasingly

[6] Tabular information from the survey beyond that presented in this article is available at www.federalreserve.gov/econresdata/scf/scf_2010.htm. This information includes versions of all of the numbered tables in this article, for all of the surveys from 1989 to 2010 where the underlying information is available. Mean values for the demographic groups reported in this article are also provided. The estimates of the means, however, are more likely to be affected by sampling error than are the estimates of the medians. In addition, some alternative versions of the tables in this article are given. For those who wish to make further alternative calculations, this website provides a variety of data files as well as access to online tabulation software that may be used to create customized tables based on the variables analyzed in this article.

Table 1. Before-tax family income, percentage of families that saved, and distribution of families, by selected characteristics of families, 2001–10 surveys—*continued*
Thousands of 2010 dollars except as noted

Family characteristic	2001				2004			
	Income		Percentage of families that saved	Percentage of families	Income		Percentage of families that saved	Percentage of families
	Median	Mean			Median	Mean		
Race or ethnicity of respondent								
White non-Hispanic	55.4	94.3	63.1	75.4	56.9	92.9	60.1	72.2
Nonwhite or Hispanic	31.5	49.9	47.4	24.6	34.3	51.7	45.6	27.8
Current work status of head								
Working for someone else	57.9	82.5	61.6	60.9	56.7	80.7	59.2	60.1
Self-employed	77.6	169.5	70.4	11.7	76.8	162.9	68.7	11.8
Retired	25.7	49.0	50.5	23.0	28.1	49.7	44.0	23.7
Other not working	20.4	44.9	42.7	4.5	23.6	43.0	44.9	4.4
Current occupation of head								
Managerial or professional	87.2	153.4	72.4	27.1	88.9	147.6	67.7	28.3
Technical, sales, or services	44.1	65.3	58.2	23.7	43.1	61.1	55.4	22.1
Other occupation	50.4	60.0	56.6	21.8	52.0	58.3	57.3	21.6
Retired or other not working	25.4	48.3	49.2	27.4	27.4	48.7	44.1	28.1
Region								
Northeast	50.6	95.2	58.1	19.0	58.5	100.7	59.5	18.8
Midwest	53.8	79.3	63.0	23.0	52.0	77.7	59.9	22.9
South	44.1	75.2	57.3	36.2	42.5	71.3	52.5	36.3
West	49.9	90.7	59.5	21.8	53.2	85.8	55.2	22.0
Urbanicity								
Metropolitan statistical area (MSA)	50.4	88.7	59.7	86.2	53.2	88.5	56.9	82.9
Non-MSA	37.0	50.2	56.3	13.8	34.4	47.2	52.3	17.1
Housing status								
Owner	63.8	104.3	66.7	67.7	63.5	100.6	62.3	69.1
Renter or other	30.2	39.5	43.6	32.3	28.4	38.8	42.3	30.9
Percentile of net worth								
Less than 25	24.1	29.4	34.5	25.0	23.6	28.8	34.7	25.0
25–49.9	42.8	48.5	54.2	25.0	42.5	48.5	53.7	25.0
50–74.9	62.6	72.2	68.2	25.0	60.3	69.8	62.1	25.0
75–89.9	85.3	96.3	77.4	15.0	88.6	101.2	72.6	15.0
90–100	155.0	313.8	84.1	10.0	165.4	294.6	76.0	10.0

more likely to be retired. Couples (families in which the family head was either married or living with a partner) tend to have higher incomes than single persons, in part because couples have more potential wage earners. Income also shows a strong positive association with education; in particular, incomes for families headed by a person who has a college degree tend to be substantially higher than for those with any lesser amount of schooling. Incomes of white non-Hispanic families are substantially higher than those of other families.[7] Families headed by a self-employed worker consistently have the highest median and mean incomes of all work-status groups. Families headed by a person in a managerial or professional occupation have higher incomes than families in the three remaining occupation categories. Income is also higher for homeowners than for other families, and it is progressively higher for groups with greater net worth.[8] Across the four regions of the country as defined by the Census Bureau, the ordering of median incomes over time has varied, but

[7] See the appendix for a discussion of racial and ethnic identification in the SCF.

[8] In this article, a family is treated as a homeowner if at least one person in the family owns at least some part of the family's primary residence.

Table 1. Before-tax family income, percentage of families that saved, and distribution of families, by selected characteristics of families, 2001–10 surveys—*continued*
Thousands of 2010 dollars except as noted

Family characteristic	2007				2010			
	Income		Percentage of families that saved	Percentage of families	Income		Percentage of families that saved	Percentage of families
	Median	Mean			Median	Mean		
All families	**49.6**	**88.3**	**56.4**	**100.0**	**45.8**	**78.5**	**52.0**	**100.0**
	(.8)	(1.4)			(.6)	(1.2)		
Percentile of income								
Less than 20	12.9	12.9	33.7	20.0	13.4	12.9	32.3	20.0
20–39.9	30.1	29.7	45.0	20.0	28.1	27.9	43.4	20.0
40–59.9	49.6	49.5	57.8	20.0	45.8	46.3	49.8	20.0
60–79.9	78.7	80.2	66.8	20.0	71.7	73.6	60.1	20.0
80–89.9	119.5	121.6	72.9	10.0	112.8	114.6	67.7	10.0
90–100	216.8	416.6	84.8	10.0	205.3	349.0	80.9	10.0
Age of head (years)								
Less than 35	39.2	54.2	58.9	21.6	35.1	47.7	54.6	21.0
35–44	59.3	87.7	56.4	19.6	53.9	81.0	47.6	18.2
45–54	67.2	117.8	55.8	20.8	61.0	102.2	51.8	21.1
55–64	57.2	116.5	58.4	16.8	55.1	105.8	51.4	17.5
65–74	40.8	96.8	56.7	10.5	42.7	75.8	53.6	11.5
75 or more	23.9	47.9	49.4	10.6	29.1	46.1	54.1	10.7
Family structure								
Single with child(ren)	30.2	44.1	41.6	12.2	29.5	39.4	38.2	12.0
Single, no child, age less than 55	35.5	49.4	54.9	14.0	30.5	42.4	49.8	14.7
Single, no child, age 55 or more	25.8	38.4	48.5	14.9	24.2	39.6	45.4	15.2
Couple with child(ren)	74.6	118.4	60.1	31.8	67.7	109.4	52.8	31.6
Couple, no child	64.6	120.5	64.0	27.1	61.8	101.7	62.2	26.5
Education of head								
No high school diploma	23.2	32.8	41.6	13.5	23.0	33.7	36.9	12.0
High school diploma	38.5	53.6	51.1	32.9	36.6	48.1	47.4	32.2
Some college	47.8	71.3	53.6	18.4	42.9	58.7	49.5	18.6
College degree	81.9	150.7	68.6	35.3	73.8	128.9	62.0	37.3

the means generally show higher values for the Northeast and the West than for the Midwest and the South. Finally, families living in metropolitan statistical areas (MSAs), which are relatively urban areas, have higher median and mean incomes than those living in rural areas.[9]

Income by Demographic Category

Across the income distribution between 2007 and 2010, only the lowest quintile did not experience a substantial reduction in median income; the median for that group rose $500.[10] For other groups, the median decreased between 5.3 percent and 8.9 percent between 2007 and 2010. Similarly, for all income groups except the lowest quintile, the direction of changes in mean income was uniformly negative, with decreases ranging from a 5.8 percent drop for the second-highest decile to a 16.2 percent drop for the top decile. The disproportion between changes in median and mean incomes for the top decile (a 5.3 percent drop in the median, compared with a 16.2 percent decline in the mean) estab-

9 For the Office of Management and Budget's definition of MSAs, see www.whitehouse.gov/omb/bulletins/fy2008/b08-01.pdf.

10 Selected percentiles of the income distribution for the past four surveys are provided in the appendix, along with definitions of selected subgroups of the distribution.

Table 1. Before-tax family income, percentage of families that saved, and distribution of families, by selected characteristics of families, 2001–10 surveys—*continued*

Thousands of 2010 dollars except as noted

Family characteristic	2007				2010			
	Income		Percentage of families that saved	Percentage of families	Income		Percentage of families that saved	Percentage of families
	Median	Mean			Median	Mean		
Race or ethnicity of respondent								
White non-Hispanic	54.3	101.6	58.8	70.7	52.9	90.1	55.8	67.5
Nonwhite or Hispanic	38.6	56.2	50.8	29.3	34.6	54.4	44.0	32.5
Current work status of head								
Working for someone else	59.3	87.1	60.3	59.9	55.9	84.2	55.2	56.9
Self-employed	79.3	201.0	62.8	10.5	64.5	149.9	55.1	11.4
Retired	25.9	53.5	46.6	25.0	29.1	44.4	47.3	24.9
Other not working	21.3	37.1	45.3	4.6	23.9	36.3	37.0	6.8
Current occupation of head								
Managerial or professional	89.4	163.6	70.2	27.5	81.3	148.7	62.9	27.7
Technical, sales, or services	46.3	70.8	55.6	21.8	42.0	59.5	49.0	21.7
Other occupation	51.7	60.7	53.6	21.1	50.0	57.3	51.1	18.8
Retired or other not working	24.9	51.0	46.4	29.6	27.4	42.7	45.1	31.7
Region								
Northeast	53.9	105.2	53.5	18.3	53.7	99.2	50.8	18.3
Midwest	46.3	78.5	58.2	22.9	46.5	70.9	57.2	22.4
South	45.0	83.1	56.9	36.7	40.7	71.5	49.8	37.1
West	54.4	92.9	56.3	22.1	48.8	80.8	51.4	22.2
Urbanicity								
Metropolitan statistical area (MSA)	52.8	95.6	57.0	82.9	48.8	84.8	51.7	82.7
Non-MSA	37.8	52.6	54.0	17.1	36.7	48.2	53.3	17.3
Housing status								
Owner	64.6	110.7	60.9	68.6	59.6	98.3	56.5	67.3
Renter or other	29.1	39.3	46.7	31.4	26.1	37.9	42.7	32.7
Percentile of net worth								
Less than 25	24.6	30.5	40.5	25.0	23.7	32.6	32.2	25.0
25–49.9	43.1	48.7	52.8	25.0	37.9	45.5	48.4	25.0
50–74.9	59.5	69.8	59.1	25.0	54.9	63.3	56.8	25.0
75–89.9	86.2	97.4	68.9	15.0	74.5	89.0	66.9	15.0
90–100	165.5	364.2	80.4	10.0	163.2	297.9	76.1	10.0

lishes a theme that is repeated for income changes for many other groups considered in this article. Often, such a difference between the changes in a median and a mean is taken to indicate relative compression of higher values in the distribution.

The decline in mean incomes in the top decile between 2007 and 2010 stands in stark contrast to the generally steady pattern of rising mean incomes at the top of the income distribution over the past two decades. Indeed, the only other decreases in mean income observed for the top decile occurred in the periods 1989 to 1992 and 2001 to 2004, when the recovery from earlier recessions was affecting families broadly.

Every age group less than 55 saw decreases in median income of between 9.1 and 10.5 percent, while families headed by a person between 65 and 74 or 75 or more saw increases at the median. In contrast to the changes at the medians, the means fell for all age groups but especially for the 65-to-74 age group (a decline of 21.7 percent). In almost every age group, the decline in the mean was greater than the decline in the median.

Table 2. Amount of before-tax family income, distributed by income sources, by percentile of net worth, 2007 and 2010 surveys
Percent

Income source	Percentile of net worth					All families
	Less than 25	25–49.9	50–74.9	75–89.9	90–100	
2007 Survey of Consumer Finances						
Wages	79.9	80.0	77.7	72.3	46.2	64.5
Interest or dividends	.1	.3	.7	1.9	7.8	3.7
Business, farm, self-employment	1.8	5.3	6.9	7.9	24.7	13.6
Capital gains	.1	.4	1.3	2.9	14.4	6.7
Social Security or retirement	9.5	10.9	11.8	14.2	6.2	9.6
Transfers or other	8.6	3.2	1.6	.8	.7	1.9
Total	**100**	**100**	**100**	**100**	**100**	**100**
2010 Survey of Consumer Finances						
Wages	75.9	80.7	76.3	69.7	55.8	68.1
Interest or dividends	.1	.1	.4	1.6	8.7	3.6
Business, farm, self-employment	3.5	4.6	4.8	7.2	23.9	12.2
Capital gains	.1	.2	.1	–.2	2.3	.9
Social Security or retirement	9.4	9.6	15.9	20.1	7.8	12.0
Transfers or other	11.1	4.7	2.5	1.7	1.5	3.2
Total	**100**	**100**	**100**	**100**	**100**	**100**

By family structure, median incomes declined over the 2007–10 period for all groups, but most notably (negative 14.1 percent) for childless single families (those headed by a person who was neither married nor living with a partner) headed by a person aged less than 55; median income fell the least (2.3 percent) for single families with children. Mean income also fell for most types of families, except childless single families headed by a person aged 55 or older, for whom it rose 3.1 percent. Mean income of childless couples fell the most of all families, when grouped by family structure (15.6 percent).

In 2010, both median and mean incomes rose substantially with educational attainment, with incomes among the group holding a college degree being more than three times as high as among those with less than a high school diploma, and at least twice as high as among those with only a high school diploma. Between 2007 and 2010, however, the decreases in incomes were much larger for the higher education groups, and mean income actually rose for the no-high-school-diploma group (albeit from the much lower starting point). This pattern of change reversed the relatively faster growth of mean income for higher-educated families that had occurred between 2004 and 2007.

Over the 2007–10 period, the median income for white non-Hispanic families fell 2.6 percent, and the mean fell 11.3 percent. In contrast, the median for nonwhite or Hispanic families fell 10.4 percent, while the mean fell 3.2 percent. However, both the median and the mean values for nonwhites or Hispanics in both years were substantially lower than the corresponding figures for non-Hispanic whites. Since 1998, the total gain in median income for nonwhite or Hispanic families was 11.3 percent, whereas it was 3.9 percent for other families; the gain in the mean over this period was larger for both groups—22.8 percent for nonwhite or Hispanic families and 14.1 percent for other families.[11]

[11] As noted in the appendix, the questions underlying the definition of race or ethnicity changed incrementally in earlier surveys. When restrictions are placed on the definition of the variable for racial and ethnic classification used in the tables in the article to make the series more comparable over a longer period, the estimates change only slightly.

Median income fell 5.7 percent from 2007 to 2010 for families headed by a person who was working for someone else, but it fell much more (18.7 percent) for those who were self-employed; the median rose 12.4 percent for the retired group and 12.2 percent for the other-not-working group.[12] The mean over this period fell for all groups, especially for the self-employed group (a decrease of 25.4 percent) and the retired group (a decrease of 17.0 percent). Over the previous three years, median incomes had fallen for the retired and the other-not-working groups but had risen for the two worker groups.

Across occupation groups, median income fell most in proportional terms (9.3 percent) for families headed by a person working in a technical, sales, or service job. Although the percentage drop for families headed by a person in a managerial or professional position was only slightly smaller (9.1 percent), the dollar amount of their decline was much larger because their 2007 median income was much higher. For the other-occupation group, a group that predominantly comprises workers in traditional blue-collar occupations, the median fell only 3.3 percent. Consistent with evidence for age or current-work-status groups, median income for families headed by retirees increased 10.0 percent. In contrast, mean income decreased for all occupation groups, but especially for the technical, sales, or service occupation groups, for whom the mean fell 16.0 percent, and for the retired and other-not-working group, for whom the mean fell 16.3 percent.

By region, median family incomes in the Northeast and the Midwest were little changed between 2007 and 2010, while the medians in the West and the South decreased substantially. Those changes in medians stand in contrast to what occurred during the period from 2004 to 2007, when median incomes fell in the Northeast and Midwest but increased in the West and South. These income changes by region mirror the regional pattern of home price changes across the two time periods. During the final years of the housing boom, which disproportionately affected the West and South, median incomes were rising in those regions but falling elsewhere. During the subsequent housing bust, which also disproportionately affected those areas, median incomes were falling there but rising elsewhere. Mean incomes declined across all four regions between 2007 and 2010, though the changes were largest for the South and West.

In the recent three-year period, families living in an MSA saw a 7.6 percent decline in median income, while those living in other, less urbanized areas saw a decrease of 2.9 percent. Mean income also fell for both types of area—by 11.3 percent for families living in an MSA and by 8.4 percent for those living in other areas.

By housing status, median and mean incomes fell from 2007 to 2010 both for homeowners and for other families. The percentage decrease in median income for homeowners (7.7 percent) matched the percentage decrease in the overall family median reported earlier (7.7 percent), while the decrease for renter and other families (10.3 percent) was greater. Mean income declined for both groups, but particularly for homeowners—11.2 percent for homeowners, versus 3.6 percent for other families. As noted later in this article, homeownership continued the decline that began between the 2004 and 2007 surveys after rising for several years prior to that.[13]

[12] To be included in the retired group, the family head must report being retired and not currently working at any job or report being out of the labor force and over the age of 65. The other-not-working group comprises family heads who are unemployed and those who are out of the labor force but are neither retired nor over age 65; the composition of this group shifted slightly from 2007 to 2010 to include fewer families headed by a person who had a college degree, continuing a trend between 2004 and 2007. In 2010, 70.0 percent of the other-not-working group was unemployed, and the remainder was out of the labor force; in 2007, 66.6 percent of the group was unemployed (data not shown in the tables).

[13] See box 2, "Cross-Sectional Data and Changes in Group Composition over Time," for a discussion of the

Box 2. Cross-Sectional Data and Changes in Group Composition over Time

A cross-sectional survey of the sort discussed in this article describes the state of a sample of families at a given point in time. Thus, when comparison is made of changes for groups of people in families in such surveys over time, it is important to consider the degree to which interpretation of the data may be a function of changes in membership in those groups over time. Some classifications, such as ones based on race or ethnicity, may be fixed characteristics of individuals, but the overall populations of such groups may still change over time through births or deaths, through immigration or emigration, or in other ways. Some classifications, including those based on age, may change in a way that is mostly predictable. But other classifications—for example, ones based on economic characteristics such as income or wealth—may vary over time for substantial fractions of families.

Gathering data on the same set of families over time in a panel survey is an alternative way to understand changes for groups of families determined as of a baseline period. To address the effects on families of the period of financial turmoil between 2007 and 2009, the Federal Reserve undertook a survey in 2009 that was intended to re-interview the panel of families that had participated in the 2007 Survey of Consumer Finances (SCF) for which the family head or that person's spouse or partner was still alive and still living in the United States. This panel survey provides detailed information on changes in a wide variety of characteristics of families over this two-year period.[1] Although the panel survey can only be used to look at the first two years of the period covered by the cross-sectional surveys reported in detail in this article, it can provide a useful indication of the degree to which the movement of families across groups was important for the interpretation of the changes observed between the 2007 and 2010 cross-sectional SCFs.

Family income is one item for which variation over time might be expected, particularly over a period of severe recession. The panel data make it possible to track the movement of families across income groups between 2007 and 2009 (table A). The data show substantial movement across income groups during the two-year period.[2] For example, 69.4 percent of families with incomes in the bottom quintile of the distribution in 2009 also had incomes in the bottom quintile in 2007 (indicated by the bold font along the diagonal). The remaining fraction of families in the lowest income group in 2009 had experienced higher incomes in 2007; in 2007, 19.1 percent were in the second quintile group, 6.7 percent were in the third quintile group, 3.0 percent were in the fourth quintile group, and 1.9 percent were in the highest quintile group.

Table A. Movement of families across the income distribution between 2007 and 2009

Percentile of income in 2007	Percentile of income in 2009				
	Less than 20	20–39.9	40–59.9	60–79.9	80–100
Less than 20	**69.4**	22.0	5.4	2.1	1.1
20–39.9	19.1	**48.9**	23.5	6.5	2.0
40–59.9	6.7	21.4	**45.1**	22.9	4.0
60–79.9	3.0	6.5	22.4	**50.3**	17.8
80–100	1.9	1.2	3.5	18.3	**75.1**
All	100	100	100	100	100

Note: Figures in bold along the diagonal show the fraction of families in the given 2007 quintile group that were in the same quintile group in 2009.

The movements of families across income groups in two years was more substantial for the three central percentile groups than for families with incomes in the two extreme groups, in part because families in one of the extreme groups could move in only one direction. Among families in the second, third, and fourth income quintile groups in 2009, only about half had been in the same group in 2007. The income group with the highest persistence of membership across the two years was the top quintile; among families in 2009 whose income was high enough to be in the top quintile, 75.1 percent had also had incomes in the top quintile in 2007.

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potential effects of changes in the composition of groups on the interpretation of changes in median and mean values for the groups.

Box 2—*continued*

Tracking changes, such as these shifts in income, for a given population over time is interesting in its own right, but that information may also have important implications for interpreting changes in a given measure, including mean net worth, for groups defined using cross-sectional data. When there is a rearrangement of families across such groups over time and estimates for the groups are affected by that change in composition, the estimates are said to reflect "composition effects." In light of the large economic shifts in the overall economy during the time covered by the cross-sectional surveys discussed in this body of this article, movements of families across some categories may be particularly important.

One such example is the effect of changes in the composition of the lowest income decile from 2007 to 2009 on estimates of the group median of net worth for 2009. The panel data make it possible to decompose this effect directly, by looking at the 2009 medians of the members of this group, but with the families separated based on their 2007 income group (table B). The overall median net worth for the lowest income quintile in 2009 was $10,000. Among families in the lowest quintile group in 2009, those who were also in the group in 2007 had median net worth in 2009 of $4,500, those who were in the second quintile group in 2007 had median net worth in 2009 of $19,200, those who were in the third quintile group in 2007 had median net worth in 2009 of $32,000, and those in the two higher quintile groups in 2007 had progressively higher median net worth in 2009—up to $740,500 for the top quintile group. The second and third of these groups constituted over one-fourth of the lowest 2009 quintile group. The median net worth of families exiting the lowest income quintile between 2007 and 2009 was $13,300 (data not shown in the tables). The higher medians of the families entering this group between 2007 and 2009 helped push up the overall median net worth of the group for 2009.

Table B. Net worth of families in the lowest income quintile in 2009, sorted by their income ranking in 2007

Percentile of income in 2007	Median net worth
Less than 20	4,500
20–39.9	19,200
40–59.9	32,000
60–79.9	166,700
80–100	740,500
All	10,000

Of course, the 2007 income group in this example may also have incorporated composition effects relative to some other point of reference. If the movement of families across income groups over time took place according to a constant pattern, the 2007 and 2009 cross-sectional estimates might have comparable composition. Given the nature of the recession over this period and the evidence on unusual income presented in the body of the article, that possibility seems unlikely.

Composition effects may vary across categories, outcomes of interest, and time periods. For example, consider a very narrowly held asset or liability whose ownership is dominated by families whose income is *usually* relatively high, as tends to be the case for directly held stocks. The median value for directly held stocks in a given income quintile might be sensitive to the fraction of families in that income quintile whose *usual* income was different from their current income. If, as in the 2009 panel interview, there was a substantial fraction of families in the lowest quintile group whose income was *usually* much higher, those families might bring with them ownership rates and values for stock holdings that were generally higher than those for families whose incomes are *usually* low. The 2010 SCF cross-sectional data indicate that ownership rates or median values for some narrowly held financial assets for lower-income families seem to have risen between 2007 and 2010. In light of the available evidence, a more likely explanation seems to be that some such changes in ownership or median values were substantially affected by the sorts of compositional effects described here.

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Box 2—*continued*

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[1] See Jesse Bricker, Brian Bucks, Arthur Kennickell, Traci Mach, and Kevin Moore (2011), "Surveying the Aftermath of the Storm: Changes in Family Finances from 2007 to 2009," Finance and Economics Discussion Series 2011-17 (Washington: Board of Governors of the Federal Reserve System, March), www.federalreserve.gov/pubs/feds/2011/201117/201117pap.pdf; and Arthur B. Kennickell (2012), "Tossed and Turned: Wealth Dynamics of U.S. Households 2007–2009," Finance and Economics Discussion Series 2011-51 (Washington: Board of Governors of the Federal Reserve System, January; paper dated November 7, 2011), www.federalreserve.gov/pubs/feds/2011/201151/201151pap.pdf.

[2] The table shows equal-sized percentile groups, the highest of which comprises two percentile groups used in the analysis presented in the article. Of the families with incomes in the 80th-to-90th percentiles of the distribution in 2009, 49.0 percent were in the same group in 2007, 38.3 percent were in one of the bottom four groups shown in the table, and 12.6 percent had incomes between the 90th and 100th percentiles. Of the families with incomes in the 90th-to-100th percentiles of the distribution in 2009, 71.4 percent were in the same group in 2007, 11.4 percent were in one of the bottom four groups shown in the table, and 17.2 percent had incomes between the 80th and 90th percentiles.

By percentile of net worth, median income fell for every group, with the smallest decline occurring for the top 10 percent of wealth holders, for whom income fell 1.4 percent. The decline in median income was also relatively small for the lowest quartile, for which the median fell 3.7 percent; the median declined most for the middle income groups (12.1 percent for the second quartile, 7.7 percent for the third quartile, and 13.6 percent for the group between the 75th and 90th percentiles).[14] The pattern of changes in the mean by net worth group was somewhat different, with mean income in the bottom quartile rising 6.9 percent and the mean income in the top decile falling 18.2 percent. This differential pattern may be attributable in part to composition effects. For example, some families with incomes sufficient to support a relatively large home mortgage may have lost enough of their home equity over the three-year period for them to have been pushed into the lowest wealth group, where their incomes would be relatively large.

Income Variability

For a given family, income at a particular time may not be indicative of its "usual" income. Unemployment, a bonus, a capital loss or gain, or other factors may cause income to deviate temporarily from the usual amount. Although the SCF is normally a cross-sectional survey, it does provide some information on income variability. In 2010, 25.3 percent of families reported that their income for the preceding year was unusually low, whereas only 14.4 percent of families had reported unusually low income in 2007. In contrast, only 6.0 percent of families reported that their income was unusually high, down from 9.2 percent in 2007 (data not shown in the tables). For those reporting unusual income in either direction, the median deviation of actual income from the usual amount was negative 27.4 percent of the normal level; the same statistic was negative 22.0 percent in 2007.

Although a family's income may vary, such variability may be a well-recognized part of its financial planning. The SCF data over the recent three-year period show some increase in the families' uncertainty about their future income. In 2010, 35.1 percent of families reported that they did not have a good idea of what their income would be for the next year, and 29.0 percent reported that they do not usually have a good idea of their next year's income. The corresponding figures for 2007 were lower, at 31.4 percent and 27.2 percent, respectively.

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[14] Selected percentiles of the distribution of net worth for the past four surveys are provided in the appendix.

Saving

Because saving out of current income is an important determinant of family net worth, the SCF asks respondents whether, over the preceding year, the family's spending was less than, more than, or about equal to its income. Though only qualitative, the answers are a useful indicator of whether families are saving. Asking instead for a specific dollar amount would require much more time from respondents and would likely lower the rate of response to the survey.

Overall, from 2007 to 2010, the proportion of families that reported that they had saved in the preceding year fell substantially, from 56.4 percent to 52.0 percent. That decrease pushed the fraction of families reporting saving to the lowest level since the SCF began collecting such information in 1992. The general pattern of changes across demographic groups in the recent three-year period is also one of decline, as retirees were the only group reporting an increase in the fraction that saved.

Estimates of the personal saving rate from the national income and product accounts (NIPA) show an annual saving rate of 5.3 percent between 2008 and 2010, up substantially from the 2.2 percent rate over the 2005–07 period. This divergence in trend arose in part because the SCF and NIPA concepts of saving differ in some important ways. First, the underlying SCF question asks only whether the family's spending has been less than, more than, or about the same as its income over the past year. Thus, while the fraction of families saving may be smaller, those who are doing so may be saving a relatively large amount; those who are spending more than their incomes may be spending a relatively small amount. Second, the NIPA measure of saving relies on definitions of income and consumption that may not be the same as those that respondents had in mind when answering the survey questions. For example, the NIPA measure of personal income includes payments employers make to their employees' defined-benefit pension plans but not the payments made from such plans to families, whereas the SCF measure includes only the latter. The SCF measure also includes realized capital gains, whereas the NIPA measure excludes such gains.

A separate question in the survey asks about families' more typical saving habits. In 2010, 6.0 percent of families reported that their spending usually exceeds their income; 19.6 percent reported that the two are usually about the same; 34.8 percent reported that they typically save income "left over" at the end of the year, income of one family member, or "unusual" additional income; and 39.6 percent reported that they save regularly (data not shown in the tables). These estimates show a small decrease between 2007 and 2010 in the share of families who reported regular saving, but in general, the fact that these figures are not much changed over the past several surveys suggests that economic conditions over this period had only modest effects on the longer-run saving plans of families.

The SCF also collects information on families' most important motivations for saving (table 3).[15] In 2010, the most frequently reported motive was liquidity related (35.2 percent of families), a response that is generally taken to be indicative of saving for precautionary reasons, and the next most frequently reported response was retirement related (30.1 percent of families).[16] At least since 1998, these two responses have been most frequently reported, but saving for retirement was marginally more likely to be reported than saving

[15] Although families were asked to report their motives for saving regardless of whether they were currently saving, some families reported only that they do not save. The analysis here is confined to the first reason reported by families.

[16] Liquidity-related reasons include "emergencies," the possibilities of unemployment and illness, and the need for ready money.

Table 3. Reasons respondents gave as most important for their families' saving, distributed by type of reason, 2001–10 surveys
Percent

Type of reason	2001	2004	2007	2010
Education	10.9	11.6	8.4	8.2
For the family	5.1	4.7	5.5	5.7
Buying own home	4.2	5.0	4.2	3.2
Purchases	9.5	7.7	10.0	11.5
Retirement	32.1	34.7	34.0	30.1
Liquidity	31.2	30.0	32.0	35.2
Investments	1.0	1.5	1.6	1.2
No particular reason	1.1	.7	1.1	1.4
When asked for a reason, reported do not save	4.9	4.0	3.3	3.5
Total	100	100	100	100

Note: See note to table 1 and text note 15.

for liquidity, until the 2010 survey. Education-related motives also appear to be important, but less so than in 2007; in 2010, 8.2 percent of families reported it as their primary motive, down only slightly from 2007 but down 3.4 percentage points since 2004. The frequency of reporting saving for purchases rose 1.5 percentage points from 2007 to 2010 to a level 3.8 percentage points above that in 2004.

The survey asks families to estimate the amount of savings they need for emergencies and other unexpected contingencies, a measure of desired savings for precautionary purposes.[17] The desired amount increases with income, but as shown by the following table, the amount is a similar percentage of usual income across levels of such income:

Table 3.1

Family characteristic	Median of desired precautionary saving (2010 dollars)	Median of ratio of desired amount to usual income (percent)
All families	**5,000**	**10.8**
Percentile of usual income		
Less than 20	2,000	14.1
20–39.9	4,000	12.3
40–59.9	5,000	9.8
60–79.9	10,000	10.2
80–89.9	10,000	8.9
90–100	30,000	12.1

Overall, the amount of such desired savings was little changed from 2007, but it rose overall and for most income groups as a percentage of usual income, largely because usual income fell over the recent three-year period (data not shown in the tables).

Net Worth

From 2007 to 2010, inflation-adjusted net worth (wealth)—the difference between families' gross assets and their liabilities—fell dramatically in terms of both the median and the

[17] For an extended analysis of desired precautionary savings as measured in the SCF, see Arthur B. Kennickell and Annamaria Lusardi (2004), "Disentangling the Importance of the Precautionary Saving Motive," NBER Working Paper Series 10888 (Cambridge, Mass.: National Bureau of Economic Research, November).

Table 4. Family net worth, by selected characteristics of families, 2001–10 surveys
Thousands of 2010 dollars

Family characteristic	2001		2004		2007		2010	
	Median	Mean	Median	Mean	Median	Mean	Median	Mean
All families	**106.1**	**487.0**	**107.2**	**517.1**	**126.4**	**584.6**	**77.3**	**498.8**
	(3.7)	(8.2)	(4.9)	(11.2)	(5.7)	(9.7)	(2.8)	(12.7)
Percentile of income								
Less than 20	9.6	64.7	8.6	83.6	8.5	110.3	6.2	116.8
20–39.9	45.9	141.2	38.8	139.8	39.6	141.3	25.6	127.9
40–59.9	78.0	199.4	82.8	224.0	92.3	220.6	65.9	199.0
60–79.9	176.8	360.7	184.0	392.9	215.7	393.9	128.6	293.9
80–89.9	322.4	560.3	360.9	563.7	373.2	638.1	286.6	567.2
90–100	1,021.5	2,777.1	1,069.7	2,925.2	1,172.3	3,474.7	1,194.3	2,944.1
Age of head (years)								
Less than 35	14.3	111.2	16.3	84.6	12.4	111.1	9.3	65.3
35–44	95.1	318.6	79.9	345.2	92.4	341.9	42.1	217.4
45–54	164.9	595.9	167.1	625.8	193.7	694.6	117.9	573.1
55–64	227.2	898.6	290.0	976.4	266.2	986.7	179.4	880.5
65–74	217.8	831.4	218.8	795.1	250.8	1,064.1	206.7	848.3
75 or more	190.3	574.8	187.7	607.7	223.7	668.8	216.8	677.8
Family structure								
Single with child(ren)	16.2	117.4	24.0	149.9	24.4	187.4	15.5	143.7
Single, no child, age less than 55	24.0	185.5	24.2	179.8	26.3	217.2	14.6	117.5
Single, no child, age 55 or more	111.9	355.8	134.0	405.8	150.7	408.9	102.0	391.6
Couple with child(ren)	139.3	540.1	140.6	580.5	147.5	629.1	86.7	555.7
Couple, no child	217.1	790.1	240.2	868.2	236.2	998.6	205.7	864.8
Education of head								
No high school diploma	31.3	127.5	23.7	157.1	34.8	149.7	16.1	110.7
High school diploma	71.1	222.0	79.1	227.2	84.3	263.8	56.7	218.1
Some college	89.8	352.1	79.8	355.7	88.8	384.5	50.9	272.2
College degree	262.2	976.6	260.2	982.3	298.6	1,154.5	195.2	977.7
Race or ethnicity of respondent								
White non-Hispanic	150.4	599.0	162.2	648.3	179.4	727.4	130.6	654.5
Nonwhite or Hispanic	22.0	144.1	28.5	176.2	29.7	240.3	20.4	175.9

Note: See note to table 1.

mean (table 4). The median fell 38.8 percent, and the mean fell 14.7 percent. The two preceding surveys showed substantial increases in both median and mean net worth. The corresponding values for the period from 2004 to 2007 were increases of 17.9 percent and 13.1 percent. And, for the period 2001 to 2004, there were smaller increases (1.0 percent and 6.2 percent). Mean net worth fell to about the level in the 2001 survey, and median net worth was close to levels not seen since the 1992 survey (data not shown in the tables). Although the overall measures of change in wealth from the 2007 and 2010 cross-sectional surveys are negative, evidence from the 2007–09 SCF panel survey suggests that there was substantial heterogeneity in wealth changes across families; in that panel, families variously showed large gains in wealth as well as losses, though there was a preponderance of losses.[18]

Movements in the dollar value of families' net worth are, by definition, a result of changes in investment, valuation, and patterns of ownership of financial assets (tables 5, 6, and 7) and nonfinancial assets (tables 8, 9, and 10), as well as decisions about acquiring or paying down debt (tables 11 through 17). A variety of financial decisions underlie these

[18] See Bricker, Bucks, Kennickell, Mach, and Moore, "Surveying the Aftermath of the Storm."

Table 4. Family net worth, by selected characteristics of families, 2001–10 surveys—*continued*
Thousands of 2010 dollars

Family characteristic	2001		2004		2007		2010	
	Median	Mean	Median	Mean	Median	Mean	Median	Mean
Current work status of head								
Working for someone else	79.7	276.9	77.4	310.7	98.5	369.1	55.2	298.8
Self-employed	431.7	1,546.5	402.2	1,639.9	407.3	2,057.4	285.6	1,743.6
Retired	141.0	556.4	160.9	539.8	169.9	569.1	151.1	485.3
Other not working	9.4	218.4	13.6	186.7	6.0	130.1	11.9	137.5
Current occupation of head								
Managerial or professional	242.1	942.4	227.3	995.6	258.8	1,174.8	167.3	1,047.0
Technical, sales, or services	57.3	244.7	51.7	284.8	77.0	325.8	32.6	219.1
Other occupation	58.9	167.1	65.0	169.8	68.4	201.3	46.6	162.8
Retired or other not working	118.2	501.4	127.9	485.0	135.6	500.6	93.5	410.4
Region								
Northeast	114.3	556.3	186.1	655.0	167.1	684.6	119.9	615.2
Midwest	130.3	418.3	132.4	503.8	112.7	491.2	68.4	399.8
South	90.4	461.4	73.4	401.0	102.0	525.9	68.3	440.8
West	109.0	541.8	109.3	605.3	164.1	695.4	73.4	599.9
Urbanicity								
Metropolitan statistical area (MSA)	108.0	525.0	120.1	582.0	138.8	652.6	78.4	553.6
Non-MSA	98.0	250.1	68.2	203.5	82.0	253.9	74.5	236.1
Housing status								
Owner	211.5	687.2	212.6	720.9	246.0	817.6	174.5	713.4
Renter or other	5.9	67.7	4.6	62.3	5.4	74.7	5.1	57.2
Percentile of net worth								
Less than 25	1.4	.1	2.0	–1.6	1.3	–2.3	†	–12.8
25–49.9	50.1	54.4	50.2	54.2	56.8	60.9	32.2	35.6
50–74.9	193.6	204.9	196.7	213.7	230.8	238.6	157.2	168.9
75–89.9	528.0	553.5	586.7	608.4	601.2	616.7	482.7	527.9
90–100	1,602.6	3,390.0	1,645.5	3,591.1	1,991.9	4,176.9	1,864.1	3,716.5

† Less than 0.05 ($50).

changes. Box 3, "Shopping for Financial Services," provides a discussion of the intensity of families' decisionmaking efforts and their sources of financial information.

By age group, median and mean values of family net worth generally increase with age, though there are some signs of decrease among older age groups. This pattern reflects both life-cycle saving behavior and a historical pattern of long-run growth in inflation-adjusted wages. The median and mean values of wealth rise in tandem with income, a relationship reflecting both income earned from assets and a higher likelihood of substantial saving among higher-income families. Wealth shows strong differentials across groups defined in terms of family structure, education, racial or ethnic background, work status, occupation, housing status, and the urbanicity and region of residence; these differentials generally mirror those for income, but the wealth differences tend to be larger.

Net Worth by Demographic Category

Analysis by demographic group for the 2007–10 period shows a pattern of substantial losses in median and mean net worth for most groups, but a small number of groups experienced gains. Most groups saw declines in the median that far exceeded declines in the mean.

Box 3. Shopping for Financial Services

As a normal part of their financial lives, families must make a variety of decisions to select particular investments for any savings they may have, as well as to select the forms and terms of credit they may use. To the extent that families devote more or less attention to such activities or that they are better or worse informed, the wealth of otherwise comparable families may differ substantially over time.

The Survey of Consumer Finances (SCF) contains a self-assessment of families' intensity of shopping for borrowing or investing services. In 2010, 53.0 percent of families reported that they undertake a moderate amount of shopping for borrowing, and 54.7 percent reported that they undertake a moderate amount of shopping for investing (table A).[1] Only 26.2 percent of families reported shopping a great deal for loan terms, and only 23.3 percent reported shopping a great deal for the best terms on investments. These figures are little changed from 2007 (data not shown in the tables). Even though the survey questions are intended to elicit a description of behavior in general, the behavior reported could still be more reflective of the short-term needs for such services and consequently the immediate need for shopping. When broken out by categories of net worth, the patterns in 2010 are similar for all groups for loan shopping (data not shown in the tables). For investment shopping, the data show a more pronounced gradient toward more-intensive shopping by families with higher levels of wealth.

Table A. Intensity of shopping for borrowing or investing, 2010

Percent

Intensity of shopping	Type of service	
	Borrowing	Investing
Almost none	20.8	21.9
Moderate amount	53.0	54.7
A great deal	26.2	23.3

More families turn to friends, family members, or associates for financial information than to any other source of information on borrowing or investing (table B). This result suggests that there may be important feedback effects in financial outcomes; that is, families who know relatively well-informed people may obtain better services. Sellers of financial services—bankers, brokers, and so on—and the Internet are either the second or third most frequently cited sources of information for borrowing or investing. The Internet was reported by 41.7 percent of families as a source of information on borrowing and by 33.0 percent as a source of information on investing. When viewed across categories of net worth, the data show similar patterns of use of sources of information by all groups (data not shown in the tables).

Table B. Information used for decisions about borrowing or investing, 2010

Percent

Source	Type of service	
	Borrowing	Investing
Calling around	27.0	15.7
Magazines, newspapers, and other media	14.5	14.4
Material in the mail	28.3	19.0
Internet	41.7	33.0
Friends, relatives, associates	43.9	40.8
Bankers, brokers, and other sellers of financial services	39.5	39.1
Lawyers, accountants, and other financial advisors	19.5	31.1
Does not borrow or invest	14.6	11.7

Note: Figures sum to more than 100 because of reporting of multiple sources.

In addition to serving as a source of information, the Internet can also be a medium for obtaining financial services. In 2010, 58.5 percent of families reported using the Internet to

continued on next page

Box 3—*continued*

access at least some type of service at one of the financial institutions they used (data not shown in the tables). If accessing information and using services are combined, the Internet played a part in the financial life of 67.4 percent of all families (table C). This figure is up sharply from 59.7 percent in 2007 and 46.5 percent in 2004 (data not shown in the tables). The proportion of such users rises strongly over net worth groups: Among the least wealthy 25 percent of families, 60.3 percent made such use of the Internet, whereas the figure was 84.4 percent for the wealthiest 10 percent (data not shown in the tables). More striking is the variation over age groups. Among families headed by a person younger than age 35, 80.0 percent reported using the Internet for financial information or services, whereas the figure for families with a head aged 75 or older was only 25.8 percent. These figures are both up substantially from their respective values in 2007—71.9 percent and 16.4 percent (data not shown in tables). If the relatively greater expression of such behavior by younger families persists as they age, and if succeeding cohorts follow their example, Internet-based financial services may become even more important in the future.[2]

Table C. Use of the Internet for financial information or financial services, by age of head, 2010

Percent

Family characteristic	Percentage of families
All families	**67.4**
Age of head (years)	
Less than 35	80.0
35–44	77.2
45–54	74.6
55–64	69.0
65–74	51.7
75 or more	25.8

[1] The underlying question allows the survey respondent to shade the intermediate response toward a greater or lesser amount of shopping. About one-third of the respondents choose to do so, and of those, somewhat more than one-half shaded their response toward a greater degree of shopping.

[2] For a discussion of the definition of local banking markets, see Dean F. Amel, Arthur B. Kennickell, and Kevin B. Moore (2008), "Banking Market Definition: Evidence from the Survey of Consumer Finances," Finance and Economics Discussion Series 2008-35 (Washington: Board of Governors of the Federal Reserve System, August; paper dated July 7), www.federalreserve.gov/pubs/feds/2008/200835/200835pap.pdf.

Median net worth fell for all percentile groups of the distribution of net worth, with the largest decreases in proportional terms being for the groups below the 75th percentile of the net worth distribution. From 2007 to 2010, the median for the lowest quartile of net worth fell from $1,300 to zero—a 100 percent decline; at the same time, the mean for the group fell from negative $2,300 to negative $12,800. For the second and third quartiles, the median and mean declines in net worth were smaller but still sizable; for example, median net worth for the second quartile fell 43.3 percent. Median and mean net worth did not fall quite as much for the higher net worth groups. For the 75th-to-90th percentile group, the median fell 19.7 percent while the mean fell 14.4 percent. For the wealthiest decile, the 11.0 percent decline in the mean exceeded the 6.4 percent decline in the median for that group; as was discussed earlier in the case of family income, this pattern of the changes in the median and mean suggests that there was some compression of higher values in the wealth distribution.

Over the recent three-year period, median net worth decreased for all income groups except the top decile, for which it was basically unchanged; mean net worth fell substantially for all of the groups except the lowest quintile, for which mean wealth rose 5.9 percent. The broad middle of the income distribution (the groups between the 20th and 90th percentiles) saw consistently large drops in median net worth between 2007 and 2010, with much smaller drops in mean net worth within those income groups. In contrast to the stability of the

median for the top decile, the mean for that group was down 15.3 percent over the recent three-year period.

The opposing pattern of a 27.1 percent decline in median net worth for the lowest income quintile and a 5.9 percent increase in the mean for the group differs from the patterns seen for the other groups. To some extent, this finding reflects composition effects. Box 2, “Cross-Sectional Data and Changes in Group Composition over Time” provides an example of how income-related composition affects median net worth across income groups.

The survey shows substantial declines in median and mean net worth by age group between 2007 and 2010, with the exception that mean net worth rose modestly (1.3 percent) for the 75-or-more age group. The 35-to-44 age group saw a 54.4 percent decline in median net worth during the most recent three-year period, and the mean for that age group fell 36.4 percent. The wealth decreases for the less-than-35 age group were also large; the median fell 25.0 percent while the mean fell 41.2 percent. The declines in median and mean net worth for middle-aged families (the 45-to-54 and 55-to-64 age groups) were also large.

By family structure, single families headed by a person younger than 55 with no children and couples with children (who also tend to be relatively young) had the largest drops in wealth from 2007 to 2010 in median net worth—declines of 44.5 percent and 41.2 percent, respectively. Single families with children and families headed by a single person who was aged 55 or older and without children also experienced large decreases in median net worth—36.5 percent and 32.3 percent, respectively. Mean net worth fell for all family structure groups as well, though the extent of the decreases ranged from 4.2 percent (childless families headed by a single person aged 55 or older) to 45.9 percent (other childless families headed by a single person).

From 2007 to 2010, median and mean net worth decreased for all education groups. Mirroring the pattern for all families, each of the four education groups experienced a very large decline in the median (ranging from a drop of 53.7 percent for the no-high-school-diploma group to a drop of 32.7 percent for the high-school-educated group) and smaller declines in the mean (ranging from 29.2 percent for the some-college group to a drop of 15.3 percent for the college-educated group). The patterns of changes in medians and means across education groups are similar to those for the income groups, largely because income and education are strongly correlated.

The data show losses from 2007 to 2010 in median and mean wealth for both categories of race or ethnicity. Declines in the median were roughly the same for white non-Hispanic families (27.2 percent) and for nonwhite or Hispanic families (31.3 percent).[19]

However, the decline in the mean was much smaller for white non-Hispanic families—10.0 percent—than the decline for nonwhite or Hispanic families—26.8 percent. Among nonwhite or Hispanic families, the subgroup of African American families saw a decline of 13.3 percent in their median net worth from 2007 ($17,900) to 2010 ($15,500), and their mean net worth fell 30.4 percent, from $140,800 to $98,000; over the 2004–07 period, the median for the group had fallen 23.9 percent, while the mean had risen 10.6 percent (data not shown in the tables).

[19] If the additional information on Hispanic or Latino ethnic identification available in the SCF is used in the classification of the 2010 results, the median net worth of nonwhites or Hispanics was $22,200, and the mean was $183,600; for other families, the median was $131,900, and the mean was $658,500. These figures are all slightly higher than the corresponding values reported in table 4 for the larger group of nonwhite or Hispanic families.

From 2007 to 2010, median and mean net worth fell among all work-status groups except one. The exception was families headed by persons who were not working, for reasons other than retirement (the other-not-working group), which showed increases in both measures (albeit from relatively low starting points); in both years, the group had the lowest levels of both median and mean net worth of all work-status groups. The dollar amounts of decreases in median and mean net worth for the self-employed group were far larger than those for the other groups that experienced losses over the period; in percentage terms, however, the decreases for this group in both median and mean wealth were well below the rates of decline for families headed by a person working for someone else.

Median and mean net worth decreased for all occupation groups in the recent three-year period, but they did so most markedly for families headed by a worker in a technical, sales, or service occupation, for whom median net worth fell 57.7 percent and mean net worth fell 32.8 percent. Wealth losses were substantial for every other occupation group as well, however, with median declines ranging from 35.4 percent (managerial and professional group) to 31.0 percent (retired group), and mean declines ranging from 19.1 (other-occupation group) to 10.9 percent (managerial and professional group).

Between 2007 and 2010, median net worth fell dramatically for families living in all regions of the country, but especially for those living in the West—a 55.3 percent decline. This pattern reflects the effect of the collapse of housing values in several parts of the West region. Median wealth in every other region fell 28.2 percent or more. As with the overall population and most other demographic groups discussed earlier, the decline in mean net worth within every region was smaller than the drop in the median. In the South and Midwest regions, the percentage decline in the median was about twice as large as the percentage decline in the mean, but in percentage terms, the median for the West fell four times as much as the mean.

By urbanicity of the place of residence, in the recent three-year period, median net worth fell much more dramatically in MSA areas than in non-MSA areas, but the declines in the means were more similar. The decline in median net worth in MSA areas was large enough to erase most of the widening gap that had developed since 1998, in large part due to a run-up in house values. Mean net worth remained much higher in MSA areas than in non-MSA areas in 2010.

As might be expected from the previous discussion on the role of the decline in housing values in explaining median and mean wealth losses across various demographic groups, there are large differences in net worth changes by housing status. Median net worth for homeowners fell 29.1 percent between 2007 and 2010, while the mean fell 12.7 percent. The decline in median net worth for non-homeowners (hereafter, renters) was only 5.6 percent, though the decline in the mean was much larger at 23.4 percent. Renters have much lower median and mean net worth than homeowners in any survey year, so the dollar value of wealth losses for the renter group tended to be much smaller; for example, the median net worth of renters fell $300 over the three-year period, in contrast with $71,500 for homeowners.

Assets

At 97.4 percent in 2010, the overall proportion of families with any asset was barely changed from 2007 (first half of tables 9.A and 9.B, last column). Overall, this figure has declined 0.3 percentage point since 2007 (data not shown in the tables). Across demographic groups, the pattern of changes in the recent three-year period is mostly one of small increases or decreases. Noticeable exceptions are declines for the following groups:

the second quintile of the income distribution (0.9 percentage point), families headed by a person aged less than 35 (1.6 percentage points) or between 65 and 74 (1.3 percentage points), families headed by a person with a high school diploma (1.2 percentage points), and families in the bottom quartile of the net worth distribution (1.2 percentage points). For many groups, the figure remained at or near 100 percent.

From 2007 to 2010, median assets for families having any assets fell 19.3 percent, from $232,100 to $187,200 (second half of tables 9.A and 9.B, last column), and the mean fell 12.8 percent, from $702,100 to $612,300 (memo line). The percentage change in median assets between 2007 and 2010 is only about half the percentage change in median net worth reported in table 4, in part for reasons related to housing. Because houses are frequently mortgaged, net equity in homes tends to be smaller than the asset value of the home itself; consequently, a given change in housing values will tend to have an amplified proportional effect on net worth changes relative to the change in value as a proportion of gross assets.

Across net worth groups, the percentage changes in median assets and net worth were most similar for families in the highest or lowest quartiles of the distribution of net worth. For the wealthier groups, housing tends to be a smaller share of net worth, and it is less likely to be mortgages than is the case for the middle wealth groups. For the least wealthy group, homeownership is much less common than for other groups. The divergence between fluctuations in median asset change and median net worth change is largest for the middle two quartiles, whose net worth tends to be dominated by housing. A similar effect shows up across income groups, as middle-income families experienced smaller declines in median assets than in median net worth, in part because they are more likely to be leveraged homeowners whose assets are dominated by housing. Across other demographic groups such as age, race or ethnicity, and education, the percentage declines in median assets are generally about half the percentage decline in median net worth. Not unexpectedly, such divergence of changes in wealth and assets was largest for homeowners, whose median assets fell 18.0 percent, well below their decline in median net worth of 29.1 percent; for renters, in contrast, median assets fell 11.3 percent, which is greater than their 5.6 percent decline in median net worth.

Financial Assets

Although median and mean financial assets declined from 2007 to 2010, financial assets as a share of total assets rose 3.9 percentage points to 37.9 percent (table 5, memo line); this movement reverses a decline in this share from a level in 2001 that marked the high point observed in the survey since at least 1989. The share of financial assets in total assets had fallen 8.2 percentage points between 2001 and 2007. The relative shares of various financial assets also shifted. The decline in the percentage share of directly held stock was mostly offset by increases in the shares of transaction and retirement accounts.[20] The share of financial assets held in retirement accounts has nearly doubled since 1989, and as of 2010, it stood at 38.1 percent of families' financial assets (data not shown in the tables).

Across the groups considered, the 94.0 percent rate of ownership of any financial asset in 2010 was almost unchanged over the recent three-year period (first half of tables 6.A and 6.B, last column). Changes in ownership rates were also generally small across demographic groups, though there are a few exceptions. By age, families in the less-than-35 group saw a 2.1 percentage point increase in their financial asset ownership rate, while those in the 55-to-64 group saw a 2.0 percentage point decline; by family structure, owner-

[20] The definitions of asset categories in table 5 are given later in the article, in the sections of text devoted to those categories.

Table 5. Value of financial assets of all families, distributed by type of asset, 2001–10 surveys
Percent

Type of financial asset	2001	2004	2007	2010
Transaction accounts	11.4	13.1	10.9	13.3
Certificates of deposit	3.1	3.7	4.0	3.9
Savings bonds	.7	.5	.4	.3
Bonds	4.5	5.3	4.1	4.4
Stocks	21.5	17.5	17.8	14.0
Pooled investment funds (excluding money market funds)	12.1	14.6	15.8	15.0
Retirement accounts	29.0	32.4	35.1	38.1
Cash value life insurance	5.3	2.9	3.2	2.5
Other managed assets	10.5	7.9	6.5	6.2
Other	1.9	2.1	2.1	2.3
Total	**100**	**100**	**100**	**100**
MEMO				
Financial assets as a share of total assets	42.2	35.8	34.0	37.9

Note: For this and following tables, see text for definition of asset categories. Also see note to table 1.

Table 6. Family holdings of financial assets, by selected characteristics of families and type of asset, 2007 and 2010 surveys
A. 2007 Survey of Consumer Finances

Family characteristic	Transaction accounts	Certificates of deposit	Savings bonds	Bonds	Stocks	Pooled investment funds	Retirement accounts	Cash value life insurance	Other managed assets	Other	Any financial asset
Percentage of families holding asset											
All families	**92.1**	**16.1**	**14.9**	**1.6**	**17.9**	**11.4**	**53.0**	**23.0**	**5.8**	**9.3**	**93.9**
Percentile of income											
Less than 20	74.9	9.4	3.6	*	5.5	3.4	10.8	12.8	2.7	6.6	79.1
20–39.9	90.1	12.7	8.4	*	7.8	4.6	35.8	16.4	4.7	8.7	93.2
40–59.9	96.3	15.5	15.2	*	14.0	7.1	55.6	21.6	5.4	10.2	97.2
60–79.9	99.3	19.3	20.9	1.4	23.2	14.6	74.3	29.4	5.7	8.4	99.7
80–89.9	100.0	19.9	26.2	1.8	30.5	18.9	86.9	30.6	7.6	9.7	100.0
90–100	100.0	27.7	26.1	8.9	47.5	35.5	89.6	38.9	13.6	15.3	100.0
Age of head (years)											
Less than 35	87.3	6.7	13.7	*	13.7	5.3	42.1	11.4	*	10.0	89.2
35–44	91.2	9.0	16.8	.7	17.0	11.6	57.8	17.5	2.2	9.4	93.1
45–54	91.7	14.3	19.0	1.1	18.6	12.6	65.4	22.3	5.1	10.5	93.3
55–64	96.4	20.5	16.2	2.1	21.3	14.3	61.2	35.2	7.7	9.2	97.8
65–74	94.6	24.2	10.3	4.2	19.1	14.6	51.7	34.4	13.2	9.4	96.1
75 or more	95.3	37.0	7.9	3.5	20.2	13.2	30.0	27.6	14.0	5.3	97.4
Family structure											
Single with child(ren)	81.1	9.0	10.9	*	7.1	6.8	35.0	21.4	2.4	11.5	84.6
Single, no child, age less than 55	87.4	9.9	9.4	*	18.0	8.9	46.7	10.2	2.0	11.6	90.0
Single, no child, age 55 or more	94.6	24.0	9.6	2.1	13.5	10.8	36.7	22.0	11.2	7.9	96.2
Couple with child(ren)	94.3	12.5	24.0	1.2	18.9	12.0	62.1	23.6	4.4	8.6	95.1
Couple, no child	95.7	22.5	11.6	2.9	24.1	14.4	62.6	30.2	8.1	8.7	97.3
Education of head											
No high school diploma	75.7	9.5	3.4	*	3.9	2.2	21.6	12.6	1.7	7.1	79.7
High school diploma	90.9	14.1	11.5	.6	9.3	5.8	43.3	22.6	4.2	8.2	93.3
Some college	93.9	14.1	16.4	1.2	17.4	8.9	53.0	23.4	6.6	10.0	95.6
College degree	98.7	21.6	21.6	3.3	31.5	21.4	73.9	27.2	8.5	10.8	98.9

Table 6. Family holdings of financial assets, by selected characteristics of families and type of asset, 2007 and 2010 surveys—*continued*

A. 2007 Survey of Consumer Finances—*continued*

Family characteristic	Trans-action accounts	Certifi-cates of deposit	Savings bonds	Bonds	Stocks	Pooled invest-ment funds	Retire-ment accounts	Cash value life insurance	Other managed assets	Other	Any financial asset
Race or ethnicity of respondent											
White non-Hispanic	95.5	19.4	17.8	2.1	21.4	13.7	58.5	25.3	7.3	9.7	96.8
Nonwhite or Hispanic	83.9	8.2	7.8	.4	9.4	5.8	39.5	17.6	2.3	8.3	86.7
Current work status of head											
Working for someone else	92.6	13.2	17.0	.9	17.8	10.4	62.7	20.3	3.7	9.2	94.2
Self-employed	96.9	15.0	15.9	4.2	24.3	21.4	55.4	32.1	6.9	14.8	98.0
Retired	91.6	25.7	10.2	2.3	16.4	11.3	34.2	27.3	11.2	7.0	93.7
Other not working	78.6	5.6	10.7	*	12.8	*	22.4	14.6	*	10.4	81.3
Current occupation of head											
Managerial or professional	98.3	18.2	21.1	3.1	28.7	19.7	74.9	24.9	6.7	11.0	98.7
Technical, sales, or services	91.9	11.5	15.0	.4	14.9	8.8	54.9	21.3	4.0	9.1	94.1
Other occupation	87.9	9.2	13.1	*	9.9	5.4	51.3	19.0	1.1	9.8	90.2
Retired or other not working	89.5	22.5	10.3	2.0	15.8	9.9	32.3	25.3	9.8	7.5	91.8
Region											
Northeast	91.3	18.1	18.9	2.0	21.4	15.5	53.7	23.5	6.4	5.4	92.5
Midwest	93.6	16.8	16.0	1.2	17.9	10.6	58.1	26.6	6.7	9.3	95.4
South	91.3	15.1	12.0	1.7	15.4	9.7	49.3	23.4	5.2	8.5	93.5
West	92.7	15.5	15.0	1.6	19.2	11.5	53.1	18.3	5.5	13.9	93.9
Urbanicity											
Metropolitan statistical area (MSA)	92.8	16.2	15.1	1.8	19.4	12.1	55.1	22.2	5.9	9.5	94.3
Non-MSA	88.7	15.9	13.8	.8	10.9	7.7	42.5	26.8	5.5	8.5	91.8
Housing status											
Owner	97.3	20.0	18.2	2.2	22.4	15.0	63.7	28.9	7.5	9.4	98.4
Renter or other	80.8	7.7	7.5	.4	8.1	3.5	29.6	10.1	2.1	9.1	84.0
Percentile of net worth											
Less than 25	76.3	2.5	4.8	*	4.3	*	19.7	7.8	*	7.4	79.6
25–49.9	93.6	9.9	12.3	*	10.2	3.6	48.6	19.7	1.9	8.9	96.4
50–74.9	98.6	19.4	17.6	*	17.2	10.4	63.1	28.5	6.2	8.6	99.5
75–89.9	100.0	32.5	25.9	*	31.7	22.8	77.5	32.3	11.1	9.4	100.0
90–100	100.0	32.9	23.2	11.7	52.4	42.2	84.8	41.7	20.6	16.6	100.0

ship increased 4.3 percentage points for single families with children but declined 2.7 percentage points for childless single families headed by someone 55 or older; and by work status, ownership fell 1.6 percentage points for families headed by a person who was self-employed. Ownership increased for nonwhite or Hispanic families and for white non-Hispanic families. The share of homeowners with financial assets fell 0.4 percentage points, but the ownership rate for renters rose 1.8 percentage points.

Although the overall ratio of financial assets to total assets rose over the recent period, that increase is attributable to the relatively larger declines in the value of nonfinancial assets; the median holding of financial assets for families having such assets fell 28.8 percent, while the mean fell 3.3 percent. The recent change in the median erased the gains experienced in the previous three-year period (2004 to 2007) and left median financial assets at their lowest level since the 1995 survey (data not shown in the tables). The decline in median financial asset holdings was widespread across demographic groups, with gains observed for families headed by someone 75 or older, the top 10 percent of families ranked by income, and the top 10 percent of families ranked by net worth.

Table 6. Family holdings of financial assets, by selected characteristics of families and type of asset, 2007 and 2010 surveys—*continued*

A. 2007 Survey of Consumer Finances—*continued*

Family characteristic	Transaction accounts	Certificates of deposit	Savings bonds	Bonds	Stocks	Pooled investment funds	Retirement accounts	Cash value life insurance	Other managed assets	Other	Any financial asset
Median value of holdings for families holding asset (thousands of 2010 dollars)											
All families	**4.2**	**21.0**	**1.0**	**83.8**	**17.8**	**58.7**	**47.1**	**8.4**	**73.3**	**6.3**	**30.2**
Percentile of income											
Less than 20	.8	18.9	.5	*	4.0	31.4	6.3	2.6	104.8	1.6	1.8
20–39.9	1.7	18.9	1.0	*	10.5	31.4	12.6	5.2	90.1	3.1	7.3
40–59.9	2.9	17.8	.7	*	5.8	39.3	25.1	5.4	61.8	4.2	19.9
60–79.9	6.3	11.5	1.0	19.9	14.7	36.7	50.3	10.4	54.5	10.5	62.9
80–89.9	13.5	21.0	2.1	84.9	15.7	48.2	94.7	9.4	31.4	10.5	138.0
90–100	38.4	44.0	2.6	261.9	78.6	188.6	214.8	29.4	94.3	47.1	423.8
Age of head (years)											
Less than 35	2.5	5.2	.7	*	3.1	18.9	10.0	2.9	*	1.6	7.1
35–44	3.6	5.2	1.0	10.2	15.7	23.6	38.8	8.7	25.1	8.4	27.2
45–54	5.2	15.7	1.0	209.5	19.4	52.4	66.0	10.5	47.1	6.3	56.9
55–64	5.4	24.1	2.0	95.1	25.1	117.3	104.8	10.5	61.8	21.0	77.2
65–74	8.1	24.4	1.0	52.4	39.8	90.1	80.7	10.5	73.3	10.5	71.3
75 or more	6.4	31.4	21.0	104.8	41.9	78.6	36.7	5.2	104.8	15.7	43.5
Family structure											
Single with child(ren)	1.7	7.9	1.0	*	10.5	48.2	17.8	4.0	21.0	4.2	6.3
Single, no child, age less than 55	2.6	6.3	1.6	*	4.0	16.8	25.4	5.8	62.9	3.1	13.3
Single, no child, age 55 or more	2.9	29.3	4.2	52.4	26.2	80.7	48.8	5.2	104.8	3.8	28.3
Couple with child(ren)	4.8	10.5	1.0	84.9	15.7	52.4	49.5	9.9	36.7	5.2	31.3
Couple, no child	7.9	27.2	1.6	83.8	26.2	65.5	69.1	10.5	54.5	15.7	73.8
Education of head											
No high school diploma	1.3	14.7	1.0	*	2.8	67.1	15.7	2.6	31.4	1.6	3.1
High school diploma	2.6	16.8	1.0	48.7	10.5	31.4	29.9	5.4	83.8	5.2	14.9
Some college	2.9	18.9	1.0	52.4	6.3	26.2	33.5	8.4	54.5	4.2	21.0
College degree	10.5	26.2	1.2	104.8	26.2	78.6	78.6	13.6	78.6	10.5	101.0

Note: See note to table 1.

* Ten or fewer observations.

Transaction Accounts and Certificates of Deposit

In 2010, 92.5 percent of families had some type of transaction account—a category comprising checking, savings, and money market deposit accounts; money market mutual funds; and call or cash accounts at brokerages. The increase of 0.4 percentage point in ownership since 2007 continued the general upward trend seen in recent surveys; the ownership rate is now 1.9 percentage points higher than in 1998 (data not shown in the tables). Families that did not have any type of transaction account in 2010 were disproportionately likely to have incomes in the lowest income quintile, to be headed by a person younger than age 35, to be nonwhite or Hispanic, to be headed by a person who was neither working nor retired, to be renters, or to have net worth in the lowest quartile. See box 4 "Decisions about Checking Accounts" for a discussion of the reasons families do or do not have a checking account. Over the 2007–10 period, transaction account ownership rose noticeably—between 2.2 and 4.1 percentage points—for single families with children, families headed by a person in the other-not-working work-status group, and families in the bottom quartile of the net worth distribution.

Table 6. Family holdings of financial assets, by selected characteristics of families and type of asset, 2007 and 2010 surveys—*continued*

A. 2007 Survey of Consumer Finances—*continued*

Family characteristic	Trans-action accounts	Certifi-cates of deposit	Savings bonds	Bonds	Stocks	Pooled invest-ment funds	Retire-ment accounts	Cash value life insurance	Other managed assets	Other	Any financial asset
Race or ethnicity of respondent											
White non-Hispanic	5.3	21.0	1.0	100.4	19.9	67.1	55.5	9.4	73.3	10.1	47.2
Nonwhite or Hispanic	2.1	10.5	1.0	24.2	8.4	31.4	26.2	5.2	31.4	3.1	9.4
Current work status of head											
Working for someone else	4.0	10.5	1.0	49.1	11.0	44.0	42.1	7.9	28.5	5.2	30.2
Self-employed	10.4	26.2	1.0	157.2	62.9	83.8	95.3	25.1	83.8	16.8	56.7
Retired	4.2	31.4	2.6	83.3	30.1	81.9	52.4	5.8	104.8	10.5	31.3
Other not working	1.0	15.7	2.1	*	6.5	*	21.8	2.3	*	3.1	3.9
Current occupation of head											
Managerial or professional	9.2	15.7	1.0	83.8	21.0	78.6	75.4	13.6	61.8	10.5	82.1
Technical, sales, or services	3.1	15.7	1.0	129.1	12.6	41.9	31.4	9.4	10.5	5.2	18.4
Other occupation	2.6	10.5	.7	*	4.2	18.9	25.3	5.2	21.0	5.2	14.6
Retired or other not working	3.5	31.4	2.1	100.4	26.2	81.9	47.1	5.2	104.8	5.8	24.8
Region											
Northeast	5.3	21.0	1.0	120.1	18.7	52.4	60.1	9.4	76.5	10.5	46.4
Midwest	3.9	12.6	1.0	51.6	14.7	39.3	38.3	7.3	70.2	6.3	32.7
South	3.7	21.0	1.3	104.8	18.7	73.3	41.9	8.4	83.8	4.2	22.0
West	4.5	24.1	1.0	62.9	18.9	61.6	47.7	10.4	62.9	6.3	30.5
Urbanicity											
Metropolitan statistical area (MSA)	4.7	21.0	1.0	104.8	19.9	62.9	50.0	9.4	73.3	8.4	34.2
Non-MSA	2.6	10.5	1.3	52.4	11.5	35.6	35.3	5.2	47.1	2.5	16.8
Housing status											
Owner	6.5	21.0	1.0	104.8	21.0	62.9	59.7	10.4	73.3	10.5	57.7
Renter or other	1.3	10.5	.7	15.7	5.8	41.9	10.5	2.1	56.6	2.1	4.0
Percentile of net worth											
Less than 25	.7	2.1	.5	*	1.1	*	3.1	1.3	*	1.3	1.5
25–49.9	2.1	7.3	.7	*	3.1	9.4	15.7	3.1	14.5	3.1	14.0
50–74.9	6.3	15.7	1.3	*	6.3	26.2	52.4	6.8	52.4	10.5	63.6
75–89.9	16.2	26.2	2.1	*	21.0	52.4	125.7	15.7	83.8	21.0	226.6
90–100	48.7	52.4	3.7	173.8	131.0	276.6	333.2	31.4	165.5	52.4	809.9
MEMO											
Mean value of holdings for families holding asset	27.7	58.3	6.9	601.7	231.7	324.4	154.7	32.7	260.7	52.7	248.8

The slight overall expansion in ownership of transaction accounts in the recent three-year period is reflected in the mostly offsetting changes in the types of transaction account held by families. Ownership of checking and savings accounts rose, while ownership of money market accounts declined and that of call accounts was basically unchanged, as shown in table 6.1:

Table 6. Family holdings of financial assets, by selected characteristics of families and type of asset, 2007 and 2010 surveys—*continued*

B. 2010 Survey of Consumer Finances

Family characteristic	Trans-action accounts	Certifi-cates of deposit	Savings bonds	Bonds	Stocks	Pooled invest-ment funds	Retire-ment accounts	Cash value life insurance	Other managed assets	Other	Any financial asset
Percentage of families holding asset											
All families	**92.5**	**12.2**	**12.0**	**1.6**	**15.1**	**8.7**	**50.4**	**19.7**	**5.7**	**8.0**	**94.0**
Percentile of income											
Less than 20	76.2	5.7	3.6	.1	3.8	2.1	11.2	10.7	1.7	7.0	79.2
20–39.9	91.1	11.1	6.0	*	6.0	3.5	30.5	17.2	4.2	6.7	93.6
40–59.9	96.4	11.7	10.8	*	11.7	5.8	52.8	19.5	5.5	9.6	97.8
60–79.9	98.9	15.8	16.0	1.3	17.3	8.8	69.7	22.8	6.9	7.3	99.6
80–89.9	99.8	12.1	23.0	2.0	25.7	14.6	85.7	25.8	7.8	8.5	100.0
90–100	99.9	21.5	24.4	8.3	47.8	32.1	90.1	30.9	12.3	10.3	100.0
Age of head (years)											
Less than 35	89.0	5.7	10.0	*	10.1	3.6	41.1	9.6	.9	9.0	91.3
35–44	90.6	5.7	11.6	.4	12.1	7.7	52.2	12.3	2.0	8.4	92.7
45–54	92.5	10.0	15.0	1.4	16.0	9.6	60.0	19.8	4.5	7.7	94.2
55–64	94.2	14.6	14.3	2.4	19.5	11.3	59.8	25.7	7.7	8.9	95.8
65–74	95.8	20.6	9.1	3.4	16.1	11.1	49.0	28.4	11.4	7.5	96.2
75 or more	96.4	27.2	10.1	3.6	20.1	11.9	32.8	32.4	14.1	5.0	96.4
Family structure											
Single with child(ren)	84.9	6.7	6.3	*	6.9	3.0	34.0	11.1	3.3	8.3	88.9
Single, no child, age less than 55	88.3	6.0	6.3	*	10.7	5.0	40.2	9.8	1.5	11.3	90.6
Single, no child, age 55 or more	92.8	20.1	7.0	2.5	11.9	9.5	33.7	23.5	9.9	7.7	93.5
Couple with child(ren)	94.3	10.4	18.9	1.2	17.0	9.1	60.1	18.9	3.9	7.6	95.7
Couple, no child	95.9	15.8	12.4	2.9	20.9	12.4	61.6	27.9	8.8	6.7	96.6
Education of head											
No high school diploma	77.4	6.0	2.7	*	2.2	*	17.1	11.9	3.1	5.3	80.8
High school diploma	90.0	10.8	9.1	.2	8.1	3.2	40.6	19.8	4.2	7.2	92.7
Some college	94.6	11.8	11.7	1.0	11.3	5.4	48.6	17.3	5.5	7.6	95.0
College degree	98.4	15.6	17.7	3.6	27.2	17.6	70.5	23.3	7.9	9.8	98.9

Table 6.1

Type of transaction account	All families	
	2010 (percent)	Change, 2007–10 (percentage points)
Checking	90.4	.7
Savings	50.5	3.4
Money market	17.2	–3.7
Call	2.0	–.1

The savings account category includes a relatively small number of tax-preferred accounts such as medical or health savings accounts and Coverdell or 529 education accounts.[21] Ownership of any of these types of tax-preferred accounts decreased from 3.8 percent in 2007 to 2.9 percent in 2010 (data not shown in the tables). In both of the two years,

[21] Coverdell savings accounts, formerly known as education individual retirement accounts, and 529 saving plans are tax-preferred plans that parents or others may use to save for educational expenses.

Table 6. Family holdings of financial assets, by selected characteristics of families and type of asset, 2007 and 2010 surveys—*continued*

B. 2010 Survey of Consumer Finances—*continued*

Family characteristic	Trans-action accounts	Certifi-cates of deposit	Savings bonds	Bonds	Stocks	Pooled invest-ment funds	Retire-ment accounts	Cash value life insurance	Other managed assets	Other	Any financial asset
Race or ethnicity of respondent											
White non-Hispanic	96.5	15.0	14.8	2.3	18.6	11.6	58.1	22.6	7.3	8.2	97.3
Nonwhite or Hispanic	84.3	6.5	6.3	.2	7.9	2.6	34.4	13.7	2.3	7.6	87.2
Current work status of head											
Working for someone else	93.6	9.0	13.7	1.0	13.8	8.1	59.6	17.1	3.6	7.7	95.2
Self-employed	94.8	15.7	12.9	3.5	24.5	14.9	54.7	25.9	8.3	11.1	96.4
Retired	91.7	20.1	9.6	2.6	15.4	8.9	34.4	25.5	10.4	7.3	92.9
Other not working	82.7	3.9	5.8	*	9.5	2.8	24.6	10.2	*	8.3	85.0
Current occupation of head											
Managerial or professional	98.2	14.1	17.3	2.6	24.3	16.0	73.5	21.6	6.8	10.2	99.2
Technical, sales, or services	91.7	7.4	11.0	.8	10.8	5.8	47.7	17.3	2.8	7.5	93.8
Other occupation	89.6	7.5	11.0	*	8.3	3.1	50.0	15.6	2.4	6.2	91.6
Retired or other not working	89.7	16.6	8.8	2.1	14.1	7.6	32.3	22.2	8.5	7.5	91.2
Region											
Northeast	91.2	12.4	16.9	2.0	16.5	11.7	54.4	20.6	6.1	7.1	93.0
Midwest	94.2	13.5	13.5	.8	13.8	7.2	54.6	23.3	6.1	7.3	95.5
South	91.1	11.4	9.8	1.5	13.1	7.2	45.9	19.3	5.1	7.2	92.9
West	94.2	12.0	10.1	2.3	18.7	10.4	50.5	16.1	6.0	10.8	95.4
Urbanicity											
Metropolitan statistical area (MSA)	92.8	12.1	12.7	1.8	16.6	9.6	52.2	19.3	6.0	8.1	94.2
Non-MSA	91.2	12.6	8.8	.8	7.9	4.5	41.9	21.9	3.9	7.5	93.1
Housing status											
Owner	97.4	15.6	15.0	2.3	19.6	11.4	61.7	24.0	7.6	7.6	98.0
Renter or other	82.4	5.2	5.8	.3	6.0	3.1	27.1	10.9	1.8	8.7	85.8
Percentile of net worth											
Less than 25	78.5	1.4	4.8	*	2.9	*	19.8	7.3	*	5.9	81.7
25–49.9	94.2	5.3	7.0	*	5.6	2.1	42.7	14.2	1.9	8.5	96.1
50–74.9	98.0	14.8	14.2	*	14.0	6.1	58.6	24.1	4.6	7.2	98.7
75–89.9	99.0	27.0	21.6	2.0	26.8	15.5	75.8	30.8	13.1	8.0	99.4
90–100	99.9	27.7	22.8	12.0	54.9	41.8	87.8	36.8	19.3	13.7	100.0

529 plans accounted for about 80 percent of the number of these tax-preferred savings accounts, up from 71 percent in 2004.

Median holdings in transaction accounts for those who had such accounts fell 16.7 percent from 2007 to 2010, while the mean rose 17.0 percent. The decline in median transaction account balances was widely observed across demographic groups, but there were noticeable exceptions for childless single families headed by someone aged 55 or older, families headed by individuals who reported their current work status as retired, families in the 75-or-older age group, and families in the highest decile of the net worth distribution. Indeed, within the highest decile of net worth, median transaction balances rose from $48,700 to $60,800, an increase of 24.8 percent. The increase in the already substantial holdings of highly liquid and secure transaction account balances among this group of wealthy families is a key to understanding the rise in the overall mean transaction account balances while the overall median fell.

Certificates of deposit—interest-bearing deposits with a set term—are traditionally viewed

Table 6. Family holdings of financial assets, by selected characteristics of families and type of asset, 2007 and 2010 surveys—*continued*

B. 2010 Survey of Consumer Finances—*continued*

Family characteristic	Trans-action accounts	Certifi-cates of deposit	Savings bonds	Bonds	Stocks	Pooled invest-ment funds	Retire-ment accounts	Cash value life insurance	Other managed assets	Other	Any financial asset
Median value of holdings for families holding asset (thousands of 2010 dollars)											
All families	**3.5**	**20.0**	**1.0**	**137.0**	**20.0**	**80.0**	**44.0**	**7.3**	**70.0**	**5.0**	**21.5**
Percentile of income											
Less than 20	.7	15.0	.5	20.0	20.0	38.0	8.0	3.1	38.0	2.3	1.1
20–39.9	1.5	15.0	.5	*	8.0	38.1	11.0	4.2	45.0	2.7	5.2
40–59.9	2.8	18.0	1.0	*	5.6	50.0	22.8	5.0	60.0	5.0	17.1
60–79.9	5.3	16.0	.7	30.0	13.0	50.0	37.0	7.5	33.0	7.0	39.5
80–89.9	11.1	29.0	.8	141.0	14.0	65.5	88.0	10.0	82.0	10.0	120.2
90–100	35.0	34.0	2.0	297.2	60.0	200.0	277.0	30.0	150.0	28.0	550.8
Age of head (years)											
Less than 35	2.1	5.2	.5	*	5.4	8.5	10.5	2.1	9.0	2.0	5.5
35–44	2.5	7.0	.9	10.0	10.0	41.0	31.2	5.0	10.0	2.7	14.5
45–54	3.5	16.0	.8	150.0	30.0	110.0	60.0	10.0	50.0	7.0	33.7
55–64	5.0	20.0	1.2	250.0	35.0	110.0	100.0	9.3	65.0	11.0	55.8
65–74	5.7	25.0	4.0	100.0	48.0	115.0	100.0	10.0	95.0	15.0	45.2
75 or more	7.2	32.2	1.0	141.0	45.0	120.0	54.0	7.0	82.0	16.0	43.8
Family structure											
Single with child(ren)	1.0	6.0	1.3	*	15.0	28.0	17.8	2.0	30.0	8.0	4.8
Single, no child, age less than 55	2.0	6.7	.5	*	7.9	21.0	20.5	5.0	15.0	2.0	7.9
Single, no child, age 55 or more	3.9	20.0	1.7	120.0	37.5	120.0	46.0	4.0	70.0	10.0	22.1
Couple with child(ren)	3.8	14.0	.8	129.0	15.0	75.0	44.1	8.0	50.0	5.0	25.1
Couple, no child	7.1	30.0	1.2	175.0	33.0	90.0	77.4	11.6	90.0	9.0	57.2
Education of head											
No high school diploma	.8	40.0	.5	*	2.7	*	16.3	4.5	50.0	1.3	1.6
High school diploma	2.0	20.0	.6	49.8	9.5	62.0	25.0	5.2	35.0	3.6	10.3
Some college	2.5	12.0	.8	40.0	9.9	35.0	27.0	6.0	60.0	5.0	14.1
College degree	9.3	20.0	1.0	150.0	32.0	101.0	76.3	12.0	95.0	10.0	75.7

Note: See note to table 1.

* Ten or fewer observations.

as a low-risk saving vehicle, and they are often used by persons who desire a safe haven from the volatility of financial markets. Over the 2007–10 period, the attractiveness of CDs was subjected to competing forces, two of which seem particularly powerful. Increased volatility in stock and bond markets made CDs more attractive relative to those investments as a haven from risk, but the convergence of yields on all relatively safe assets at a level near zero implied that the advantage CDs typically hold over transaction accounts was greatly reduced. The net result of these and other factors is that CD ownership fell 3.9 percentage points between 2007 and 2010, and the median balance held in CDs among those owning them fell 4.8 percent; at the same time, the mean holdings rose 24.5 percent. The decline in ownership rates was widespread, with the self-employed being the only demographic group to show an increase in the ownership rate. However, the growth in median balances across demographic groups was more diverse; notable increases in median balances were observed for the highest decile of the net worth distribution, families in the Midwest region, families headed by a person who was self-employed, families with incomes between the 40th and 90th percentiles of the income distribution, and families headed by a person who did not have any college education.

Table 6. Family holdings of financial assets, by selected characteristics of families and type of asset, 2007 and 2010 surveys—*continued*

B. 2010 Survey of Consumer Finances—*continued*

Family characteristic	Transaction accounts	Certificates of deposit	Savings bonds	Bonds	Stocks	Pooled investment funds	Retirement accounts	Cash value life insurance	Other managed assets	Other	Any financial asset
Race or ethnicity of respondent											
White non-Hispanic	5.0	20.0	1.0	142.0	25.0	91.0	54.0	8.0	73.0	7.5	37.1
Nonwhite or Hispanic	1.6	13.0	1.0	5.0	10.0	50.0	25.0	5.0	25.0	3.0	6.0
Current work status of head											
Working for someone else	3.3	10.0	.6	100.0	12.5	50.0	35.6	6.0	31.7	3.0	20.9
Self-employed	7.5	30.0	1.3	257.4	50.0	103.6	85.0	19.0	89.0	10.0	50.5
Retired	4.5	30.0	2.0	140.0	35.0	120.0	66.7	7.3	75.0	10.0	29.1
Other not working	1.0	10.0	1.0	*	11.0	120.0	19.3	5.0	*	3.5	2.8
Current occupation of head											
Managerial or professional	8.5	15.0	1.0	170.0	30.0	100.0	73.1	10.0	84.0	9.0	64.5
Technical, sales, or services	2.1	12.0	1.0	36.4	10.0	54.9	25.0	5.0	25.0	2.5	10.6
Other occupation	2.2	10.0	.5	*	5.6	9.0	25.3	6.0	17.8	2.8	11.7
Retired or other not working	3.0	29.0	1.5	141.0	30.0	120.0	56.5	7.0	73.0	7.0	15.9
Region											
Northeast	4.5	15.0	1.0	104.0	25.0	110.0	60.0	10.0	38.0	6.5	33.4
Midwest	3.4	17.0	.5	300.0	11.0	52.0	40.0	5.6	80.0	3.0	23.5
South	3.0	20.0	1.0	200.0	20.0	87.5	37.2	7.0	85.0	5.0	16.6
West	4.0	20.0	1.0	100.0	30.0	75.0	45.0	9.0	40.0	8.0	20.3
Urbanicity											
Metropolitan statistical area (MSA)	3.9	19.0	1.0	142.6	23.4	91.0	49.6	8.0	70.0	5.0	23.9
Non-MSA	2.5	20.0	.5	53.1	10.0	40.0	28.8	5.0	70.0	4.0	13.3
Housing status											
Owner	5.8	20.0	1.0	129.0	26.5	100.0	59.3	8.5	75.0	8.0	45.8
Renter or other	1.0	10.0	.6	164.0	5.6	20.0	10.0	4.0	16.0	3.0	3.0
Percentile of net worth											
Less than 25	.6	1.5	.2	*	1.0	*	5.0	1.5	*	1.0	1.1
25–49.9	1.7	5.5	.5	*	2.5	5.0	12.0	3.1	10.0	3.0	7.8
50–74.9	5.2	15.0	.6	*	7.0	20.5	42.0	5.8	30.0	5.0	45.2
75–89.9	14.5	25.0	1.4	50.0	25.0	60.0	133.0	13.7	70.0	10.0	201.0
90–100	60.8	65.0	3.0	220.0	110.0	245.0	413.0	30.0	150.0	70.0	888.0
MEMO											
Mean value of holdings for families holding asset	32.4	72.6	6.1	615.0	209.7	388.6	171.2	28.4	247.9	63.9	240.6

Savings Bonds and Other Bonds

Savings bonds are owned disproportionately by families in the highest 40 percent of the income distribution and by families in the top half of the distribution of net worth. Over the 2007–10 period, the ownership of savings bonds declined 2.9 percentage points to 12.0 percent overall, and it fell for virtually all demographic groups. The drop in ownership between 2007 and 2010 continued a general downward trend observed in the SCF for some time; in 1998, 19.3 percent of families owned savings bonds (data not shown in the tables). Median holdings were unchanged over the recent three-year period, but the mean fell 11.6 percent.

Box 4. Decisions about Checking Accounts

Between 2007 and 2010, the proportion of families with any type of transaction account edged up (table 6 in the main text), while the share without a checking account fell 0.7 percentage point, from 10.3 percent to 9.6 percent (data not shown in the tables). The decline in the fraction of families without a checking account follows a longer trend; in 1989, the share was 18.7 percent.[1]

Among families without a checking account in 2010, 55.5 percent had held such an account in the past, 59.1 percent had incomes in the lowest quintile of that distribution, 50.9 percent were headed by a person younger than age 45, and 66.0 percent were nonwhite or Hispanic. The Survey of Consumer Finances (SCF) asked all families that did not have a checking account to give a reason for not having an account (table A). The most commonly reported reason—given by 27.8 percent of such families—was that the family did not like dealing with banks; the percentage citing this reason has risen steadily since 1989. Another 20.3 percent did not write enough checks to make account ownership worthwhile; this reason had been the most frequently reported one in each of the years before 2007. Another 10.6 percent of families said that service charges were too high. The SCF showed a decrease in the fraction of families reporting credit problems as a reason—from 6.6 percent in 2007 to 4.2 percent in 2010; this reason had risen substantially through 2007 from previous years.

Table A. Distribution of reasons cited by respondents for their families' not having a checking account, by reason, 2001–10 surveys

Percent

Reason	2001	2004	2007	2010
Do not write enough checks to make it worthwhile	28.5	27.9	18.7	20.3
Minimum balance is too high	6.5	5.6	7.6	7.4
Do not like dealing with banks	22.6	22.6	25.2	27.8
Service charges are too high	10.2	11.6	12.3	10.6
Cannot manage or balance a checking account	6.6	6.8	3.9	4.7
Do not have enough money	14.0	14.4	10.4	10.3
Credit problems	3.6	*	6.6	4.2
Do not need/want an account	5.1	5.2	8.9	7.3
Other	2.8	3.5	6.4	7.4
Total	**100**	**100**	**100**	**100**

* Ten or fewer observations in any of the types of income.

When attention is further restricted to families that once had a checking account (data not shown in the tables), the general pattern of responses is similar to that for all families without a checking account, but some differences are evident. For families that once had a checking account, the proportion reporting they do not have enough money, do not write enough checks, or do not need or want an account rose in 2010. These increases were offset by decreases in the proportion reporting they have credit problems, dislike dealing with banks, or cannot manage or balance a checking account.

The SCF asked all families with a checking account to give the most important reason they chose the financial institution for their main checking account (table B). In 2010, 46.0 percent of families chose the institution for their main checking account for reasons related to the location of the offices of the institution.[2] Another 16.6 percent placed the most importance on the ability to obtain many services at one place, and 14.2 percent singled out the importance of obtaining the lowest fees or minimum balance requirements. Absence of risk was of primary importance for only a relatively small fraction of families. Over the 2007–10 period, the most noticeable changes in these responses were decreases in the fraction of families citing reasons related to a personal relationship with the bank or a connection through work or school. Overall, the fractions of families reporting each reason changed little from 2007.

continued on next page

Box 4—*continued*

Table B. Distribution of reasons cited by respondents as the most important reason for choosing institution for their main checking account, 2001–10 surveys

Percent

Reason	2001	2004	2007	2010
Location of their offices	42.8	45.4	45.9	46.0
Had the lowest fees/minimum balance requirement	16.6	16.3	13.7	14.2
Able to obtain many services at one place	16.4	15.3	16.2	16.6
Recommended; friend/family has account there	4.7	3.9	4.2	4.0
Personal relationship; they know me; family member works there	4.0	3.5	4.2	3.3
Connection through work or school	2.0	3.5	3.3	2.1
Always done business there; banked there a long time; other business there	2.4	2.9	3.0	2.4
Offered safety and absence of risk	2.2	1.9	2.9	3.6
Other convenience; payroll deduction/direct deposit	1.3	1.2	.5	.7
Other	7.5	6.1	6.1	7.1
Total	**100**	**100**	**100**	**100**

[1] For the definition of "transaction account," see the main text. For a more extensive discussion of the ways that families obtain checking and credit services, see Jeanne M. Hogarth, Christoslav E. Anguelov, and Jinhook Lee (2005), "Who Has a Bank Account? Exploring Changes over Time, 1989–2001," *Journal of Family and Economic Issues*, vol. 26 (Spring), pp. 7–30.

[2] For a discussion of the definition of local banking markets, see Dean F. Amel, Arthur B. Kennickell, and Kevin B. Moore (2008), "Banking Market Definition: Evidence from the Survey of Consumer Finances," Finance and Economics Discussion Series 2008-35 (Washington: Board of Governors of the Federal Reserve System, August; paper dated July 7), www.federalreserve.gov/pubs/feds/2008/200835/200835pap.pdf.

Other bond types tend to be very narrowly held, and the ownership rate was unchanged from 2007 at 1.6 percent in 2010.[22] As shown in the following table, the proportion of families that owned tax-exempt bonds or corporate or foreign bonds increased slightly in the recent period, while ownership of other types of bonds declined slightly:

Table 6.2

Type of bond	All families	
	2010 (percent)	Change, 2007–10 (percentage points)
Government	.3	–.1
Tax exempt	1.2	.2
Mortgage backed	.2	–.1
Corporate or foreign	.5	.1

Ownership of any type of bond other than savings bonds is concentrated among the highest tiers of the income and wealth distributions, and these groups saw little change in ownership from 2007 to 2010. The median value of holdings of such bonds for families that had them rose 63.5 percent over this period, while the mean rose 2.2 percent.

[22] "Other bonds" as reported in the survey are held directly and include corporate and mortgage-backed bonds; federal, state, and local government bonds; and foreign bonds. In this article, financial assets held indirectly are those held in tax-preferred retirement accounts or managed accounts such as trusts or annuities.

Publicly Traded Stock

The direct ownership of publicly traded stocks is more widespread than the direct ownership of bonds, but, as with bonds, it is also concentrated among high-income and high-wealth families. The overall share of families with any such stock holdings declined 2.8 percentage points from 2007 to 2010, to 15.1 percent, thereby continuing a decrease observed since direct stock ownership peaked in the 2001 SCF at 21.3 percent (data not shown in the tables). Across demographic groups, declines in ownership were more common than increases, with the noticeable exception of families in the top decile of net worth, for whom ownership rose 2.5 percentage points. Ownership also rose slightly for families in the top decile of income (by 0.3 percentage point) and for families headed by a person who was self-employed (by 0.2 percentage point).

Although the major stock price indexes decreased about 25 percent over the 2007–10 period, the median amount of directly held stock for families with such assets rose 12.4 percent, and the mean fell only 9.5 percent. The seeming contradiction between the movement in the indexes and the movement in the median and mean may be explained, in part, by the exit of holders of smaller amounts of stocks.

The wide variation in changes observed across demographic groups reflects changes in ownership rates as well as changes in the composition of some of the demographic groups noted earlier. One noticeable such instance is the group of families included in the lowest 20 percent of the income distribution in each year. The direct stock ownership rate for this group fell from 5.5 percent in 2007 to 3.8 percent in 2010, while median holdings for direct stock owners within the group rose from $4,000 in 2007 to $20,000 in 2010, a level that exceeded that for all but the highest income quintile group. An important part of the change in the median for the lowest income group may be explained by a change in the composition of the group to include a larger-than-usual fraction of families with relatively high net worth.

The great majority of families with directly held stock owned stock in only a small number of companies. As shown in the following table, over the three-year period, there were signs of increased diversification as the share of families owning stock in only one company decreased:

Table 6.3

Number of directly-held stocks	Families with directly-held stocks	
	2010 (percent)	Change, 2007–10 (percentage points)
1	29.2	–7.2
2 to 9	53.0	5.4
10 or more	17.8	1.8

For 35.5 percent of stockowners in 2010, at least one of the companies in which they owned stock was one that employed, or had employed, the family head or that person's spouse or partner (data not shown in the tables). Direct ownership of stock in a foreign company was less common; only 15.3 percent of stockholders had this type of stock.

Pooled Investment Funds

Directly held pooled investment funds are among the least commonly held of the types of financial assets shown in table 6.[23] As was the case for directly held stocks, from 2007 to 2010, direct ownership of pooled investment funds fell—a decline of 2.7 percentage points, to 8.7 percent of families in 2010. Ownership of pooled investment funds dropped for almost every demographic group over the three-year period, though the decrease was very slight for the top decile of the net worth distribution. The ownership declines at both the overall level and the level of the demographic groups continue a pattern observed since 2001, when overall ownership of pooled investment funds was at 17.7 percent (data not shown in the tables).

The survey also collects information on the different types of pooled investment funds owned by families. Ownership shifted over the recent period away from stock funds and toward "other bond" funds (largely corporate bonds); the residual "other" category, which consists almost entirely of hedge funds and exchange-traded funds, also increased, as shown in the following table:

Table 6.4

Type of pooled investment fund	All families	
	2010 (percent)	Change, 2007–10 (percentage points)
Stock	7.7	–2.6
Tax-free bond	1.9	–.1
Government bond	1.0	–.2
Other bond	1.4	.4
Combination	1.4	.1
Other	.9	.4

Among families owning pooled investment funds, the value of holdings has continued an increase seen over the preceding decade; in the recent three-year period, the median holding rose 36.3 percent, and the mean rose 19.8 percent. Median and mean values increased across almost every demographic group, evidence that the decrease in ownership may have been concentrated among families with relatively small account balances (data not shown in the tables).

Retirement Accounts

Ownership of tax-deferred retirement assets such as personally established individual retirement accounts (IRAs) or job-based 401(k) accounts tends to increase with families' income and net worth.[24] For several reasons, ownership is also more likely among families headed by a person less than 65 years of age than among the older groups. First, even though

[23] In this article, pooled investment funds exclude money market mutual funds and indirectly held mutual funds and include all other types of directly held pooled investment funds, such as traditional open-end and closed-end mutual funds, real estate investment trusts, and hedge funds.

[24] Tax-deferred retirement accounts consist of IRAs, Keogh accounts, and certain employer-sponsored accounts. Employer-sponsored accounts consist of 401(k), 403(b), and thrift savings accounts from current or past jobs; other current job plans from which loans or withdrawals can be made; and accounts from past jobs from which the family expects to receive the account balance in the future. This definition of employer-sponsored plans is intended to confine the analysis to accounts that are portable across jobs and for which families will ultimately have the option to withdraw the balance.

Usually, such accounts may be invested in virtually any asset, including stocks, bonds, pooled investment funds, options, and real estate. In principle, employer-sponsored plans may be invested in a similarly broad way, but, in practice, a person's choices for investment are sometimes limited to a narrower set of assets.

retirement accounts have been increasingly prevalent in the past 30 years, they may not have become available until relatively late in the careers of many persons in the older groups. Second, beginning in the year that a person reaches age 59½, funds held by that person in retirement accounts may be withdrawn without penalty, and some in the two oldest age groups may have already done so. Third, families may have used funds from retirement accounts accumulated from previous employment to purchase an annuity at retirement; annuities are treated in the SCF as a separate type of managed asset.

From 2007 to 2010, the fraction of families with retirement accounts fell 2.6 percentage points to 50.4 percent; the decrease offset most of the 3.1 percentage point increase over the preceding three years. The overall rate of retirement account ownership has varied around 50 percent for about the past decade. In the recent three-year period, the fraction of families that had some type of account plan associated with a current or past job or that held an IRA or Keogh account decreased, and the fraction that had at least one account of each type declined as well, as shown in the following table:

Table 6.5

Type of retirement account	All families	
	2010 (percent)	Change, 2007–10 (percentage points)
Account plan from current or past job	35.1	–2.9
Individual retirement account or Keogh	28.1	–2.5
MEMO		
Both types	12.6	–2.1

Over the 2007–10 period, ownership of retirement accounts decreased for nearly all of the groups considered here. The most noticeable declines in ownership were among families in the middle-income, middle-wealth, and middle-age groups; for those groups, retirement accounts had been growing in importance as a supplement to Social Security and other types of retirement income, and the decrease in ownership in the past three years may represent a setback in retirement preparedness. Across employment and occupation categories, the largest changes were the 3.1 percentage point drop in retirement account ownership among families whose head was working for someone else and the 7.2 percentage point drop for the technical, sales, or services occupation group.

In a reversal of a trend over the preceding decade, median holdings in retirement accounts decreased in the 2007–10 period; for families having such accounts, the median fell 6.6 percent. Mean balances continued to grow, however, at a rate of 10.7 percent over the three-year period. The patterns of changes in median account balances across demographic groups were mixed, but as with ownership rates, families in the middle-income, middle-wealth, and middle-age groups saw decreases in median account balances, while retirees and those with higher incomes and higher net worth saw noticeable increases.[25]

Although tax-deferred retirement assets are clearly an important element in retirement planning, families may hold a variety of other assets that are intended, at least in part, to finance retirement. Such other assets might also be used for contingencies as necessary.

[25] In addition, the 2009 panel interview with the 2007 SCF respondents indicated that some families in the age range for which a penalty is assessed for withdrawals from such accounts had closed their retirement accounts during the two-year period. Of the 55.8 percent of families headed by someone younger than age 58 that owned retirement accounts in 2007, 10.8 percent of the group reported not having such an account in 2009 (data not shown in the tables).

Similarly, a need for liquidity might drive a family to liquidate or borrow against a tax-deferred retirement asset, even if it will be assessed a penalty for doing so.

Two common and often particularly important types of retirement plans are not included in the assets described in this section: Social Security (the federally funded Old-Age and Survivors' Insurance program (OASI)) and employer-sponsored defined-benefit plans. OASI is well described elsewhere, and it covers the great majority of the population.[26] The retirement income provided by defined-benefit plans is typically based on workers' salaries and years of work with an employer, a group of employers, or a union. Unfortunately, future income streams from OASI and defined-benefit plans cannot be translated directly into a current value because valuation depends critically on assumptions about future events and conditions—work decisions, earnings, inflation rates, discount rates, mortality, and so on—and no widely agreed-upon standards exist for making these assumptions.[27]

However, the SCF does contain substantial information for family heads and their spouse or partner regarding any defined-benefit plans or other types of plans with some kind of account feature to which they have rights from a current or past job.[28] In 2010, 55.1 percent of families had rights to some type of plan other than OASI through the current or past work of either the family head or that person's spouse or partner, below the 57.7 percent level in 2007. For this group of families, the fraction with a standard defined-benefit plan with an annuity payout scheme increased slightly over the recent period, while the fraction with a plan with at least some account feature and the fraction that had both types of plans decreased, as shown in the following table:

Table 6.6

Type of pension plan	Families with any pension plan	
	2010 (percent)	Change, 2007–10 (percentage points)
Defined benefit	56.4	.6
Account plan	63.6	–2.2
MEMO		
Both types	20.0	–1.6

In many pension plans with account features, contributions may be made by the employer, the worker, or both. In some cases, these contributions represent a substantial amount of saving, though workers may offset this saving by reducing their saving in other forms. An employer's contributions also represent additional income for the worker. In 2010, 85.4 percent of families with an account plan on a current job of either the family head or that person's spouse or partner had an employer that made contributions to the plan, a decline of 1.8 percentage points from 2007. In 2010, 91.9 percent of families with such plans made contributions themselves, an increase of 0.5 percentage point from 2007. The median annual contribution by employers who contributed to such accounts was $2,300 in 2010,

[26] For a detailed description of OASI, see Social Security Administration, "Online Social Security Handbook: Your Basic Guide to the Social Security Programs," Publication 65-008, www.ssa.gov/OP_Home/handbook/ssa-hbk.htm.

[27] For one possible calculation of net worth that includes the annuity value of payments from defined-benefit pensions and OASI, see Arthur B. Kennickell and Annika E. Sundén (1997), "Pensions, Social Security, and the Distribution of Wealth," Finance and Economics Discussion Series 1997-55 (Washington: Board of Governors of the Federal Reserve System, October), www.federalreserve.gov/pubs/feds/1997/index.html.

[28] The definition of account plan used here differs slightly from that used in computing the survey wealth measure, which includes account balances only if the family has the ability to make withdrawals from, or borrow against, the account. Here the only criterion used in classification is whether any account balance exists. For example, a defined-benefit plan with a portable cash option, which would allow the covered worker to receive a lump sum in lieu of regular payments in retirement, would be treated as an account plan here.

and the median contribution by families who contributed was $3,000; both amounts were little changed from 2007 levels (data not shown in the tables).

The eligibility of working heads of families to participate in any type of job-related pension fell from 55.9 percent in 2007 to 52.9 percent in 2010; it had risen 1.1 percentage points over the preceding three years (data not shown in the tables). Participation by eligible workers is usually voluntary. In 2010, 84.3 percent of family heads who were eligible to participate elected to do so, up slightly from 83.8 percent in 2007.[29] The choice to participate appears to be related strongly to income. In 2010, the fraction of eligible family heads declining to participate was progressively lower at higher income levels, and this general pattern was not substantially altered from 2007, as shown by the following table:

Table 6.7

Percentile of income	Families headed by a person who was eligible for a work-related retirement plan on a current job and who declined to participate	
	2010 (percent)	Change, 2007–10 (percentage points)
Less than 20	54.6	.3
20–39.9	26.8	–1.3
40–59.9	17.0	–1.5
60–79.9	14.3	3.8
80–89.9	7.7	–3.2
90–100	5.5	–1.0

Cash Value Life Insurance

Cash value life insurance combines an investment vehicle with insurance coverage in the form of a death benefit.[30] Some cash value life insurance policies offer a high degree of choice in the way the policy payments are invested. Investment returns on such policies are typically shielded from taxation until the money is withdrawn; if the funds remain untapped until the policyholder dies, the beneficiary of the policy may receive, tax-free, the death benefit. In contrast, term insurance, the other popular type of life insurance, offers only a death benefit. One attraction of cash value policies for some people is that they promote regular saving funded through the required policy premium.

Ownership of cash value life insurance is broadly spread across demographic groups, with a tendency toward increasing rates among families with higher levels of income and net worth and those with older family heads. The change in ownership of cash value policies over the 2007–10 period continued a declining trend, decreasing 3.3 percentage points, to 19.7 percent of families in 2010. The decline was shared by virtually all demographic groups; the only group with a noticeable increase in ownership is families headed by someone aged 75 or older. Over the three-year period, ownership of any type of life insurance, cash value or term, also fell—from 64.9 percent in 2007 to 62.6 percent in 2010 (data not shown in the tables). Of those families with some type of life insurance, the proportion

[29] An analysis of the March Current Population Survey (CPS) with a definition of family head that is closest to that in this article does not show the same magnitude of decline in pension eligibility for employed family heads, but the levels are generally similar to those seen in the SCF. The CPS eligibility estimate for family heads with a job in the past year was 53.9 percent in 2007 and 53.5 percent in 2010. Differences in the definition of employment may explain some of the difference between the two surveys. Like the SCF, the CPS shows a small increase in the uptake rate for eligible workers—from 83.3 percent in 2007 to 83.6 percent in 2010.

[30] The survey measures the value of such policies according to their current cash value, not their death benefit. The cash value is included as an asset in this article only when the cash value at the time of the interview was nonzero.

with term policies was about unchanged, while the proportion with cash value policies fell; these changes are similar to trends observed in the earlier surveys.

After rising over the previous three-year period, the median value of cash value life insurance for families that had any such insurance fell 13.1 percent between 2007 and 2010, and the mean fell 13.1 percent. The median showed a mix of increases and decreases across demographic groups, although it declined considerably for younger families, single families with children, families headed by a person who was self-employed or working for someone else, and families headed by someone working in a technical, sales, or service occupation.

Other Managed Assets

Ownership of other managed assets—personal annuities and trusts with an equity interest and managed investment accounts—is concentrated among families with higher levels of income and wealth and among families headed by a person who is aged 55 or older or who is retired.[31] Ownership of these assets was little changed between 2007 and 2010, following a more substantial decrease over the previous three years. Changes in ownership rates across demographic groups were mixed in the recent three-year period, with the vast majority of 2010 values within 2 percentage points of the corresponding 2007 values. Across all families, the fraction with an annuity was nearly unchanged over the period, and the fraction with a trust or managed investment account edged down, as shown in the following table:

Table 6.8

Type of other managed asset	All families	
	2010 (percent)	Change, 2007–10 (percentage points)
Annuity	4.5	.1
Trust or managed investment account	1.3	–.3
MEMO		
Both types	.2	–.1

Between 2007 and 2010, the median value of other managed assets for families that had such assets decreased 4.5 percent, offsetting some of the substantial increase in the preceding three-year period. Over the more recent period, the corresponding mean value fell 4.9 percent. Changes in median holdings varied greatly across demographic groups—for example, increasing substantially in the top two income groups, but falling by more than 60 percent in the group of families headed by someone aged 35 to 44. For families with an equity interest in an annuity, the median holding increased 14.5 percent, to $60,000

[31] Annuities may be those in which the family has an equity interest in the asset or in which the family possesses an entitlement only to a stream of income. The wealth figures in this article include only the annuities in which the family has an equity interest. In 2010, 5.9 percent of families reported having any type of annuity, and of these families, 77.3 percent reported having an equity interest. The trusts or managed investment accounts included in other managed assets are those in which families have an equity interest and for which component parts were not separately reported; typically, such accounts are those in which the ownership is complicated or the management is undertaken by a professional. In 2010, 88.6 percent of families with trusts or managed investment accounts had an equity interest in such an account.

The survey encourages respondents who have trusts or managed investment accounts that are held in relatively common investments to report the components separately. Of the 3.9 percent of families that reported having any kind of trust or managed investment account in 2010, 59.3 percent of them reported at least one of the component assets separately. Of families that detailed the components in 2010, 89.2 percent reported some type of financial asset, 11.5 percent reported a primary residence, 17.0 percent reported other real estate, 5.0 percent reported a business, and 2.0 percent reported another type of asset (data not shown in the tables). The fraction of these families reporting the primary residence as a component of a trust decreased 7.4 percentage points between 2007 and 2010, and the fraction reporting a business decreased 10.3 percentage points.

in 2010; for families with a trust or managed investment account as defined in this article, the median holding fell 13.3 percent, to $109,000 (data not shown in the tables).

As noted in the discussion of retirement accounts, some families use settlements from retirement accounts to purchase an annuity. In 2010, 35.0 percent of families with annuities had done so (data not shown in the tables). Of these families, 73.7 percent had an equity interest in their annuities.

Other Financial Assets

Ownership of other financial assets—a heterogeneous category including oil and gas leases, futures contracts, royalties, proceeds from lawsuits or estates in settlement, and loans made to others—fell 1.3 percentage points between 2007 and 2010, to 8.0 percent. Ownership of such assets tends to be more common among higher income and wealth groups, younger age groups, and families headed by a person who is self-employed or retired. Ownership across demographic groups generally declined over this period, while the median holding for those who had such assets decreased 20.6 percent, to $5,000.

Holdings may be grouped into four categories: cash, which includes money owed to families by other persons; future proceeds, which include amounts to be received from a lawsuit, estate, or other type of settlement; employment and business-related items, which include deferred compensation, royalties, futures contracts, and derivatives; and other. As shown in the following table, the proportion of families holding various types of other financial assets remained fairly constant over the three-year period, with cash being by far the most frequently held component:

Table 6.9

Type of other financial asset	All families	
	2010 (percent)	Change, 2007–10 (percentage points)
Cash	6.8	–1.3
Future proceeds	.8	–.1
Business items	.4	†
Other	.2	.2

† Less than 0.05 percent.

Some publicly traded companies offer stock options to their employees as a form of compensation.[32] Although stock options, when executed, may represent an appreciable part of a family's net worth, the survey does not specifically ask for the value of these options.[33] Instead, the survey asks whether the family head or that person's spouse or partner had been given stock options by an employer during the preceding year. In 2010, 6.2 percent of families reported having received stock options, a decline of 2.1 percentage points below the level in 2007; this decrease continues a downward trend since the peak of 11.4 percent recorded in the SCF in 2001 (data not shown in the tables).

[32] See Jeffrey L. Schildkraut (2004), "Stock Options: National Compensation Survey Update" (Washington: Bureau of Labor Statistics, September), www.bls.gov/opub/cwc/cm20040628yb01p1.htm.

[33] Because such options are typically not publicly traded or their execution is otherwise constrained, their value is uncertain until the exercise date; until then, meaningful valuation would require complex assumptions about the future behavior of stock prices.

Table 7. Direct and indirect family holdings of stock, by selected characteristics of families, 2001–10 surveys
Percent except as noted

Family characteristic	Families having stock holdings, direct or indirect				Median value among families with holdings (thousands of 2010 dollars)				Stock holdings as share of group's financial assets			
	2001	2004	2007	2010	2001	2004	2007	2010	2001	2004	2007	2010
All families	**52.3**	**50.3**	**53.2**	**49.9**	**42.3**	**37.7**	**35.5**	**29.0**	**56.0**	**51.4**	**54.0**	**47.0**
Percentile of income												
Less than 20	12.9	11.7	14.3	12.5	9.2	8.6	6.3	5.3	37.4	32.0	39.2	40.5
20–39.9	34.3	29.8	36.5	30.5	9.2	11.5	8.7	7.1	35.6	30.9	34.6	31.3
40–59.9	52.6	51.9	52.9	51.7	18.4	16.9	18.3	12.0	46.8	43.4	39.5	37.5
60–79.9	75.9	69.9	73.3	68.1	35.5	30.6	35.2	22.3	52.0	41.9	53.1	41.6
80–89.9	82.1	83.9	86.3	82.6	79.2	65.0	66.1	57.9	57.3	48.9	50.5	44.4
90–100	89.7	92.7	91.5	90.6	305.2	235.8	234.7	267.5	60.4	57.6	58.3	50.9
Age of head (years)												
Less than 35	49.1	40.8	41.6	39.8	8.6	9.2	6.8	7.0	52.5	40.4	45.6	39.3
35–44	59.7	54.5	55.9	50.1	33.7	23.0	25.7	19.8	57.2	53.7	54.7	50.5
45–54	59.4	56.6	63.1	58.0	61.3	57.5	47.1	37.8	59.2	53.8	54.5	48.6
55–64	57.4	63.2	60.8	59.7	98.6	80.5	81.7	56.0	56.0	55.2	55.6	48.3
65–74	40.0	46.9	53.1	45.6	184.2	80.5	58.1	78.1	55.4	51.5	55.6	44.2
75 or more	35.7	34.8	40.2	42.0	134.8	98.8	47.1	55.0	51.8	39.3	48.2	44.6
Housing status												
Owner	62.5	61.0	64.6	61.3	61.3	51.8	41.9	39.9	56.7	52.0	54.5	47.5
Renter or other	31.0	26.5	28.1	26.3	8.6	10.1	8.2	6.0	46.1	39.3	46.2	37.3

Note: Indirect holdings are those in pooled investment trusts, retirement accounts, and other managed assets. See also note to table 1.

Direct and Indirect Holdings of Publicly Traded Stocks

Families may hold stocks in publicly traded companies directly or indirectly, and information about each of these forms of ownership is collected separately in the SCF. When direct and indirect forms are combined, the 2010 data show a decline in stock ownership to levels not seen in the SCF since the late 1990s (table 7). Between 2007 and 2010, the fraction of families holding any such stock fell 3.3 percentage points to 49.9 percent, a level well below the 2007 peak. Much like ownership of directly held stock, ownership of direct and indirect equity holdings is more common among higher-income groups and among families headed by a person aged 35 to 64. Over the recent three-year period, ownership decreased for all income groups. Across age groups, ownership fell the most—7.5 percentage points—for families headed by persons aged 65 to 74; for other age groups, the declines were much more modest, and for some, ownership rates were basically unchanged or rose slightly.

The overall median value of direct and indirect stock holdings dropped 18.3 percent between 2007 and 2010. Changes in the median value across demographic groups were generally negative, with the exception of the highest income decile and families headed by a person aged less than 35 or by a person aged 65 or older. As a proportion of financial assets, holdings fell from 54.0 percent in 2007 to 47.0 percent in 2010. The lowest income quintile is the only demographic group that saw an increase in the share of financial assets held in stocks, rising from 39.2 percent in 2007 to 40.5 percent in 2010.

Among families that held equity, either directly or indirectly in 2010, ownership through a tax-deferred retirement account was most common, followed by direct holdings of stocks, direct holdings of pooled investment funds, and managed investment accounts or an equity interest in a trust or annuity. Over the 2007–10 period, ownership of equity holdings through tax-deferred accounts rose, while both direct ownership of equity and ownership through pooled investment funds fell. Ownership of equity through a trust or annuity was

basically unchanged. The fraction of equity owners with multiple types also declined, as shown in the following table:

Table 7.1

Type of direct or indirect equity	Families with equity	
	2010 (percent)	Change, 2007–10 (percentage points)
Tax-deferred account	85.9	.9
Directly held stock	30.3	–3.4
Directly held pooled investment fund	16.6	–3.7
Managed investment account, or equity interest in a trust or annuity	8.1	.3
MEMO		
Multiple types	32.8	–3.6

The distribution of amounts of holdings over these types of equities shows a different pattern. Of the total amount of equity, 42.3 percent was held in tax-deferred retirement accounts, 30.9 percent as directly held stocks, 20.4 percent as directly held pooled investment funds, and 6.4 percent as other managed assets (data not shown in the tables).

Nonfinancial Assets

By definition, a decrease in nonfinancial assets as a share of total assets from 2007 to 2010 must exactly offset the 3.9 percentage point rise in the share of financial assets from 2007 to 2010 that was discussed earlier in this article (table 5). In any given survey, the changes in these shares are driven by spending decisions, changes in portfolio choices, portfolio valuation, or all three. Between 2007 and 2010, the largest drivers were declines in house values and business equity.

Over the 2007 to 2010 period, housing as a share of total nonfinancial assets fell 0.6 percentage point, while business equity as a share of total nonfinancial assets fell 1.5 percentage points (table 8). However, housing is a much larger share of total nonfinancial assets than business equity in any given year, so the two asset types account for roughly the same share of the overall decline in the ratio of nonfinancial to total assets. That is, of the 3.9 percentage point decrease in the overall *share* of nonfinancial assets, housing and business equity each accounted for approximately 2.2 percentage points. Other residential property contributed slightly to the decline (0.2 percentage point). These drops in asset shares

Table 8. Value of nonfinancial assets of all families, distributed by type of asset, 2001–10 surveys
Percent

Type of nonfinancial asset	2001	2004	2007	2010
Vehicles[1]	5.9	5.1	4.4	5.2
Primary residence	46.9	50.3	48.0	47.4
Other residential property	8.1	9.9	10.7	11.2
Equity in nonresidential property	8.2	7.3	5.8	6.7
Business equity	29.3	25.9	29.7	28.2
Other	1.6	1.5	1.3	1.3
Total	**100**	**100**	**100**	**100**
MEMO				
Nonfinancial assets as a share of total assets	57.8	64.2	66.0	62.1

Note: See note to table 1.

[1] For definition, see text note 34.

Table 9. Family holdings of nonfinancial assets and of any asset, by selected characteristics of families and type of asset, 2007 and 2010 surveys

A. 2007 Survey of Consumer Finances

Family characteristic	Vehicles	Primary residence	Other residential property	Equity in nonresidential property	Business equity	Other	Any nonfinancial asset	Any asset
Percentage of families holding asset								
All families	**87.0**	**68.6**	**13.8**	**8.1**	**13.6**	**7.2**	**92.0**	**97.7**
Percentile of income								
Less than 20	64.4	41.4	5.4	2.5	3.3	3.9	73.5	89.8
20–39.9	85.9	55.2	6.5	3.9	5.3	5.7	91.2	98.9
40–59.9	94.3	69.3	9.9	7.5	10.6	7.4	97.2	100.0
60–79.9	95.4	83.9	15.4	9.4	18.1	7.2	98.5	100.0
80–89.9	95.6	92.6	21.0	13.6	20.0	9.0	99.6	100.0
90–100	94.8	94.3	42.2	21.0	40.9	14.1	99.7	100.0
Age of head (years)								
Less than 35	85.4	40.6	5.6	3.2	8.0	5.8	88.2	97.1
35–44	87.5	66.1	12.0	7.5	18.2	5.5	91.3	96.9
45–54	90.3	77.3	15.7	9.5	17.2	8.7	95.0	97.6
55–64	92.2	81.0	20.9	11.5	18.1	8.5	95.6	99.1
65–74	90.6	85.5	18.9	12.3	11.2	9.1	94.5	98.4
75 or more	71.5	77.0	13.4	6.8	4.5	5.8	87.3	98.1
Family structure								
Single with child(ren)	77.3	48.9	7.4	4.3	7.5	5.4	85.0	93.8
Single, no child, age less than 55	78.4	43.4	6.2	3.2	8.8	7.6	83.6	94.8
Single, no child, age 55 or more	73.7	67.5	12.1	7.1	3.6	5.9	85.0	97.6
Couple with child(ren)	94.9	78.1	15.5	9.8	18.5	6.3	97.4	99.2
Couple, no child	94.0	80.1	19.4	10.9	18.4	9.3	97.0	99.4
Education of head								
No high school diploma	73.7	52.8	5.8	2.6	5.9	2.2	80.9	91.7
High school diploma	87.5	68.9	10.0	7.3	9.5	5.1	92.2	97.7
Some college	86.7	62.3	13.2	6.5	12.7	7.0	91.0	98.6
College degree	91.9	77.8	20.6	11.9	20.7	11.0	96.6	99.6

were offset by a 0.8 percentage point increase in the share of vehicles and a 0.9 percentage point increase in the share of nonresidential property.

In 2010, the level of ownership of nonfinancial assets was 91.3 percent of families, 0.7 percentage point lower than in 2007 (first half of tables 9.A and 9.B, next-to-last column). Across most of the demographic groups shown, the 2010 ownership rate was 80 percent or more; exceptions were the lowest income and wealth groups, families headed by a person who was neither working nor retired, and renters. Over the 2007–10 period, ownership fell most for the less-than-35 age group, childless single families headed by someone younger than age 55, nonwhite or Hispanic families, families living in the South or the West, and families in the lowest quartile of the net worth distribution.

Over the recent period, the median holdings of nonfinancial assets for families having any such assets fell 16.8 percent, and the mean fell 17.6 percent. Across demographic groups, substantial declines in the medians far outnumbered increases. The largest drops in the median value occurred for the lowest quintile of the income distribution; families headed by someone with less than a high school diploma; families headed by someone working in technical, sales, or service occupations; and families in the second quartile of the net worth distribution. Median holdings inched up for a few demographic groups whose total nonfinancial holdings tend to be relatively low and that are generally not dominated by housing or business assets.

Table 9. Family holdings of nonfinancial assets and of any asset, by selected characteristics of families and type of asset, 2007 and 2010 surveys—*continued*

A. 2007 Survey of Consumer Finances—*continued*

Family characteristic	Vehicles	Primary residence	Other residential property	Equity in nonresidential property	Business equity	Other	Any nonfinancial asset	Any asset
Race or ethnicity of respondent								
White non-Hispanic	89.6	75.6	15.3	9.0	15.8	8.3	94.6	98.9
Nonwhite or Hispanic	80.9	51.9	10.0	5.9	8.2	4.3	85.8	94.9
Current work status of head								
Working for someone else	91.3	67.2	11.9	7.0	7.7	7.1	94.4	98.7
Self-employed	90.6	82.4	26.5	17.3	74.9	11.0	97.6	99.7
Retired	78.6	72.9	14.6	7.7	3.8	5.4	87.2	96.1
Other not working	69.3	33.1	3.8	4.7	3.7	8.2	74.8	90.0
Current occupation of head								
Managerial or professional	93.1	78.2	20.7	10.8	25.4	9.9	97.2	99.8
Technical, sales, or services	87.4	61.5	10.2	7.3	10.8	7.7	91.6	97.8
Other occupation	92.6	66.3	9.6	6.7	14.7	4.9	95.2	98.5
Retired or other not working	77.1	66.7	12.9	7.2	3.8	5.8	85.2	95.2
Region								
Northeast	75.4	66.1	13.3	5.6	9.1	5.5	84.2	94.6
Midwest	89.5	71.3	13.7	8.4	15.4	6.4	93.4	98.4
South	89.2	70.1	11.3	8.8	12.6	7.2	93.8	98.5
West	90.5	65.4	18.3	8.7	16.9	9.3	94.1	98.4
Urbanicity								
Metropolitan statistical area (MSA)	86.2	68.1	14.2	7.6	13.9	7.6	91.5	97.7
Non-MSA	90.9	71.1	11.7	10.7	11.8	5.1	94.3	97.9
Housing status								
Owner	93.8	100.0	17.5	10.8	17.5	8.0	100.0	100.0
Renter or other	72.3	*	5.6	2.1	5.0	5.3	74.5	92.8
Percentile of net worth								
Less than 25	69.5	13.7	*	*	2.3	2.4	71.6	91.0
25–49.9	91.2	72.2	7.1	3.7	7.5	6.4	97.7	100.0
50–74.9	93.3	92.8	11.9	7.6	13.4	7.8	99.5	100.0
75–89.9	94.5	95.2	26.4	16.5	19.6	7.3	99.0	100.0
90–100	93.6	96.8	47.5	27.2	48.3	19.0	99.6	100.0

Vehicles

Vehicles continue to be the most commonly held nonfinancial asset.[34] From 2007 to 2010, the share of families that owned some type of vehicle edged down 0.3 percentage point to 86.7 percent. Trends in ownership rates over the recent three years were mixed across most demographic groups. Across age groups, ownership decreased for the less-than-35 and 55-to-74 age groups while rising for the 75-or-more age category. Vehicle ownership decreased for single families without children headed by someone younger than age 55; families headed by a person with a high school degree, some college, or a college degree; families headed by a person who was working for someone else, self-employed, or included in any occupation group except retired; nonwhite or Hispanic families; families living in the South or the West; and renters.

[34] The definition of vehicles in this article is a broad one that includes cars, vans, sport utility vehicles, trucks, motor homes, recreational vehicles, motorcycles, boats, airplanes, and helicopters. Of families owning any type of vehicle in 2010, 99.8 percent had a car, van, sport utility vehicle, motorcycle, or truck. The remaining types of vehicles were held by 14.4 percent of families.

Table 9. Family holdings of nonfinancial assets and of any asset, by selected characteristics of families and type of asset, 2007 and 2010 surveys—*continued*

A. 2007 Survey of Consumer Finances—*continued*

Family characteristic	Vehicles	Primary residence	Other residential property	Equity in nonresidential property	Business equity	Other	Any nonfinancial asset	Any asset
Median value of holdings for families holding asset (thousands of 2010 dollars)								
All families	**16.2**	**209.5**	**154.0**	**78.6**	**96.6**	**14.7**	**185.9**	**232.1**
Percentile of income								
Less than 20	5.9	104.8	62.9	68.1	52.4	3.1	41.9	24.6
20–39.9	9.6	125.7	60.2	62.9	20.4	6.3	80.9	89.0
40–59.9	15.3	157.2	104.8	41.9	32.2	10.5	145.6	192.2
60–79.9	21.4	225.3	125.7	74.4	57.8	15.7	258.0	359.8
80–89.9	26.6	314.3	183.3	75.4	75.5	21.0	377.3	593.6
90–100	35.5	523.8	340.5	183.3	397.6	78.6	838.0	1,423.2
Age of head (years)								
Less than 35	14.0	183.3	89.1	52.4	36.7	8.7	32.3	40.7
35–44	18.3	214.8	157.2	52.4	61.8	10.5	191.3	232.9
45–54	19.6	241.0	157.2	83.8	80.5	15.7	235.6	320.6
55–64	18.2	220.0	164.5	94.3	104.8	21.0	244.2	365.1
65–74	15.3	209.5	157.2	78.6	314.3	21.0	222.3	317.8
75 or more	9.8	157.2	104.8	115.2	235.7	26.2	164.5	229.8
Family structure								
Single with child(ren)	9.0	157.2	52.4	45.1	52.4	10.5	85.2	74.4
Single, no child, age less than 55	10.3	162.4	157.2	52.4	34.0	8.7	56.6	61.5
Single, no child, age 55 or more	8.0	151.9	83.8	78.6	261.9	10.5	141.4	191.5
Couple with child(ren)	22.6	251.4	157.2	68.1	94.3	15.7	249.3	312.1
Couple, no child	20.2	220.0	188.6	104.8	104.8	24.6	240.7	342.4
Education of head								
No high school diploma	10.9	128.4	68.1	131.0	61.8	13.8	88.4	67.7
High school diploma	13.9	157.2	79.6	52.4	94.3	7.6	144.2	169.6
Some college	15.2	201.2	104.8	55.3	47.1	13.6	164.8	195.2
College degree	20.8	293.4	209.5	94.3	104.8	23.0	303.2	456.5

Note: See note to table 1.

Given the slowdown in purchases of new cars during the period between 2007 and 2010 noted earlier and the consequent aging of families' holdings of vehicles, it is not surprising that the median market value of vehicles for those who owned at least one vehicle declined 5.6 percent from 2007 to 2010, and the mean declined 4.3 percent.[35] Indeed, the median value of vehicle holdings was flat or rising only for higher-income or higher-wealth groups, families headed by someone aged 65 or older, and families in the other-not-working work-status group. The largest declines in the median were observed for the third and fourth quintiles of income, the lowest three quartiles of wealth, and families headed by someone younger than 55 years of age. Continuing a trend, the share of the total value of owned vehicles attributable to sport utility vehicles rose over the recent period from 21.5 percent to 23.8 percent (data not shown in the tables).

Some families have vehicles that they lease or that are provided to them by an employer for personal use. The share of families having a vehicle from any source fell 0.7 percentage point over the recent period, to 88.9 percent (data not shown in the tables). The small dif-

[35] Survey respondents are asked to provide the year, make, and model of each of their cars, vans, sport utility vehicles, and trucks. This information is used to obtain market prices from data collected by the National Automobile Dealers Association and a variety of other sources. For other types of vehicles, the respondent is asked to provide a best estimate of the current value.

Table 9. Family holdings of nonfinancial assets and of any asset, by selected characteristics of families and type of asset, 2007 and 2010 surveys—*continued*

A. 2007 Survey of Consumer Finances—*continued*

Family characteristic	Vehicles	Primary residence	Other residential property	Equity in nonresidential property	Business equity	Other	Any nonfinancial asset	Any asset
Race or ethnicity of respondent								
White non-Hispanic	17.9	209.5	143.0	78.6	104.8	15.7	213.8	285.2
Nonwhite or Hispanic	12.5	188.6	183.3	65.7	52.4	8.4	106.8	93.5
Current work status of head								
Working for someone else	17.8	209.5	125.7	55.3	21.0	10.5	175.1	223.5
Self-employed	23.2	314.3	314.3	159.8	110.0	52.4	476.7	569.8
Retired	11.9	162.4	104.8	78.6	157.2	13.8	163.4	213.2
Other not working	7.2	167.6	136.7	51.1	98.1	2.6	30.7	29.1
Current occupation of head								
Managerial or professional	21.2	282.9	209.5	110.0	118.8	21.0	292.2	431.0
Technical, sales, or services	15.1	209.5	131.0	89.1	26.2	15.7	162.4	195.9
Other occupation	17.5	165.4	94.3	38.8	61.8	10.5	142.0	165.1
Retired or other not working	10.9	162.4	104.8	78.6	157.2	13.1	154.5	186.0
Region								
Northeast	15.1	288.1	199.1	117.3	104.8	21.0	261.9	304.2
Midwest	15.2	162.4	115.2	55.3	104.8	10.5	165.0	214.5
South	16.3	167.6	125.7	74.9	62.9	15.7	152.7	189.6
West	17.9	314.3	225.3	94.3	99.5	14.7	263.5	308.5
Urbanicity								
Metropolitan statistical area (MSA)	16.6	230.5	157.2	86.4	98.1	14.1	203.2	255.7
Non-MSA	15.1	120.5	99.5	52.4	94.3	23.0	124.2	156.3
Housing status								
Owner	19.3	209.5	157.2	83.8	104.8	21.0	265.6	361.4
Renter or other	9.0	*	89.1	39.8	34.6	5.6	10.6	14.2
Percentile of net worth								
Less than 25	7.2	89.2	*	*	.5	1.4	9.0	8.5
25–49.9	13.7	104.8	31.4	26.2	12.0	7.9	100.4	113.4
50–74.9	18.3	209.5	62.9	41.9	52.4	13.6	240.8	319.3
75–89.9	22.9	330.0	153.0	86.4	104.8	31.4	460.1	721.6
90–100	32.8	588.6	419.1	279.4	639.1	71.2	1,215.3	2,211.1
MEMO								
Mean value of holdings for families holding asset	23.1	316.9	352.3	324.2	991.4	84.6	492.0	702.1

* Ten or fewer observations.

ference between this rate and the ownership rate for personally owned vehicles belies a larger change in the rates of holding for leased and employer-provided vehicles. The proportion of families with a leased vehicle fell from 5.2 percent in 2007 to 3.0 percent in 2010, while that of families with an employer-provided vehicle fell less dramatically, from 6.8 percent to 6.4 percent over the recent period.

Primary Residence and Other Residential Real Estate

The homeownership rate fell 1.3 percentage points over the 2007–10 period, to 67.3 percent.[36] Homeownership had fallen in the previous three-year period as well after reaching a

[36] This measure of primary residences comprises mobile homes and their sites, the parts of farms and ranches not used for a farming or ranching business, condominiums, cooperatives, townhouses, other single-family homes,

Table 9. Family holdings of nonfinancial assets and of any asset, by selected characteristics of families and type of asset, 2007 and 2010 surveys—*continued*

B. 2010 Survey of Consumer Finances

Family characteristic	Vehicles	Primary residence	Other residential property	Equity in nonresidential property	Business equity	Other	Any nonfinancial asset	Any asset
Percentage of families holding asset								
All families	**86.7**	**67.3**	**14.4**	**7.7**	**13.3**	**7.0**	**91.3**	**97.4**
Percentile of income								
Less than 20	64.9	37.2	4.4	3.9	5.1	2.7	72.0	89.9
20–39.9	85.4	55.9	7.4	5.2	6.6	4.4	90.7	98.0
40–59.9	91.8	71.1	11.6	6.3	10.6	7.3	96.0	99.5
60–79.9	95.4	80.7	16.0	7.9	15.5	9.3	98.6	99.9
80–89.9	96.4	90.6	22.8	11.4	19.3	10.8	99.4	100.0
90–100	95.7	92.4	42.1	18.8	37.6	12.3	99.4	100.0
Age of head (years)								
Less than 35	79.4	37.5	4.5	2.3	8.4	6.1	82.8	95.5
35–44	88.9	63.8	9.7	3.9	11.2	4.2	92.7	97.4
45–54	91.0	75.2	17.0	7.5	16.8	6.7	94.7	98.3
55–64	90.3	78.1	22.1	12.6	19.6	9.6	94.4	98.3
65–74	86.5	82.6	22.8	11.0	15.8	11.0	92.6	97.1
75 or more	83.4	81.9	14.6	13.4	6.0	6.0	93.0	98.7
Family structure								
Single with child(ren)	79.1	52.0	6.2	4.0	5.2	3.9	84.5	94.6
Single, no child, age less than 55	74.6	40.2	6.3	2.4	7.4	5.7	80.7	95.3
Single, no child, age 55 or more	76.3	66.7	11.8	8.2	6.6	8.0	86.8	96.6
Couple with child(ren)	94.8	75.6	15.5	7.1	17.0	5.9	97.0	99.0
Couple, no child	93.2	79.7	22.6	12.8	19.5	10.0	96.3	98.5
Education of head								
No high school diploma	76.2	54.3	5.0	3.3	5.2	1.3	82.2	92.5
High school diploma	85.8	64.7	10.0	6.9	10.9	5.5	90.5	96.5
Some college	85.4	61.5	11.7	6.4	11.2	7.6	89.6	98.2
College degree	91.5	76.6	22.4	10.4	18.9	9.9	95.9	99.5

peak of 69.1 percent of families in 2004. The 2010 homeownership rate is roughly the same as it was in 2001, which was 3.0 percentage points higher than the rate in1995 (data not shown in the tables).

In 2010, groups that had an ownership rate less than the overall rate included nonwhite or Hispanic families; families with relatively low income or wealth; families living in the Northeast or the West; single families; and families headed by a person who was working for someone else, who was neither working nor retired, who was aged less than 45, or who had less than a college degree. Over the three-year period, homeownership fell most for the lowest quintile of the income distribution; families in the second quartile of the net worth distribution; families headed by a person who was self-employed or working in a technical, sales, or service job; and families headed by a high school graduate. Across geographic regions, the decline in ownership was most pronounced in the South and West regions but also fell in the Northeast; in contrast, the Midwest saw a 2.0 percentage point increase in homeownership.

Housing wealth represents a large component of total family wealth; in 2010, primary residences accounted for 29.5 percent of total family assets. Over the 2007–10 period,

and other permanent dwellings. The 2007 and 2010 SCF estimates of homeownership differ only marginally from those of the Current Population Survey (CPS) for a comparable specification of household; the CPS shows an identical decline in the homeownership rate.

Table 9. Family holdings of nonfinancial assets and of any asset, by selected characteristics of families and type of asset, 2007 and 2010 surveys—*continued*

B. 2010 Survey of Consumer Finances—*continued*

Family characteristic	Vehicles	Primary residence	Other residential property	Equity in nonresidential property	Business equity	Other	Any nonfinancial asset	Any asset
Race or ethnicity of respondent								
White non-Hispanic	90.9	75.3	16.5	9.4	15.6	8.8	94.9	99.1
Nonwhite or Hispanic	78.1	50.6	9.9	4.2	8.3	3.3	84.0	94.1
Current work status of head								
Working for someone else	89.9	64.8	11.9	5.5	6.6	6.4	92.8	98.3
Self-employed	88.5	78.4	28.3	17.5	71.1	12.0	96.4	98.8
Retired	82.4	74.6	15.0	9.6	4.5	6.8	89.2	96.3
Other not working	72.8	42.9	8.7	2.8	4.1	4.8	78.6	92.5
Current occupation of head								
Managerial or professional	91.0	76.1	22.9	10.7	25.9	9.6	95.7	99.7
Technical, sales, or services	86.7	56.0	9.7	5.1	9.6	5.1	90.1	97.7
Other occupation	91.1	66.6	8.4	5.6	13.8	6.6	93.8	97.1
Retired or other not working	80.3	67.8	13.7	8.1	4.4	6.3	86.9	95.5
Region								
Northeast	78.5	65.0	15.3	5.9	11.1	5.5	85.6	95.1
Midwest	90.1	73.3	11.0	7.6	13.0	5.8	93.8	98.0
South	87.5	67.6	14.1	9.4	12.5	6.6	92.1	97.5
West	88.8	62.5	17.4	6.4	16.6	10.2	92.4	98.7
Urbanicity								
Metropolitan statistical area (MSA)	86.0	65.9	14.9	7.2	13.4	6.9	90.6	97.4
Non-MSA	90.2	73.9	11.9	10.1	12.3	7.8	95.0	97.8
Housing status								
Owner	93.9	100.0	19.1	10.5	17.0	8.4	100.0	100.0
Renter or other	71.9	*	4.6	1.9	5.5	4.2	73.6	92.2
Percentile of net worth								
Less than 25	67.4	21.8	2.8	.8	2.9	2.5	69.7	89.8
25–49.9	91.6	61.3	4.6	2.1	6.1	4.9	96.8	100.0
50–74.9	93.2	90.1	13.1	7.8	12.9	7.3	99.2	100.0
75–89.9	94.3	95.3	27.1	14.9	20.8	9.2	99.6	100.0
90–100	95.2	97.1	51.7	27.9	46.6	19.7	99.9	100.0

this percentage declined 2.2 percentage points overall. The relative importance of housing in the total asset portfolio varies substantially over the income distribution, with housing generally constituting a progressively smaller share of assets with increasing levels of income, as shown in the following table:

Table 9.1

Family characteristic	House value as a percentage of all assets in group	
	2010 (percent)	Change, 2007–10 (percentage points)
All families	**29.5**	**–2.2**
Percentile of income		
Less than 20	35.6	–11.5
20–39.9	50.6	–1.2
40–59.9	44.8	–3.5
60–79.9	42.7	–2.5
80–89.9	37.5	–6.9
90–100	19.2	–.6

Table 9. Family holdings of nonfinancial assets and of any asset, by selected characteristics of families and type of asset, 2007 and 2010 surveys—*continued*

B. 2010 Survey of Consumer Finances—*continued*

Family characteristic	Vehicles	Primary residence	Other residential property	Equity in nonresidential property	Business equity	Other	Any nonfinancial asset	Any asset
Median value of holdings for families holding asset (thousands of 2010 dollars)								
All families	**15.3**	**170.0**	**120.0**	**65.0**	**78.7**	**15.0**	**154.6**	**187.2**
Percentile of income								
Less than 20	5.8	89.0	82.0	36.0	25.0	5.3	23.6	15.2
20–39.9	9.3	110.0	70.0	60.0	25.3	5.0	73.5	75.4
40–59.9	13.8	135.0	82.0	60.0	44.7	10.0	131.2	159.8
60–79.9	20.1	175.0	71.0	50.0	50.0	13.0	198.3	267.0
80–89.9	27.9	250.0	120.0	58.0	82.4	22.0	311.1	448.4
90–100	35.8	475.0	320.0	200.0	455.0	35.0	756.4	1,486.7
Age of head (years)								
Less than 35	12.4	140.0	72.0	24.0	30.0	5.0	34.2	35.7
35–44	16.5	170.0	75.0	50.0	50.0	10.0	142.8	156.3
45–54	18.4	200.0	103.5	50.0	80.0	15.0	191.4	248.4
55–64	17.8	185.0	165.0	102.0	100.0	20.0	206.6	286.6
65–74	16.0	165.0	125.0	60.0	100.0	28.1	199.8	281.7
75 or more	10.6	150.0	125.0	65.0	220.9	26.0	168.2	237.7
Family structure								
Single with child(ren)	9.7	134.0	100.0	50.0	20.0	15.0	79.0	70.0
Single, no child, age less than 55	9.6	135.2	70.0	75.0	43.0	7.0	56.9	50.1
Single, no child, age 55 or more	7.5	130.0	151.0	50.0	80.3	15.0	115.5	143.9
Couple with child(ren)	21.3	190.0	120.0	60.0	75.0	12.0	193.4	233.9
Couple, no child	20.3	180.0	120.0	75.0	109.0	20.0	209.0	306.7
Education of head								
No high school diploma	9.7	95.0	75.0	30.0	27.8	5.0	59.0	47.8
High school diploma	13.3	130.0	62.5	58.0	64.1	8.0	122.2	138.4
Some college	14.5	150.0	65.0	35.0	110.0	14.4	136.2	150.1
College degree	19.5	250.0	190.0	100.0	88.0	20.0	251.5	352.6

Note: See note to table 1.

The median and mean values of the primary residences of homeowners fell between 2007 and 2010; overall, the median decreased 18.9 percent, and the mean fell 17.6 percent. These percentage losses in the median and mean translated into large dollar losses: $39,500 for the median and $55,700 for the mean. Homeowners in virtually all demographic groups saw losses in the median, and most of those losses were substantial; the one exception was the lowest quartile of the net worth distribution, where homeownership jumped 8.1 percentage points and the median home value increased 31.2 percent, most likely reflecting a compositional shift within that lowest wealth group. Otherwise, substantial decreases in median housing values were widespread.

In 2010, 14.4 percent of families owned some form of residential real estate other than a primary residence (second homes, time-shares, one- to four-family rental properties, and other types of residential properties), a level that is up 0.6 percentage point from the corresponding figure in 2007 and up 1.9 percentage points since 2004 (data not shown in the tables).[37] Although the survey does not ask directly about ownership of second homes, such homes should largely be captured as residential properties that are owned 100 percent by the family and for which no rent was collected; in 2010, 5.8 percent of families had at

[37] This measure of residential real estate also includes outstanding balances on loans that the family may have made to finance the sale of properties they previously owned, which are still owed to the family.

Table 9. Family holdings of nonfinancial assets and of any asset, by selected characteristics of families and type of asset, 2007 and 2010 surveys—*continued*

B. 2010 Survey of Consumer Finances—*continued*

Family characteristic	Vehicles	Primary residence	Other residential property	Equity in nonresidential property	Business equity	Other	Any nonfinancial asset	Any asset
Race or ethnicity of respondent								
White non-Hispanic	16.7	175.0	140.0	75.0	97.2	15.0	183.6	238.9
Nonwhite or Hispanic	12.3	139.0	70.0	50.0	43.0	10.0	86.0	76.8
Current work status of head								
Working for someone else	16.3	170.0	96.0	50.0	25.0	10.0	142.7	165.7
Self-employed	21.7	270.0	250.0	132.0	100.0	30.0	370.0	440.2
Retired	11.7	150.0	100.0	62.5	125.5	25.0	155.9	198.0
Other not working	10.7	135.0	60.0	46.6	37.6	10.0	56.7	41.0
Current occupation of head								
Managerial or professional	20.8	250.0	200.0	100.0	102.0	23.0	260.0	347.5
Technical, sales, or services	12.7	153.0	70.0	50.0	27.0	8.0	107.6	115.5
Other occupation	17.2	130.0	57.0	50.0	51.5	8.0	125.0	147.2
Retired or other not working	11.5	150.0	98.0	62.0	81.6	22.0	139.9	163.3
Region								
Northeast	16.2	260.0	154.0	65.0	70.0	30.0	220.4	260.0
Midwest	13.6	135.0	86.5	70.0	100.0	10.0	142.1	174.9
South	15.4	141.7	100.0	50.0	80.3	15.0	134.3	153.1
West	16.3	230.0	170.0	159.4	52.8	15.0	189.1	216.8
Urbanicity								
Metropolitan statistical area (MSA)	15.5	181.0	135.0	70.0	73.6	15.0	168.0	200.0
Non-MSA	14.4	100.0	75.0	60.0	104.5	12.5	111.6	140.1
Housing status								
Owner	18.8	170.0	120.0	70.0	95.0	20.0	217.0	296.2
Renter or other	8.5	*	120.0	22.5	25.0	5.3	9.7	12.6
Percentile of net worth								
Less than 25	6.9	117.0	60.0	3.0	1.2	5.0	9.4	7.4
25–49.9	11.7	95.5	25.0	10.0	11.6	5.0	60.0	69.1
50–74.9	17.7	150.0	48.0	30.0	40.0	13.0	181.6	240.3
75–89.9	22.7	250.0	120.0	65.0	125.0	20.6	360.7	583.8
90–100	32.7	531.5	350.0	250.0	600.0	50.0	1,114.3	2,082.8
MEMO								
Mean value of holdings for families holding asset	22.1	261.2	288.9	321.6	788.3	66.5	405.5	612.3

* Ten or fewer observations.

least one such property, down 0.3 percentage point from 2007 but still 1.2 percentage points higher than in 2004.

Ownership of other residential real estate is more common among the highest income and wealth groups; the age groups between 45 and 74; or families headed by a self-employed person, a person working in a management or professional occupation, or a person who was a college graduate. Over the recent three-year period, the median and mean values of other residential real estate decreased roughly in line with the median and mean values of primary residences over the recent period; the median for those having such real estate fell 22.1 percent, and the mean fell 18.0 percent. Most of the demographic groups saw substantial declines in the median; exceptions were generally groups where ownership of other residential real estate is low, including the first and second quintiles of income groups,

families headed by someone with less than a high school degree, and families that rented their primary residence.

Net Equity in Nonresidential Real Estate

The ownership of nonresidential real estate fell slightly, to 7.7 percent of families in 2010.[38] Ownership follows approximately the same relative distribution across demographic groups as does the ownership of other residential real estate. Changes in ownership during the recent period were mixed across demographic groups. Ownership fell most for families in the age groups between 35 and 54; couples with children; families headed by someone working in a technical, sales, or service occupation; and families living in the West region. Overall, the median value of such property for owners fell 17.3 percent, and the mean fell 0.8 percent. Particularly large swings in the median value were seen for groups with below-average ownership rates, suggesting that these changes are likely to be due at least in part to sampling variability.

Net Equity in Privately Held Businesses

The share of families that owned a privately held business interest edged down 0.3 percentage point during the recent period, to 13.3 percent in 2010.[39] The proportion has changed little over the past several surveys. Ownership of this type of asset tends to increase with income, wealth, and education and to be the highest for families headed by a person who is aged 45 to 64, who is married or living with a partner, or who has a college degree. Business ownership is about three times as prevalent among homeowners as renters; it is generally lowest in the Northeast and highest in the West. Over the recent three-year period, changes in ownership varied across demographic groups, with relatively large declines observed for families headed by someone 35 to 44 years of age, higher-income families, and families living in the Midwest region. Ownership also fell among families headed by a person who was self-employed, from 74.9 percent in 2007 to 71.1 percent in 2010.

As noted earlier, equity in privately held businesses makes up a large portion of families' total nonfinancial assets. Over the recent period, privately held business assets as a share of nonfinancial assets fell 2.1 percentage points. Across income-distribution groups, the share of nonfinancial assets attributable to business equity has a U-shape, with the largest shares at the top and bottom of the income distribution, as shown in the following table:

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[38] Nonresidential real estate comprises the following types of properties unless they are owned through a business: commercial property, rental property with five or more units, farm and ranch land, undeveloped land, and all other types of nonresidential real estate. Most often, nonresidential real estate properties are functionally more like a business than a residential property. They may have several owners, they are typically worth a considerable amount, and they often carry large mortgages, which appear to be paid from the revenues from the property, not the family's other income. As in the case of privately owned businesses, the value of the property in this analysis is taken to be the net value.

[39] The forms of business in this category are sole proprietorships, limited partnerships, other types of partnerships, subchapter S corporations and other types of corporations that are not publicly traded, limited liability companies, and other types of private businesses. If the family surveyed lived on a farm or ranch that was used at least in part for agricultural business, the value of that part, net of the corresponding share of associated debts, is included with other business assets.

In the survey, self-employment status and business ownership are independently determined. Among the 13.3 percent of families with a business in 2010, 71.5 percent had a family head or the spouse or partner of the head who was self-employed; among the 13.3 percent of families in which either the head or the spouse or partner of the head was self-employed, 71.2 percent owned a business (data not shown in the tables).

Table 9.2

Family characteristic	Net equity in business as a percentage of all assets	
	2010 (percent)	Change, 2007–10 (percentage points)
All families	**17.5**	**–2.1**
Percentile of income		
Less than 20	19.5	.7
20–39.9	7.6	3.3
40–59.9	7.3	–1.8
60–79.9	7.9	1.1
80–89.9	8.1	–3.3
90–100	24.6	–3.4

The median holding of business equity for those having any such equity declined 18.5 percent, while the mean decreased 20.5 percent. The mean value in 2010 is 4.1 percent above its level in 2004, and the median is 8.8 percent lower than it was in 2004 (data not shown in the tables). In general, median business equity increases across income, age, and net worth groups, and the medians for white non-Hispanic families and homeowners are substantially higher than for the complementary groups. Over the recent three-year period, large increases in median net equity in businesses were observed in the second, third, and fifth income quintiles; the bottom wealth quartile; and the South region. There were large declines in median holdings for families in the lowest income quintile and in the West and Northeast regions.

The SCF classifies privately owned business interests into those in which the family has an active management role and those in which it does not. Of families having any business interests in 2010, 94.0 percent had an active role, and 10.1 percent had a non-active role; 4.1 percent had interests of both types (data not shown in the tables). In terms of assets, actively managed interests accounted for 87.5 percent of total privately owned business interests. The median number of actively managed businesses was 1. The businesses reported in the survey were a mixture of very small businesses with moderate values and businesses with substantially greater values.

The SCF attempts to collect information about items owned or owed by a family's business interests separately from items owned or owed directly by the family. But, in practice, the balance sheet of a business that is actively managed by a family is not always separate from that of the family itself.[40] Families often use personal assets as collateral or guarantees for loans for the businesses, or they loan personal funds to their businesses. In 2010, 18.2 percent of families with actively managed businesses reported using personal assets as collateral, which is up slightly from 17.8 percent in 2007; at the same time, 15.2 percent of families reported lending the business money, which is down from 17.5 percent in 2007 (data not shown in the tables).

Families with more than one actively managed business are asked to report which business is most important; that business is designated as the primary one.[41] In 2010, the vast majority of primary businesses operated in an industry other than manufacturing; the most common organizational form of those businesses was sole proprietorship, and the median number of employees was 2. However, primary actively managed businesses with more than two

[40] Technically, in a sole proprietorship, there is no legal distinction between the balance sheet of the business and that of its owner.

[41] For families with only one business, that business is, by default, considered the primary one. In 2010, primary actively managed businesses accounted for 76.3 percent of the value of all actively managed businesses.

employees accounted for 79.5 percent of the value of all such businesses, and the largest shares of value were attributable to businesses organized as subchapter S corporations or limited liability companies, each of which accounted for approximately 30 percent. These patterns are also typical of those observed in the earlier surveys (data not shown in the tables).

Other Nonfinancial Assets

In 2010, ownership of the remaining nonfinancial assets (tangible items including substantial holdings of artwork, jewelry, precious metals, antiques, hobby equipment, and collectibles) was not very widespread and decreased marginally compared with the level in the previous survey period, to 7.0 percent. Among other nonfinancial assets, the most commonly held items are antiques and other collectibles, which were reported by only 3.0 percent of families in 2010. The composition of other nonfinancial assets changed little from 2007 to 2010, as shown in the following table:

Table 9.3

Type of other nonfinancial asset	All families	
	2010 (percent)	Change, 2007–10 (percentage points)
Gold, silver, or jewelry	2.3	.2
Antiques, collectibles	3.0	–.5
Art objects	1.6	–.2
Other	1.4	.5

Groups most likely to hold other nonfinancial assets generally include families in the top two deciles of the income distribution, families headed by a college graduate, homeowners, and families in the top quartile of the net worth distribution. Minor changes in holdings were evident across all of the demographic groups. For families having such assets, the median value rose 2.0 percent over the recent period, and the mean fell 21.4 percent. Across income and wealth categories, median holdings generally fell for families in middle and top groups.

Unrealized Capital Gains

Changes in the values of assets such as stock, real estate, and businesses that families own are often a key determinant of changes in their net worth. Unrealized gains are net changes in the value of assets that are yet to be sold; such "gains" may be positive or negative. To obtain information on this part of net worth, the survey asks about changes in value from the time of purchase for certain key assets—publicly traded stocks, pooled investment funds, the primary residence, and other real estate. In addition, it asks about the tax cost basis of any business holdings, and this figure, along with the current value, may be used as a credible indicator of unrealized gains.[42] Among families with any unrealized capital gain, the median value of that gain fell 52.7 percent over the 2007–10 period, and the mean fell 39.1 percent (table 10). These declines pushed unrealized capital gains as a share of total family assets down to 24.5 percent, well below the peak of 36.1 percent observed in 2007. The decrease in median and mean unrealized gains was universal across the types of families and assets considered here. The median of unrealized gains on real estate fell 50.5 percent, the median on business assets declined 23.7 percent, and the median of unrealized

[42] The survey does not collect information on capital gains on every asset for which such gains are possible. Most important, it does not collect such information for retirement accounts.

Table 10. Family holdings of unrealized capital gains on selected assets as a share of total assets, by selected characteristics of families, 2001–10 surveys

Percent except as noted

Family characteristic	2001				2004				2007				2010			
	Real estate	Business	Financial	All	Real estate	Business	Financial	All	Real estate	Business	Financial	All	Real estate	Business	Financial	All
All families	**15.4**	**11.6**	**2.3**	**29.3**	**19.3**	**10.9**	**1.1**	**31.2**	**19.3**	**14.2**	**2.6**	**36.1**	**12.8**	**10.6**	**1.1**	**24.5**
Percentile of income																
Less than 20	26.7	2.0	–.1	28.6	29.4	7.7	–.6	36.5	30.6	10.6	1.4	42.7	22.8	8.5	.3	31.6
20–39.9	27.2	3.9	–.3	30.9	28.8	5.9	.3	35.0	31.6	3.2	.3	35.1	23.7	4.3	–.2	27.8
40–59.9	18.9	3.9	.2	22.9	25.9	3.0	.5	29.4	24.7	5.6	.8	31.1	18.5	3.8	.2	22.4
60–79.9	17.3	5.2	1.7	24.3	23.4	4.0	.5	27.9	23.4	3.8	1.6	28.9	14.2	3.8	†	17.9
80–89.9	15.9	7.8	1.8	25.5	19.7	4.4	.8	24.9	23.9	8.8	.9	33.6	13.8	4.9	–.2	18.5
90–100	12.3	16.9	3.3	32.5	15.1	16.6	1.6	33.2	14.5	20.8	3.9	39.1	9.3	15.6	2.1	27.0
Age of head (years)																
Less than 35	8.2	10.7	2.1	20.9	13.4	7.5	–.4	20.4	12.6	14.6	1.0	28.2	2.6	9.6	–1.3	10.9
35–44	12.7	14.8	.2	27.7	16.8	11.9	1.4	30.2	16.2	12.3	.4	29.0	5.9	9.4	.6	15.8
45–54	13.1	12.6	2.0	27.7	16.6	13.4	1.1	31.1	18.6	15.5	2.1	36.2	9.7	13.7	1.0	24.5
55–64	14.8	12.4	2.0	29.2	19.8	11.8	†	31.5	18.0	15.3	3.2	36.5	13.3	10.8	1.4	25.5
65–74	21.2	10.3	3.5	35.0	22.0	8.8	2.1	32.9	21.1	13.8	4.0	38.8	15.2	10.3	.8	26.3
75 or more	21.9	5.1	5.2	32.2	27.5	5.5	2.4	35.3	29.6	11.0	4.1	44.7	23.8	6.0	2.6	32.5
MEMO																
Percent of families with any such gains	67.2	11.6	27.6	72.1	68.8	11.1	25.1	73.0	69.0	11.5	21.7	72.4	66.7	11.3	17.3	70.2
Median for those with any such gains	47.3	62.5	.6	49.0	63.9	51.8	.8	62.1	74.4	52.4	3.7	78.6	36.8	40.0	.3	37.2
Mean for those with any such gains	126.9	555.7	46.0	224.9	170.4	594.7	25.4	259.7	192.4	843.5	83.1	342.8	114.3	563.8	39.1	208.7

Note: See note to table 1.

† Less than 0.05 percent.

gains on the financial assets covered in this measure fell 91.9 percent, to $300 in 2010; the mean of unrealized gains in real estate fell 40.6 percent, the mean on business assets declined 33.2 percent, and the mean of unrealized gains on financial assets fell 52.9 percent.

Some families saw losses on the value of their assets sufficient to eliminate any prior gains. Among all families in 2010, 15.1 percent reported a net loss on their primary residence or other real estate, meaning the value they reported for the property in 2010 was below what they reported having paid for it, regardless of when they made the purchase. That rate is nearly triple the 5.5 percent of families reporting a capital loss on their primary residence in 2007 and more than triple the 4.3 percent of families in 2004 (data not shown in the tables).

Liabilities

The composition of family debt shifted between 2007 and 2010. Debt secured by a primary residence remained the largest component of overall family debt, but its share slipped 0.6 percentage point between the most recent surveys (table 11).[43] This decline in mortgage debt was reinforced by a 0.3 percentage point decrease in the fraction of debt secured by

[43] The SCF measure of liabilities excludes debt owed by businesses owned by the family and debt owed on non-residential real estate; in this article, such debt is netted against the corresponding assets.

Table 11. Amount of debt of all families, distributed by type of debt, 2001–10 surveys
Percent

Type of debt	2001	2004	2007	2010
Secured by residential property				
Primary residence	75.2	75.2	74.7	74.1
Other	6.2	8.5	10.1	9.8
Lines of credit not secured by residential property	.5	.7	.4	1.0
Installment loans	12.3	11.0	10.2	11.1
Credit card balances	3.4	3.0	3.5	2.9
Other	2.3	1.6	1.1	1.1
Total	**100**	**100**	**100**	**100**

Note: See note to table 1.

residential property other than the primary residence. The share of outstanding credit card balances also decreased 0.6 percentage point over the three-year period. Offsetting these relative declines in mortgage and credit card debt were increases in the share of liabilities accounted for by nonmortgage lines of credit and other installment loans.

The overall value of families' liabilities decreased between 2007 and 2010, but the rate of decline was less than the corresponding rate for families' assets. Accordingly, the ratio of the sum of the debt of all families to the sum of their assets—the leverage ratio—rose from 14.8 percent in 2007 to 16.4 percent in 2010 (table 12). The leverage ratio for the subset of families that had any debt rose at a faster pace, from 19.4 percent in 2007 to 22.0 percent in 2010 (data not shown in the tables).

The overall leverage ratio differs considerably across types of family groups. It rises and then falls across income groups. By comparison, the ratio declines with age, a result consistent with the expected life-cycle patterns of asset and debt accumulation. These general patterns in the leverage ratios among groups hold across survey years, and the proportional increase in leverage ratios in the most recent period was fairly uniform across income and age groups.

Holdings of Debt

The share of families with any type of debt decreased 2.1 percentage points to 74.9 percent over the 2007–10 period (first half of tables 13.A and 13.B, last column), reversing an increase that had taken place since 2001. In any given survey year, borrowing is less prevalent among childless single families headed by a person aged 55 or older and families headed by a person who is retired or is aged 75 or older. Families in the lowest income, wealth, and education groups—which tend to have fewer economic resources—are also less likely to have any debt. Across income groups, borrowing rates peak among families above the median. By net worth group, debt ownership also peaks among families in the third quartile. Families in the highest three income groups, couples with children, and families headed by a person employed in a managerial or professional position have comparatively high rates of debt ownership.

With few exceptions, the fraction of families with any debt fell broadly across demographic groups. By age groups, debt ownership fell for those in the less than 35, 45-to-54, and 55-to-64 age groups but rose for the 75-or-older group. Debt ownership fell for most income groups, but the lowest quintile saw an increase of 0.8 percentage point. Similarly, debt ownership rose 0.4 percentage point for the lowest wealth quartile. The percentage of families with debt decreased just 0.9 percentage point for white non-Hispanic families but

Table 12. Leverage ratio of group by selected family characteristics, 2001–10 surveys
Percent

Family characteristic	2001	2004	2007	2010
All families	12.0	15.0	14.8	16.4
Percentile of income				
Less than 20	13.5	15.1	13.5	18.3
20–39.9	14.5	19.4	18.6	21.4
40–59.9	19.2	23.2	24.3	26.5
60–79.9	18.0	21.6	25.3	27.7
80–89.9	18.1	22.7	23.3	23.0
90–100	7.4	9.1	8.3	9.8
Age of head (years)				
Less than 35	33.5	46.4	44.3	51.6
35–44	22.6	26.0	28.1	37.3
45–54	13.5	17.3	16.3	19.7
55–64	7.1	9.3	10.2	11.0
65–74	4.2	5.2	6.5	7.8
75 or more	1.8	4.0	2.2	3.9
Education of head				
No high school diploma	13.4	14.0	18.2	20.3
High school diploma	16.1	19.3	20.5	20.9
Some college	15.0	19.4	19.1	23.3
College degree	10.4	13.2	12.5	14.3
Race or ethnicity of respondent				
White non-Hispanic	11.0	13.4	12.8	14.4
Nonwhite or Hispanic	23.4	27.2	27.0	29.1
Region				
Northeast	10.2	12.8	12.7	14.7
Midwest	13.0	14.3	14.4	17.7
South	11.4	15.2	14.3	15.5
West	13.8	17.1	17.4	17.9
Urbanicity				
Metropolitan statistical area (MSA)	12.0	14.7	14.6	16.2
Non-MSA	13.2	17.7	17.2	18.7
Housing status				
Owner	11.9	14.9	14.7	16.2
Renter or other	14.2	16.7	17.7	21.7
Percentile of net worth				
Less than 25	99.7	107.4	108.4	128.7
25–49.9	47.9	54.1	56.4	64.5
50–74.9	26.2	33.3	31.7	35.4
75–89.9	14.4	16.2	17.5	17.9
90–100	4.8	6.4	6.1	6.8

fell 4.7 percentage points for nonwhite or Hispanic families. Families headed by a self-employed person saw a decrease in debt ownership of 4.8 percentage points, whereas the fraction fell more modestly or increased among families in the complementary work-status categories.

The overall median and mean values of outstanding debt for families that had any such debt were little changed between 2007 and 2010; the median rose 0.1 percent, while the mean fell 1.1 percent. Median debt tends to rise with income, education, and wealth; the median by age peaks among families headed by a person aged 35 to 44; median debt is also higher for couples, homeowners, and families headed by a self-employed person or a person working in a managerial or professional position. Over the recent three-year period, changes in the median amount of outstanding debt varied substantially across demographic subgroups. One consistent impression from the data is a marked increase in the amount of debt held by older families; median debt rose substantially in percentage terms for families headed by someone aged 55 or older—especially childless single families

Table 13. Family holdings of debt, by selected characteristics of families and type of debt, 2007 and 2010 surveys

A. 2007 Survey of Consumer Finances

Family characteristic	Secured by residential property		Installment loans	Credit card balances	Lines of credit not secured by residential property	Other	Any debt
	Primary residence	Other					
Percentage of families holding debt							
All families	**48.7**	**5.5**	**46.9**	**46.1**	**1.7**	**6.8**	**77.0**
Percentile of income							
Less than 20	14.9	1.1	27.8	25.7	*	3.9	51.7
20–39.9	29.6	1.9	42.4	39.5	1.8	6.8	70.2
40–59.9	50.5	2.6	53.9	54.8	*	6.4	83.8
60–79.9	69.7	6.9	59.2	62.1	2.1	8.7	90.9
80–89.9	80.8	8.5	57.4	55.8	*	9.6	89.6
90–100	76.4	21.9	45.0	40.6	2.1	7.0	87.6
Age of head (years)							
Less than 35	37.3	3.3	65.2	48.5	2.1	5.9	83.6
35–44	59.5	6.5	56.2	51.7	2.2	7.5	86.2
45–54	65.5	8.0	51.9	53.6	1.9	9.8	86.8
55–64	55.3	7.8	44.6	49.9	1.2	8.7	81.8
65–74	42.9	5.0	26.1	37.0	1.5	4.4	65.5
75 or more	13.9	.6	7.0	18.8	*	1.3	31.4
Family structure							
Single with child(ren)	38.3	2.7	50.2	45.3	2.6	10.1	78.0
Single, no child, age less than 55	35.0	3.5	44.1	42.9	*	7.0	76.9
Single, no child, age 55 or more	22.0	1.9	18.9	30.2	*	3.7	48.2
Couple with child(ren)	69.0	8.4	62.9	54.7	2.0	7.9	91.1
Couple, no child	51.3	6.6	43.6	46.7	1.5	5.7	76.0
Education of head							
No high school diploma	26.0	1.9	33.3	26.9	*	5.3	55.5
High school diploma	45.0	3.2	46.0	46.8	1.4	6.4	75.1
Some college	46.9	6.4	54.3	51.0	2.2	9.3	80.8
College degree	61.7	8.7	49.1	50.2	1.7	6.5	85.1

headed by someone aged 55 or older—and for families headed by someone who was retired. Relatively large proportional decreases in the median amount of debt were widespread. Families headed by a person aged 45 to 54 saw a decrease of 8.7 percent, families headed by someone who was self-employed saw an 8.2 percent decrease, and couples with children saw their median debt fall 11.0 percent. Debt fell 17.8 percent among families headed by a person who worked in a technical, sales, or service job and 13.0 percent among nonwhite or Hispanic families. The median decreased 6.6 percent in the South region and 7.8 percent in the West region, the two areas hardest hit by the large decline in house values.

Mortgages and Other Borrowing on the Primary Residence

Paralleling the drop in homeownership discussed earlier, the share of families with debt secured by a primary residence (hereafter, home-secured debt) declined in the most recent period, ending a long upward trend dating back to at least the 1989 SCF.[44] The fraction of

[44] Home-secured debt consists of first-lien and junior-lien mortgages and home equity lines of credit secured by the primary residence. For purposes of this article, first- and junior-lien mortgages consist only of closed-end loans—that is, loans typically with a one-time extension of credit, a set frequency of repayments, and a required repayment size that may be fixed or vary over time in accordance with a pre-specified agreement or with changes in a given market interest rate. As a type of open-ended credit, home equity lines typically allow credit extensions at the borrower's discretion subject to a prearranged limit and allow repayments at the borrower's discretion subject to a prearranged minimum size and frequency.

Table 13. Family holdings of debt, by selected characteristics of families and type of debt, 2007 and 2010 surveys—*continued*

A. 2007 Survey of Consumer Finances—*continued*

Family characteristic	Secured by residential property		Installment loans	Credit card balances	Lines of credit not secured by residential property	Other	Any debt
	Primary residence	Other					
Race or ethnicity of respondent							
White non-Hispanic	52.1	5.8	46.1	45.1	1.6	6.7	76.8
Nonwhite or Hispanic	40.4	4.8	48.9	48.4	2.0	7.0	77.7
Current work status of head							
Working for someone else	56.7	5.4	57.5	53.7	1.9	8.7	86.2
Self-employed	64.8	15.1	43.9	48.9	3.6	4.7	86.8
Retired	27.0	2.6	23.6	28.2	.8	3.2	52.3
Other not working	25.5	*	42.9	36.9	*	7.5	69.9
Current occupation of head							
Managerial or professional	67.6	10.0	56.2	52.7	1.8	7.0	90.9
Technical, sales, or services	49.7	4.5	52.2	53.2	2.7	7.9	81.8
Other occupation	53.6	5.1	57.8	53.2	2.1	9.7	84.9
Retired or other not working	26.7	2.5	26.6	29.6	.7	3.9	55.0
Region							
Northeast	48.4	4.9	40.7	44.3	*	5.6	73.3
Midwest	51.0	5.2	47.9	45.5	1.9	7.0	78.3
South	46.6	4.6	48.5	43.5	1.7	6.9	75.3
West	49.9	8.1	48.4	52.4	2.7	7.5	81.6
Urbanicity							
Metropolitan statistical area (MSA)	49.7	6.1	46.0	46.3	1.8	6.6	77.4
Non-MSA	43.5	2.9	51.3	44.8	1.6	8.0	75.1
Housing status							
Owner	70.9	6.9	46.1	50.1	1.3	6.8	82.4
Renter or other	*	2.6	48.6	37.3	2.8	6.9	65.4
Percentile of net worth							
Less than 25	11.0	*	54.2	41.0	2.6	6.7	68.8
25–49.9	56.2	3.2	52.2	52.9	1.3	8.2	82.5
50–74.9	64.4	4.9	46.2	51.7	1.6	7.4	80.3
75–89.9	63.7	8.5	39.7	44.0	1.5	3.8	76.8
90–100	62.3	21.8	28.2	30.7	1.5	6.8	76.1

families with home-secured debt fell 1.7 percentage points, slightly faster than the 1.3 percentage point drop in homeownership itself. Because the fraction of families with home-secured debt fell slightly more than homeownership, the fraction of homeowners with a mortgage also fell somewhat, from 70.9 percent in 2007 to 69.9 percent in 2010.

Families in groups with higher levels of income, education, or wealth are generally more likely to have mortgage debt, as are couples and families headed by a person who is employed in a managerial or professional job or who is self-employed. Across age groups, the rate of borrowing peaks among families in the 45-to-54 age group and declines sharply among older age groups.[45] White non-Hispanic families are more likely to have home-secured debt than are nonwhite or Hispanic families.[46] Between 2007 and 2010, the prevalence of home-secured debt fell the most for families with higher levels of income, and it also fell for families headed by a person who was self-employed or employed in a technical, sales, or service occupation and for families headed by a person younger than age 75; the

[45] Of the families that owned a home, the fraction of homeowners with mortgage debt was highest among families in the two youngest age groups in 2010—both over 90 percent.

[46] This pattern reverses, however, when considering only homeowners; for example, in 2010, 68.8 percent of white non-Hispanic homeowners had a mortgage, compared with 73.3 percent of nonwhite or Hispanic homeowners (data not shown in the tables).

Table 13. Family holdings of debt, by selected characteristics of families and type of debt, 2007 and 2010 surveys—*continued*

A. 2007 Survey of Consumer Finances—*continued*

Family characteristic	Secured by residential property		Installment loans	Credit card balances	Lines of credit not secured by residential property	Other	Any debt
	Primary residence	Other					
Median value of holdings for families holding debt (thousands of 2010 dollars)							
All families	**112.1**	**104.8**	**13.6**	**3.1**	**4.0**	**5.2**	**70.6**
Percentile of income							
Less than 20	41.9	73.3	6.8	1.0	*	3.1	9.4
20–39.9	53.4	44.0	10.3	1.9	1.4	4.2	18.9
40–59.9	92.9	72.1	13.4	2.5	*	4.2	57.1
60–79.9	120.5	87.0	17.1	4.2	5.4	5.6	116.7
80–89.9	171.8	131.0	18.1	5.8	*	5.2	190.9
90–100	210.6	154.5	19.2	7.9	18.2	7.9	246.2
Age of head (years)							
Less than 35	141.8	81.7	15.7	1.9	1.0	4.7	37.9
35–44	134.1	106.4	14.2	3.7	4.8	5.2	111.2
45–54	115.2	85.9	13.5	3.8	6.3	4.7	100.5
55–64	89.1	136.2	11.4	3.8	10.5	6.3	63.2
65–74	72.3	131.0	10.8	3.1	31.4	5.2	42.0
75 or more	41.9	52.4	8.4	.8	*	4.7	13.6
Family structure							
Single with child(ren)	97.4	89.1	10.3	1.6	2.6	5.2	31.1
Single, no child, age less than 55	102.7	82.2	10.5	2.0	*	3.1	32.5
Single, no child, age 55 or more	53.4	141.4	6.9	2.4	*	4.2	15.9
Couple with child(ren)	136.2	97.4	15.6	4.2	5.2	5.6	126.8
Couple, no child	102.7	131.0	16.3	3.5	4.0	5.2	74.2
Education of head							
No high school diploma	52.4	55.8	9.2	1.6	*	4.2	20.4
High school diploma	88.0	85.9	10.7	2.4	1.4	4.7	41.9
Some college	101.6	83.8	12.6	3.0	4.0	5.2	57.0
College degree	149.5	131.0	18.2	4.2	6.3	6.3	130.3

Note: See note to table 1.

* Ten or fewer observations.

proportion of families with home-secured debt increased for the oldest age group and for childless single families headed by someone aged 55 or older.

Overall, the median amount of home-secured debt fell 2.2 percent from 2007 to 2010, and the mean fell 1.2 percent; these decreases reverse long-term trends, as both the median and mean had risen nearly 50 percent in the decade preceding the most recent period.

Among families with home-secured debt, median home equity (the difference between the value of a home and any debts secured against it) fell from $95,300 in 2007 to $55,000 in 2010, a 42.3 percent decrease (data not shown in the tables).[47] Among those with such debt, the median ratio of home-secured debt to the value of the primary residence rose 11.3 percentage points, to 64.6 percent in 2010. Over the recent three-year period, an SCF-based estimate of the aggregate ratio of home-secured debt to home values for all homeowners jumped to 41.3 percent; that ratio was 34.9 percent in 2007. At the time of the 2010 SCF interview, 8.1 percent of all homeowners had home-secured debt greater than the

[47] Among all homeowners in 2010, median home equity was $75,000; in 2007, it had been $110,000.

Table 13. Family holdings of debt, by selected characteristics of families and type of debt, 2007 and 2010 surveys—*continued*

A. 2007 Survey of Consumer Finances—*continued*

Family characteristic	Secured by residential property		Installment loans	Credit card balances	Lines of credit not secured by residential property	Other	Any debt
	Primary residence	Other					
Race or ethnicity of respondent							
White non-Hispanic	111.1	95.2	14.0	3.5	5.2	5.2	80.1
Nonwhite or Hispanic	118.4	120.2	12.6	2.1	.8	5.2	46.0
Current work status of head							
Working for someone else	122.6	93.2	14.2	3.1	3.0	5.2	86.0
Self-employed	141.4	158.8	16.2	4.5	5.2	10.5	128.5
Retired	49.3	104.8	9.1	1.6	6.7	4.7	21.0
Other not working	94.3	*	11.2	1.9	*	8.4	22.9
Current occupation of head							
Managerial or professional	155.1	136.2	17.1	4.7	9.4	7.3	144.1
Technical, sales, or services	105.7	110.0	12.8	3.1	3.7	4.2	69.0
Other occupation	98.5	62.9	12.6	2.6	4.2	5.0	67.2
Retired or other not working	55.5	104.8	10.2	1.6	6.7	5.2	21.0
Region							
Northeast	112.1	99.5	12.6	3.1	*	6.8	69.8
Midwest	98.4	86.5	11.5	3.1	5.2	5.2	64.1
South	103.7	83.8	13.8	2.9	3.3	4.7	63.8
West	157.9	167.6	14.9	3.2	4.0	6.3	100.1
Urbanicity							
Metropolitan statistical area (MSA)	123.8	105.8	13.9	3.1	3.7	5.2	81.8
Non-MSA	63.5	73.3	12.2	2.1	6.3	5.2	31.2
Housing status							
Owner	112.1	104.8	14.8	3.8	7.9	5.2	116.4
Renter or other	*	83.8	10.8	1.4	1.0	5.2	9.6
Percentile of net worth							
Less than 25	112.1	*	11.9	1.6	1.0	5.2	12.4
25–49.9	88.2	77.5	13.6	2.9	2.1	4.1	67.3
50–74.9	109.0	75.4	14.6	3.8	4.4	5.2	102.9
75–89.9	134.1	98.5	12.6	4.2	10.7	5.2	133.0
90–100	188.6	167.6	17.9	5.2	45.1	15.7	215.2
MEMO							
Mean value of holdings for families holding debt	156.1	185.7	22.0	7.7	26.0	16.2	132.0

reported value of their primary residence; among the group with home-secured debt, the figure was 11.6 percent.

Mortgage interest rates fell dramatically over the 2007–10 period to a level well below prevailing rates in the 1990s, approaching historical lows. Low interest rates and the deductibility of interest payments on mortgage debt provide an incentive for families to borrow against the equity in their home, but the decrease in home values and tighter lending standards following the financial crisis worked against the incentive. Borrowing against home equity may take the form of refinancing an existing first-lien mortgage for more than the outstanding balance, obtaining a junior-lien mortgage, or accessing a home equity line of credit. The survey provides detailed information on all of these options for home equity borrowing. The share of homeowners who had a first lien increased slightly—0.3 percentage point—to 66.4 percent in 2010 (table 14). The fraction of homeowners with a junior-lien mortgage fell 2.7 percentage points—to 5.8 percent in 2010, a level lower than any seen in the SCF since at least the 1989 survey. The proportion of homeowners who had a home equity line of credit decreased 3.1 percentage points, to 15.3 percent in 2010, and the share of homeowners with an outstanding balance fell 2.3 percentage points to 10.3 percent; the

Table 13. Family holdings of debt, by selected characteristics of families and type of debt, 2007 and 2010 surveys—*continued*

B. 2010 Survey of Consumer Finances

Family characteristic	Secured by residential property		Installment loans	Credit card balances	Lines of credit not secured by residential property	Other	Any debt
	Primary residence	Other					
Percentage of families holding debt							
All families	**47.0**	**5.3**	**46.3**	**39.4**	**2.1**	**6.4**	**74.9**
Percentile of income							
Less than 20	14.8	1.3	34.1	23.2	1.2	4.2	52.5
20–39.9	29.6	1.7	40.8	33.4	2.2	4.2	66.8
40–59.9	51.6	3.5	49.9	45.0	2.1	6.8	81.8
60–79.9	65.4	6.0	56.6	53.1	1.9	7.8	86.9
80–89.9	74.5	9.1	58.8	51.0	2.0	11.8	88.9
90–100	72.8	19.4	41.8	33.6	3.7	6.6	84.5
Age of head (years)							
Less than 35	34.0	2.9	61.9	38.7	1.8	5.5	77.8
35–44	57.6	5.1	60.0	45.6	2.2	8.6	86.0
45–54	60.4	7.6	49.8	46.2	2.7	9.7	84.1
55–64	53.6	7.6	40.7	41.3	3.0	6.7	77.7
65–74	40.5	5.0	30.4	31.9	1.2	2.3	65.2
75 or more	24.2	2.9	12.3	21.7	*	2.0	38.5
Family structure							
Single with child(ren)	36.0	2.6	49.4	35.3	1.2	6.7	73.5
Single, no child, age less than 55	31.8	2.7	48.0	37.2	2.3	5.7	73.3
Single, no child, age 55 or more	29.0	3.2	20.4	26.9	1.0	2.5	52.2
Couple with child(ren)	64.9	7.3	59.6	47.4	2.8	8.8	87.5
Couple, no child	49.5	6.9	43.0	40.1	2.1	6.2	74.5
Education of head							
No high school diploma	27.2	*	34.7	27.7	1.6	4.8	56.4
High school diploma	42.0	2.8	44.0	36.9	1.7	6.4	70.6
Some college	44.8	4.7	55.1	45.8	2.3	7.4	80.2
College degree	58.7	9.2	47.7	42.1	2.4	6.4	82.0

median amount borrowed against such lines rose from $25,100 in 2007 to $26,400 in 2010 (data not shown in the tables).[48] Overall, the share of total home-secured debt that was attributable to outstanding balances on first liens and home equity lines of credit rose across the 2007 and 2010 surveys. The share of home-secured debt attributable to first liens increased 0.8 percentage point to 92.1 percent in 2010, and the share attributable to home equity lines of credit increased 0.6 percentage point to 5.4 percent in 2010. The remaining share, which is accounted for by junior liens, decreased 1.4 percentage points, to 2.6 percent, in the most recent period (data not shown in the tables).

In 2010, there was a reversal of the previously increasing trend in the share of the amount of all first liens that was attributable to refinanced mortgages or where additional borrowing had occurred. First liens that had not been refinanced held steady at 30.5 percent of all homeowners, while the share of homeowners without additional borrowing fell (table 14). Among families in 2010 that had borrowed additional amounts at the time of their most recent refinancing, the median additional amount borrowed was $30,000, compared with $30,300 in 2007 (data not shown in the tables). In the 2010 survey, the most common use of such additional borrowing was for home improvement or some other type of real estate

[48] Of all families, 44.7 percent had a first-lien mortgage in 2010 (45.4 percent in 2007), 3.9 percent had a junior-lien mortgage (5.8 percent in 2007), 10.3 percent had a home equity line of credit (12.6 percent in 2007), and 7.2 percent had a home equity line of credit with an outstanding balance (8.5 percent in 2007).

Table 13. Family holdings of debt, by selected characteristics of families and type of debt, 2007 and 2010 surveys—*continued*

B. 2010 Survey of Consumer Finances—*continued*

Family characteristic	Secured by residential property		Installment loans	Credit card balances	Lines of credit not secured by residential property	Other	Any debt
	Primary residence	Other					
Race or ethnicity of respondent							
White non-Hispanic	51.8	6.1	45.8	39.3	2.4	6.1	75.9
Nonwhite or Hispanic	37.1	3.8	47.4	39.7	1.4	7.2	73.0
Current work status of head							
Working for someone else	54.4	5.3	56.0	45.8	2.4	7.7	83.9
Self-employed	58.6	12.4	42.4	40.4	3.2	7.0	82.0
Retired	29.1	2.9	24.6	25.4	.9	3.1	51.0
Other not working	31.1	2.8	51.8	35.5	*	6.6	75.1
Current occupation of head							
Managerial or professional	64.6	9.8	51.4	44.6	2.9	6.5	87.4
Technical, sales, or services	43.8	4.1	55.0	44.6	2.4	7.0	79.6
Other occupation	54.1	4.4	55.6	45.7	2.1	9.9	82.7
Retired or other not working	29.5	2.9	30.5	27.6	1.1	3.9	56.2
Region							
Northeast	46.9	5.5	42.6	39.9	1.6	6.6	74.8
Midwest	52.8	4.2	48.5	37.4	2.3	5.4	76.4
South	43.6	4.8	48.2	38.2	2.0	7.3	73.6
West	46.9	7.3	44.2	43.0	2.4	5.9	75.9
Urbanicity							
Metropolitan statistical area (MSA)	47.8	5.7	46.2	40.3	2.1	6.5	75.8
Non-MSA	43.3	3.7	46.9	35.0	1.9	6.3	70.7
Housing status							
Owner	69.9	6.9	46.1	43.1	2.0	6.5	81.4
Renter or other	*	2.2	46.9	31.8	2.1	6.4	61.6
Percentile of net worth							
Less than 25	20.0	1.8	57.1	36.9	2.3	6.6	69.2
25–49.9	48.9	2.0	51.1	44.5	1.5	7.3	78.8
50–74.9	61.5	4.6	47.7	46.2	2.2	6.7	80.3
75–89.9	56.9	9.7	34.4	36.1	1.8	5.4	72.2
90–100	58.6	17.8	21.9	20.9	3.0	4.5	70.4

investment; together, those accounted for about half of equity extracted. Other notable uses for extracted equity include loan consolidation, business investment, vehicle purchase, and education expenses.

Families headed by a self-employed person were more likely than families overall to have a home equity line of credit—18.8 percent of self-employed families, compared with 10.3 percent overall in 2010—and to be borrowing against such a line—13.1 percent of self-employed families, compared with 7.2 percent for all families in 2010 (data not shown in the tables). These differences reflect, in part, the relatively higher rates of homeownership among families headed by a self-employed person.

Amid rising house prices in the decade before 2007, much discussion focused on how families managed to finance the purchase of a home. Even though house price declines after 2007 benefited first-time homebuyers, existing homeowners were confronted with the necessity of servicing mortgage balances accumulated earlier. One important determinant of the size of the regular payment that families must make to service their mortgages is the length of time over which the loan must be repaid. Between 2007 and 2010, the share of fixed-term first-lien mortgages with a term of at least 30 years rose dramatically, continuing a trend observed in the prior survey. The share of fixed-term first-lien mortgages with a

Table 13. Family holdings of debt, by selected characteristics of families and type of debt, 2007 and 2010 surveys—*continued*

B. 2010 Survey of Consumer Finances—*continued*

Family characteristic	Secured by residential property		Installment loans	Credit card balances	Lines of credit not secured by residential property	Other	Any debt
	Primary residence	Other					
Median value of holdings for families holding debt (thousands of 2010 dollars)							
All families	**109.6**	**98.0**	**12.6**	**2.6**	**6.0**	**4.5**	**70.7**
Percentile of income							
Less than 20	54.6	72.0	7.6	1.0	1.0	2.0	10.1
20–39.9	65.5	60.0	8.4	1.5	2.7	2.0	20.2
40–59.9	90.0	62.5	12.0	2.2	5.0	3.5	61.4
60–79.9	116.6	66.9	15.0	3.1	3.2	6.0	106.6
80–89.9	158.0	88.0	19.0	5.9	14.5	5.0	163.8
90–100	241.0	180.0	22.4	8.0	20.0	18.0	267.2
Age of head (years)							
Less than 35	120.0	89.0	14.0	1.6	2.0	2.0	39.6
35–44	139.9	85.0	14.7	3.5	2.5	4.4	108.0
45–54	114.0	115.0	12.0	3.5	6.0	5.0	91.8
55–64	97.0	98.0	11.3	2.8	11.0	6.0	76.9
65–74	70.0	125.0	10.0	2.2	8.1	6.0	45.0
75 or more	52.0	74.8	7.8	1.8	*	13.0	30.0
Family structure							
Single with child(ren)	96.0	95.0	9.9	2.0	8.1	2.8	30.2
Single, no child, age less than 55	110.0	99.0	11.8	1.6	3.0	5.0	34.8
Single, no child, age 55 or more	64.0	72.0	7.6	1.7	3.3	2.1	28.0
Couple with child(ren)	132.0	106.3	15.0	3.4	6.0	4.2	112.8
Couple, no child	101.0	97.0	13.2	3.0	13.0	5.8	72.5
Education of head							
No high school diploma	60.0	*	7.6	1.4	.6	2.3	17.6
High school diploma	83.0	62.5	10.0	2.1	3.2	3.0	42.8
Some college	106.0	61.3	12.1	2.1	2.7	3.0	59.7
College degree	150.0	125.0	18.0	4.0	13.0	9.0	127.0

Note: See note to table 1.

* Ten or fewer observations.

term of 30 years or longer rose 5.6 percentage points, to 70.6 percent in 2010. Offsetting that increase, the share of fixed-term first-lien mortgages with a term of 15 years or shorter fell 4.4 percentage points to 21.1 percent in 2010, and the share with terms between 16 and 29 years fell 1.1 percentage points to 8.3 percent in 2010 (data not shown in the tables).

The level of interest rates is also a key determinant of the size of the regular payment that a borrower must make to repay a loan. Between 2007 and 2010, the median interest rate on the stock of outstanding first-lien mortgages on primary residences fell 0.50 percentage point to 5.50 percent, and the mean interest rate fell 0.6 percentage point to 5.71 percent (data not shown in the tables). Some mortgages have an interest rate that may rise or fall over time. From 2007, the fraction of first-lien mortgages on the primary residence that had a potentially variable rate fell 3.6 percentage points, to 10.6 percent in 2010.

Another factor that may affect a borrower's ability to service a loan is the extent to which the payment may change over the life of the loan for reasons other than a change in the interest rate. Recent declines in house prices and changes in benchmark interest rates have brought particular attention to mortgages with payments that may vary over the life of the loan. In some cases, a mortgage may be structured so that the regular payments are not sufficient to pay back the entire principal over the contract period of the loan; in such cases, a

Table 13. Family holdings of debt, by selected characteristics of families and type of debt, 2007 and 2010 surveys—*continued*

B. 2010 Survey of Consumer Finances—*continued*

Family characteristic	Secured by residential property		Installment loans	Credit card balances	Lines of credit not secured by residential property	Other	Any debt
	Primary residence	Other					
Race or ethnicity of respondent							
White non-Hispanic	112.0	110.0	13.6	3.1	6.0	5.2	85.0
Nonwhite or Hispanic	100.0	80.0	10.7	1.9	5.5	2.7	40.0
Current work status of head							
Working for someone else	116.0	92.0	13.9	3.0	6.0	4.0	85.0
Self-employed	145.0	140.0	15.3	4.0	15.6	10.0	118.0
Retired	60.8	62.0	8.1	2.0	3.3	3.0	30.0
Other not working	92.7	94.0	8.3	1.5	*	5.0	21.1
Current occupation of head							
Managerial or professional	150.0	140.0	17.0	4.0	10.0	6.0	137.0
Technical, sales, or services	110.0	86.3	12.8	2.3	2.0	3.8	56.7
Other occupation	90.0	52.0	11.1	2.6	5.6	4.0	63.5
Retired or other not working	68.0	72.0	8.1	1.8	3.0	4.0	28.2
Region							
Northeast	114.0	118.8	13.7	2.3	6.0	6.0	73.0
Midwest	95.0	85.0	13.1	2.5	3.0	4.0	70.5
South	95.0	88.0	11.3	2.8	8.1	3.4	59.6
West	157.6	125.0	14.4	3.0	6.0	5.0	92.3
Urbanicity							
Metropolitan statistical area (MSA)	119.0	104.0	12.9	2.8	5.0	5.0	80.2
Non-MSA	64.0	62.5	12.0	2.1	14.5	3.0	40.0
Housing status							
Owner	109.6	97.0	13.7	3.4	10.0	5.2	110.8
Renter or other	*	105.4	10.2	1.3	1.5	2.7	9.6
Percentile of net worth							
Less than 25	141.0	110.0	13.5	1.9	1.9	2.5	20.4
25–49.9	91.0	25.6	10.5	2.0	1.3	2.5	55.3
50–74.9	100.3	53.2	12.7	3.1	5.0	6.0	85.9
75–89.9	105.0	92.0	13.5	3.4	11.0	10.0	100.7
90–100	216.5	195.0	17.7	5.0	30.0	25.0	232.8
MEMO							
Mean value of holdings for families holding debt	154.3	179.6	23.5	7.1	49.1	16.8	130.7

"balloon payment" of the remaining principal is left at the end of the loan term. Over the 2007–10 period, the share of first-lien mortgages with a balloon payment fell 1.3 percentage

Table 14. Type of home-secured debt held by homeowners, 2001–10 surveys

Percent

Type of home-secured debt	Homeowners with home-secured debt			
	2001	2004	2007	2010
First-lien mortgage	62.5	65.2	66.1	66.4
For home purchase	35.8	28.2	30.4	30.5
Refinanced				
Extracted equity	9.7	12.9	14.3	11.4
No extracted equity	17.1	24.0	21.5	24.5
Junior-lien mortgage	8.5	6.1	8.5	5.8
For home purchase	1.3	1.5	2.1	1.7
Other purpose	7.2	4.7	6.4	4.0
Home equity line of credit	11.2	17.8	18.4	15.3
Currently borrowing	7.1	12.4	12.4	10.7

points to 3.2 percent. Payments on a mortgage may vary in a variety of other ways, but such loans tend to be rarely found in the SCF.

Borrowing on Other Residential Real Estate

Although ownership of residential real estate other than a primary residence rose slightly from 2007 to 2010, the prevalence of debt owed on such property edged down 0.2 percentage point over that time—to 5.3 percent of families in 2010. Among families that had such real estate in 2007, 40.3 percent had a loan secured by the property; in 2010, the proportion had fallen to 37.2 percent. Borrowing on other residential real estate is more common among families in higher income, education, or wealth groups; couples; and families headed by a self-employed person or by a person employed in a managerial or professional position. Most of the changes in the prevalence of such debt across groups were small, though there were substantial decreases for the highest income and wealth deciles and the self-employed.

The median amount of debt on other residential real estate for families having such debt fell 6.5 percent in 2010, and the mean amount fell 4.2 percent. Changes over the recent three-year period in the median and mean amounts exhibited a mixed pattern of increases and decreases for subgroups of families, and the percentage changes were quite large in absolute value.

Installment Borrowing

Installment borrowing is about as common as home-secured borrowing.[49] In 2010, 46.3 percent of families had installment debt, a decrease of 0.6 percentage point from the level in 2007. The use of installment borrowing is broadly distributed across demographic groups, with notably lower use by families in the lowest income group, those in the highest wealth group, childless single families headed by a person aged 55 or older, families headed by a retired person, and families headed by a person aged 65 or older. By comparison, the median amount of outstanding installment debt, for families having such debt, varies more clearly across many groups. The median amount tends to rise across income and education, and it falls across age groups. The median amount of installment debt is fairly similar among families in wealth groups below the 90th percentile and somewhat higher for families in the top net worth group.

Installment borrowing is used for a wide variety of purposes. In 2010, 45.1 percent of such borrowing was related to education, 39.3 percent was related to the purchase of a vehicle, and 15.6 percent of outstanding installment debt was owed for other purposes (table 15). In past SCF surveys, balances on vehicle loans have always accounted for more than half of installment debt; the decrease to a share of 39.3 percent in 2010 reflects, in part, a decrease in vehicle purchases in the years preceding the most recent survey. A contributing factor in the decline of that share was an increase in borrowing for education, which rose 11.9 percentage points as a share of installment borrowing over the recent three-year period. The increased importance of education-related installment debt is most evident for the youngest age group; among families headed by someone less than age 35, 65.6 percent of their installment debt was education related in 2010, up from 53.1 percent in 2007. Among families headed by someone reporting educational attainment of "some college," the share of

[49] The term "installment borrowing" in this article describes closed-end consumer loans—that is, loans that typically have fixed payments and a fixed term. Examples are automobile loans, student loans, and loans for furniture, appliances, and other durable goods.

Table 15. Value of installment debt distributed by type of installment debt, by selected characteristics of families with installment debt, 2007 and 2010 surveys
Percent

Family characteristic	2007			2010		
	Education	Vehicle	Other	Education	Vehicle	Other
All families	**33.2**	**51.7**	**15.1**	**45.1**	**39.3**	**15.6**
Percentile of income						
Less than 20	47.0	24.4	28.6	40.6	29.1	30.3
20–39.9	29.8	43.9	26.3	44.2	32.2	23.6
40–59.9	33.6	54.7	11.7	54.0	34.3	11.7
60–79.9	32.7	59.4	7.9	42.6	46.7	10.7
80–89.9	38.3	56.2	5.6	50.7	44.6	4.7
90–100	25.5	50.9	23.6	37.3	43.7	19.0
Age of head (years)						
Less than 35	53.1	41.2	5.6	65.6	25.7	8.7
35–44	24.3	57.8	17.8	48.1	37.5	14.4
45–54	27.2	53.5	19.4	36.1	51.3	12.6
55–64	21.7	53.8	24.5	29.9	42.9	27.2
65–74	*	73.2	19.0	13.3	63.7	23.0
75 or more	*	88.0	*	*	38.8	52.0
Education of head						
No high school diploma	12.8	71.5	15.8	12.3	59.4	28.3
High school diploma	15.0	69.6	15.4	22.8	53.6	23.6
Some college	23.6	53.0	23.5	49.4	39.1	11.5
College degree	48.1	40.2	11.7	54.8	32.3	12.9
Race or ethnicity of respondent						
White non-Hispanic	32.1	52.1	15.9	43.9	40.0	16.1
Nonwhite or Hispanic	36.2	50.6	13.2	47.6	37.7	14.7
Percentile of net worth						
Less than 25	47.9	32.5	19.6	65.4	16.3	18.3
25–49.9	30.4	60.8	8.7	41.0	47.2	11.8
50–74.9	30.1	60.5	9.4	34.0	56.4	9.6
75–89.9	25.9	65.8	8.3	31.1	58.7	10.2
90–100	16.7	47.7	35.7	11.3	60.0	28.7

Note: See note to table 1.
* Ten or fewer observations.

installment debt attributable to education-related loans more than doubled, from 23.6 percent in 2007 to 49.4 percent in 2010.[50]

From 2007 to 2010, the median amount owed on installment loans fell 7.4 percent, while the mean rose 7.3 percent. Changes in the median within demographic categories include both increases and decreases. Large decreases in the median debt outstanding occurred among nonwhite or Hispanic families (a 15.1 percent decrease) and among families headed by someone who lacked a high school diploma (a 17.4 percent decrease).

Credit Card Balances and Other Lines of Credit

As with installment borrowing, the carrying of credit card balances is widespread, but it is considerably less common among the highest and lowest income groups, the highest wealth group, and families headed by a person who is aged 65 or older or who is retired.[51] The

[50] For an expanded version of table 13, including the categories of installment loans given in table 15, see www.federalreserve.gov/econresdata/scf/scf_2010.htm.

[51] In this article, credit card balances consist of balances on bank-type cards (such as Visa, MasterCard, and Discover as well as Optima and other American Express cards that routinely allow carrying a balance), store cards

proportion of families carrying a balance, 39.4 percent in 2010, was down 6.7 percentage points from 2007. The decreased prevalence of credit card debt outstanding was widespread and noticeable across most of the demographic groups, though the prevalence of credit card debt rose for families headed by someone aged 75 or older and among families headed by someone with no high school diploma.

Overall, the median balance for those carrying a balance fell 16.1 percent to $2,600; the mean fell 7.8 percent to $7,100. These decreases reversed some of the preceding run-up in credit card debt (data not shown in the tables). Over the recent three-year period, the median balance fell for most demographic groups; couples and childless single families, higher-wealth families, and families headed by someone working in technical, sales, or service jobs and managerial or professional occupations all saw substantial decreases in their median credit card balances. One group that saw substantial increases in the use of credit card borrowing is families headed by someone 75 or older; median balances also rose for single families with children and for families in the bottom wealth quartile.

Many families with credit cards do not carry a balance.[52] Of the 68.0 percent of families with credit cards in 2010, only 55.1 percent had a balance at the time of the interview; in 2007, 72.9 percent had cards, and 61.0 percent of these families had an outstanding balance on them. The number of credit cards held by families also decreased. In 2007, 35.0 percent of families held four or more cards, and that level of ownership fell to 32.7 percent by 2010. Between 2007 and 2010, the fraction of families with three cards fell from 12.1 percent to 10.6 percent, the fraction with two cards fell from 12.7 percent to 12.2 percent, and the fraction with one card fell from 13.1 percent to 12.5 percent (data not shown in the tables).

The proportion of cardholders who had bank-type cards decreased slightly over this three-year period, and the proportion with store or gasoline card types fell considerably, while the proportion with travel and entertainment card types as well as miscellaneous other credit cards increased, as shown in the following table:

Table 15.1

Type of credit card	Families with credit cards	
	2010 (percent)	Change, 2007–10 (percentage points)
Bank	95.8	–.5
Store or gasoline	55.8	–4.4
Travel and entertainment	9.3	1.9
Miscellaneous	5.1	1.4

Bank-type cards are the most widely held type of card and thus hold particular importance in any examination of family finances. Indeed, balances on such cards accounted for 85.1 percent of outstanding credit card balances in 2010, down from 87.1 percent in 2007 (data not shown in the tables). The proportion of holders of bank-type cards who had a balance went down 5.9 percentage points to 52.4 percent; the proportion of holders of

or charge accounts, gasoline company cards, so-called travel and entertainment cards (such as American Express cards that do not routinely allow carrying a balance and Diners Club), other credit cards, and revolving store accounts that are not tied to a credit card. Balances exclude purchases made after the most recent bill was paid.

[52] The remaining discussion of credit cards excludes revolving store accounts that are not tied to a credit card. In 2010, 5.1 percent (5.4 percent in 2007) of families had such an account, the median outstanding balance for families that had a balance was $750 ($730 in 2007), and the total of such balances accounted for 3.5 percent (4.4 percent in 2007) of the total of balances on credit cards and such store accounts (data not shown in the tables).

bank-type cards who reported that they usually pay their balances in full rose slightly, from 55.3 percent in 2007 to 56.4 percent in 2010. Over the recent three-year period, the median new charges for the month preceding the interview on all bank-type cards held by the family rose from $260 in 2007 to $300 in 2010. For families having any bank-type cards, the median number of such cards remained at 2; the median credit limit on all such cards fell from $18,900 to $15,000, and the median interest rate on the card with the largest balance (or on the newest card, if no outstanding balances existed) rose 0.5 percentage point to 13.0 percent.

Only 4.1 percent of families had an established line of credit other than a home equity line in 2010.[53] Even fewer families—2.1 percent—had a balance on such a line, an increase of 0.4 percentage point since 2007. The median amount outstanding on these lines rose 50.0 percent between the most recent surveys, and the mean rose even more—71.9 percent—between 2007 and 2010. Borrowing on other lines of credit was more common among families headed by a person who was self-employed or families in the highest income or wealth groups, a pattern that is also apparent in earlier SCFs.

Other Debt

From 2007 to 2010, the proportion of families that owed money on other types of debts decreased 0.4 percentage point to 6.4 percent.[54] Borrowing against pension accounts rose slightly over this period, while uses of other types declined, as shown in the following table:

Table 15.2

Type of other debt	All families	
	2010 (percent)	Change, 2007–10 (percentage points)
Cash value life insurance loans	.9	†
Pension account loans	3.6	.4
Margin account loans	.3	–.2
Other miscellaneous loans	1.9	–.5

† Less than 0.05 percent.

Rates of use of other debt are noticeably lower for families in the bottom two income groups as well as for families headed by a person who is 65 years of age or older or who is retired. The highest rate of other debt ownership is among the groups of families with children. Changes in the prevalence of such debt varied widely across demographic groups, though most groups saw declines.

The median amount owed by families with this type of debt fell 13.5 percent to $4,500 between 2007 and 2010; over the same period, the mean rose 6.8 percent. In 2010, 40.2 percent of the total amount of this type of debt outstanding was attributable to margin loans (36.3 percent in 2007), 26.4 percent to loans against a pension from a current job of the family head or that person's spouse or partner (20.5 percent in 2007), 8.0 percent to loans against cash value life insurance policies (12.0 percent in 2007), and the remaining 25.4 percent to miscellaneous loans (31.2 percent in 2007) (data not shown in the tables).

[53] In this article, borrowing on lines of credit excludes borrowing on credit cards.

[54] The "other debt" category comprises loans on cash value life insurance policies, loans against pension accounts, borrowing on margin accounts, and a miscellaneous category largely comprising personal loans not explicitly categorized elsewhere.

Table 16. Amount of debt of all families, distributed by purpose of debt, 2001–10 surveys
Percent

Purpose of debt	2001	2004	2007	2010
Primary residence				
Purchase	70.9	70.2	69.5	69.5
Improvement	2.0	1.9	2.3	1.9
Other residential property	6.5	9.5	10.8	10.5
Investments excluding real estate	2.8	2.2	1.6	2.0
Vehicles	7.8	6.7	5.5	4.7
Goods and services	5.8	6.0	6.2	5.7
Education	3.1	3.0	3.6	5.2
Other	1.1	.6	.5	.4
Total	**100**	**100**	**100**	**100**

Note: See note to table 1.

In 2007, the SCF collected information for the first time on whether a family member had taken out a loan in the past year that was supposed to be repaid in full out of that person's next paycheck.[55] Overall, 3.9 percent of families reported having taken out a so-called payday loan in 2010, up from 2.4 percent in 2007. In 2010, the fraction of families that had taken out a payday loan declined over age groups, falling from 5.7 percent of families headed by a person younger than age 35 to 0.5 percent for families headed by a person aged 65 or older (data not shown in the tables). Across income groups, the share of families that reported such a loan was between 4.6 percent and 6.2 percent for the bottom three quintiles, but for families in the top quintile, the rate was only 0.2 percent. Similarly, 8.1 percent of families in the bottom net worth quartile reported having taken out a payday loan, and virtually no families with net worth above the median reported having done so.

The data indicate that families tend to take out payday loans to finance immediate expenses. In 2010, the most common reason given for choosing a payday loan for families that had taken out such a loan was "emergencies" and similar urgent needs or a lack of other options (42.4 percent).[56] The second most common reason cited was "convenience" in obtaining the loan (24.2 percent). Many families also cited reasons that conveyed difficulties in meeting their regular financial commitments; for example, 17.4 percent of families reported a need to pay other bills and loans (up from 10.8 percent in 2007), and 11.0 percent cited the need to pay for living expenses, including food, gas, vehicle expenses, medical payments, utility costs, or rent. The remaining 5.0 percent of families with a payday loan in the past year cited other needs, including "Christmas" or the need to "help family."

Reasons for Borrowing

The SCF provides information on the reasons that families borrow money (table 16). One subtle problem with the use of these data is that, even though money is borrowed for a particular purpose, it may be employed to offset some other use of funds. For example, a family may have sufficient funds to purchase a home without using a mortgage but may instead choose to finance the purchase to free existing funds for another purpose. Thus, trends in the data can only suggest the underlying use of funds by families.

[55] The family may or may not have had such a loan outstanding at the time of the interview.

[56] This discussion considers the primary reasons given by families when asked why they chose this type of loan. Families could provide up to two reasons, but 94.5 percent of those that had taken out a payday loan in the past year provided only one.

Although the survey information on use is substantial, it is not exhaustive. Most important, in the case of credit cards, it was deemed impractical to ask about the purposes of borrowing, which might well be heterogeneous for individual families. For the analysis here, all credit card debt is included in the category "goods and services." The surveys before 2004 lack information on the use of funds borrowed through a first-lien mortgage; therefore, for purposes of this calculation, all funds owed on a first-lien mortgage on a primary residence are assumed to have been used for the purchase of the home, even when the homeowner had refinanced the mortgage and extracted equity for another purpose.

The great majority of family debt is attributable to the purchase of a primary residence; between 2007 and 2010, the share of debt for this purpose was unchanged (at 69.5 percent). Looking more broadly at debt for residential real estate, there was a decrease in balances owed on residential real estate other than the primary residence—the second-largest share of debt—and a similar decrease in balances owed for improvements on the primary residence. The share of debt attributable to vehicle purchases also fell—0.8 percentage point, to 4.7 percent of the total.

With a 1.6 percent rise between 2007 and 2010, the fraction of debt owed for education, at 5.2 percent, exceeded the fraction of borrowing for vehicles for the first time in the SCF. The increase in the share of debt for education reflects to some degree the decrease in borrowing for other purposes, but the level of education debt also rose substantially. The share of families having any education debt rose from 15.2 percent in 2007 to 19.2 percent in 2010 (data not shown in the tables). Among families with education debt, the mean increased 14.0 percent (from $22,500 in 2007 to $25,600 in 2010), while the median rose 3.4 percent (from $12,600 in 2007 to $13,000 in 2010).

The fraction of debt owed for goods and services fell between 2007 and 2010 from 6.2 percent to 5.7 percent. The decline in the share of debt in the goods and services category was smaller than that in the share of debt for vehicles, so goods and services continued to account for a larger share of debt outstanding. About half of the debt in the goods and services category, 50.1 percent, was outstanding balances on credit cards.[57]

Credit Market Experiences

The SCF also collects some information on families' recent credit market experiences. Specifically, the survey asks whether the family had applied for any type of credit in the past five years and, if so, whether any application was either turned down or granted for a lesser amount than the amount initially requested. Families that give such responses are asked the reason given for the decision. The survey also asks whether, at any time in the past five years, the family ever considered applying for credit but then decided not to apply because of a belief that the application would be rejected. Such families were asked the reason they believed they would have been turned down.

In 2010, 61.7 percent of families reported that they had applied for credit at some point in the preceding five years (66.3 percent in 2007). Of these families, 33.9 percent had at least once in the preceding five years been either turned down for credit or approved for less credit than the amount for which they had applied (29.7 percent in 2007). Of all families,

[57] The surveys beginning with 2004 contain information on the use of funds obtained from refinancing a first-lien mortgage. If this information for 2010 is used in the classification of outstanding debt by purpose, the shares of debt were, for home purchase, 66.4 percent; for home improvements, 2.9 percent; for other residential real estate, 11.0 percent; for investments other than real estate, 2.3 percent; for vehicles, 4.8 percent; for goods and services, 6.9 percent; for education, 5.3 percent; and for other unclassified purposes, 0.4 percent (data not shown in the tables).

18.5 percent had considered applying but subsequently did not do so because they thought the application would be denied (15.3 percent in 2007). The most common reasons reported for either having been denied credit or having not applied for credit were related to the borrower's credit characteristics, such as the lack of a credit history, previous performance on a loan or account from another institution, and the amount of debt held by the borrower, as shown in the following table:[58]

Table 16.1

Reason turned down or did not apply	Families that applied for credit and were turned down or received less credit than the amount requested (percent)	Families that did not apply for credit because they expected to be turned down (percent)
Personal characteristics	1.7	2.2
Credit characteristics	55.5	62.9
Financial characteristics	33.0	28.2
Miscellaneous, including no reason given	9.8	6.8

In 2010, the SCF began collecting information about credit market experiences of small businesses owned by families. Although personal and business finances may be intertwined, there may be differences in the ease with which persons and businesses obtain credit. In 2010, among the 23.0 percent of families having a small business that applied for credit in the preceding five years, 25.1 percent reported having been turned down or received less credit than the amount requested, and another 7.5 percent reported they did not apply for credit because they thought they would be turned down. Among those who were turned down or received less than the amount requested, 29.5 percent reported the reason was personal or business credit characteristics, 50.4 reported it was due to the financial characteristics of the business, and 20.1 percent reported miscellaneous reasons (data not shown in the tables).

Debt Burden

The ability of individual families to service their loans is a function of two factors: the level of their loan payments and the income and assets they have available to meet those payments. In planning their borrowing, families make assumptions about their future ability to repay their loans. Problems may occur when events turn out to be contrary to those assumptions. If such misjudgments are sufficiently large and prevalent, a broad pattern of default, restraint in spending, and financial distress in the wider economy might ensue (such as was seen in the period after the 2007 survey).

The Federal Reserve staff has constructed an aggregate-level debt service ratio, defined as an estimate of total scheduled loan payments (interest plus minimum repayments of principal) for all families, divided by total disposable personal income. From the third quarter of 2007 to the same period in 2010, the aggregate-level measure dropped 2.2 percentage points, to 11.7 percent.[59]

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[58] Personal characteristics include responses related to family background or size, marital status, sex, or age; credit characteristics include responses related to the need to have a checking or savings account, lack of a credit history, credit reports from a credit rating agency or from other institutions, or the level of outstanding debt and insufficient credit references; and financial characteristics include responses related to previous difficulty getting credit, more "strict" lending requirements of the institution, an error in processing the application, or credit problems of an ex-spouse.

[59] Data on this measure, the "debt service ratio," and a description of the series are available at www.federalreserve.gov/releases/housedebt/default.htm. See Karen Dynan, Kathleen Johnson, and Karen Pence (2003), "Recent Changes to a Measure of U.S. Household Debt Service," *Federal Reserve Bulletin*, vol. 89 (October), pp. 417–26, www.federalreserve.gov/pubs/bulletin/default.htm.

The survey data for individual families may be used to construct a similar estimate of debt burden for families overall as well as for various demographic groups (table 17).[60] The SCF-based estimate is the ratio of total debt payments for all families to total family income of all families. From 2007 to 2010, the SCF-based estimate was barely changed at 14.7 percent; conceptual differences between the aggregate measure and the SCF-based

Table 17. Ratio of debt payments to family income (aggregate and median), share of debtor families with ratio greater than 40 percent, and share of debtors with any payment 60 days or more past due, 2001–10 surveys

Percent

Family characteristic	Aggregate				Median for debtors				Debtors with ratio greater than 40 percent				Debtors with any payment past due 60 days or more			
	2001	2004	2007	2010	2001	2004	2007	2010	2001	2004	2007	2010	2001	2004	2007	2010
All families	**12.9**	**14.4**	**14.6**	**14.7**	**16.7**	**18.1**	**18.7**	**18.1**	**11.8**	**12.3**	**14.8**	**13.8**	**7.0**	**8.9**	**7.1**	**10.8**
Percentile of income																
Less than 20	16.1	18.2	17.7	23.5	19.2	19.7	19.1	16.3	29.3	26.8	26.9	26.1	13.4	15.9	15.1	21.2
20–39.9	15.8	16.7	17.2	16.9	16.7	17.4	17.1	17.5	16.6	18.6	19.5	18.6	11.7	13.8	11.5	15.2
40–59.9	17.1	19.4	19.8	19.5	17.6	19.5	20.3	20.0	12.3	13.8	14.5	15.4	7.9	10.4	8.3	10.2
60–79.9	16.8	18.6	21.8	19.3	18.1	20.7	21.9	20.4	6.5	7.3	12.9	11.0	4.0	7.1	4.1	8.8
80–89.9	17.0	17.4	19.8	18.0	17.2	18.3	19.3	19.3	3.5	2.6	8.2	5.3	2.6	2.3	2.1	5.4
90–100	8.1	9.3	8.4	9.4	11.2	12.7	12.5	13.1	2.0	1.5	3.8	2.9	1.3	.3	.2	2.1
Age of head (years)																
Less than 35	17.2	17.8	19.7	17.0	17.7	18.0	17.6	16.4	12.0	12.8	15.1	11.6	11.9	13.7	9.4	10.4
35–44	15.1	18.3	18.6	18.4	17.8	20.6	20.3	20.9	10.1	12.4	12.8	16.4	5.9	11.7	8.6	15.7
45–54	12.8	15.4	15.0	16.2	17.4	18.5	19.6	19.2	11.6	13.3	16.3	15.5	6.2	7.6	7.3	12.6
55–64	10.9	11.6	12.6	12.5	14.3	15.9	17.5	17.6	12.3	10.3	14.5	13.0	7.1	4.2	4.9	8.4
65–74	9.2	8.7	9.6	11.3	16.0	15.6	17.9	17.0	14.7	11.6	15.6	12.1	1.5	3.4	4.4	6.1
75 or more	3.9	7.1	4.4	6.8	8.0	12.8	13.0	14.1	14.6	10.7	13.9	11.9	.8	3.9	1.0	3.2
Percentile of net worth																
Less than 25	13.3	13.0	15.0	19.2	11.5	13.0	12.1	13.6	11.6	10.6	10.7	14.9	17.8	23.0	16.8	22.2
25–49.9	18.1	19.6	22.5	19.3	20.1	21.2	23.4	21.2	14.2	15.9	19.3	15.3	7.1	11.0	7.7	13.3
50–74.9	16.7	20.7	20.4	19.2	18.3	21.5	21.8	20.8	11.2	12.9	16.0	14.0	3.6	3.2	4.2	6.8
75–89.9	15.4	15.2	17.0	15.9	16.9	18.0	18.2	16.7	10.6	9.6	13.1	11.0	.7	1.0	1.2	2.0
90–100	7.4	8.6	8.1	8.8	11.2	12.7	12.7	13.4	8.5	7.6	11.1	11.0	.3	.1	.7	1.2
Housing status																
Owner	13.9	15.7	15.6	16.1	19.9	21.5	22.8	22.2	14.7	15.0	18.1	17.1	4.3	5.6	4.8	8.7
Renter or other	7.4	7.2	7.9	7.0	8.3	8.2	8.4	6.8	4.2	4.3	5.4	5.0	14.0	18.6	13.5	16.6

Note: The aggregate measure is the ratio of total debt payments to total income for all families. The median is the median of the distribution of ratios calculated for individual families with debt. Also see note to table 1.

[60] The survey measure of payments relative to income may differ from the aggregate-level measure for several reasons. First, the debt payments included in each measure are different. The aggregate-level measure includes only debts originated by depositories, finance companies, and other financial institutions, whereas the survey includes, in principle, debts from all sources.

Second, the aggregate-level measure uses an estimate of disposable personal income from the national income and product accounts for the period concurrent with the estimated payments as the denominator of the ratio, whereas the survey measure uses total before-tax income reported by survey families for the preceding year; the differences in these two income measures are complex.

Third, the payments in the aggregate-level measure are estimated using a formula that entails complex assumptions about minimum payments and the distribution of loan terms at any given time; the survey measure of payments is directly asked of the survey respondents but may also include payments of taxes and insurance on real estate loans.

Fourth, because the survey measures of payments and income are based on the responses of a sample of respondents, they may be affected both by sampling error and by various types of response errors. As mentioned earlier in this article, the survey income measure tracks the most comparable measure of income in the Census Bureau's Current Population Survey.

estimate can account for this divergence in the recent period.[61] If total payments and incomes are computed from the survey data using only families with debt payments, the results for the recent period show an increase from 18.1 percent in 2007 to 18.5 percent in 2010; if the ratio is computed using only families with home-secured debt, the data show a rise from 20.5 percent in 2007 to 21.1 percent in 2010 (data not shown in the tables). The SCF-based estimate of the aggregate debt-burden ratio decreased for many demographic groups over the recent three-year period, but there were notable increases for low-income and low-net-worth families as well as families headed by a person aged 65 or older.

The ability to look at the distribution of payments relative to income at the level of families potentially offers insights that are not available from any of the aggregate-level figures. In particular, the survey allows a detailed look at the spectrum of payments relative to income across all families with debts. Over the recent period, the median of the ratios for individual families that had any debt fell 0.6 percentage point, to 18.1 percent in 2010; this decline is small relative to the cumulative increases in this measure since 1989 that were otherwise interrupted only by a decline between 1998 and 2001. Changes in the most recent three-year period in the median ratio of debt payments to income across demographic groups were mixed.[62]

A limitation of the median ratio is that it may not be indicative of distress because it reflects the situation of only a typical family. Unless errors of judgment by both families and lenders are pervasive, one would not expect to see signs of financial distress at the median. Thus, a more compelling indicator of distress is the proportion of families with unusually large total payments relative to their incomes. From 2007 to 2010, the proportion of debtors with payments exceeding 40 percent of their previous-year income fell 1.0 percentage point to 13.8 percent; in the preceding three years, the proportion had increased 2.5 percentage points. The changes were generally negative across demographic groups except families in the bottom net worth group, for which the share rose 4.2 percentage points. Changes for most of the income groups were small, though families with income between the 60th and 80th percentiles saw a 1.9 percentage point decline in the fraction exceeding the 40 percent mark, and those between the 80th and 90th income percentiles saw a 2.9 percentage point decline.[63]

Fluctuations in a family's income away from its usual level can have substantial effects on the family's payment-to-income ratio. If the payment ratio is defined in terms of families' reported usual incomes, the fraction of families with a ratio exceeding 40 percent falls to 10.0 percent. This 3.8 percentage point difference reflects two facts: first, 4.4 percent of families with debt had relatively high payment-to-income ratios based on the previous year's income but would not have if income had been at its usual level, and, second, a far smaller share of families with debt—0.6 percent—had debt payments less than or equal to 40 percent of last year's income but would have had a ratio above 40 percent if income had been at its usual level. Families may draw on assets as well as income to meet debt payments. For all families with debt, 56.7 percent had transaction account balances equal to at least three months of debt payments in 2010. For families with payment-to-income ratios above 40 percent, however, this share fell to 22.4 percent.

[61] The definition of debt payments in the SCF does not include payments on leases or rental payments. The survey collects information on vehicle lease payments and rent on primary residences, and, thus, in principle a broader measure of debt payments could be constructed, one that would be similar to the "financial obligations ratio" estimated by the Federal Reserve staff.

[62] The median of the ratio for families with home-secured debt in 2010 was 24.8 percent, down from 25.2 percent in 2007 (data not shown in the tables).

[63] Of families with home-secured debt, the proportion that had total payments of more than 40 percent of their income was 19.3 percent in 2010, a level 0.9 percentage point lower than that in 2007 (data not shown in the tables).

Other commonly used indicators of debt-repayment problems are aggregate delinquency rates—that is, the percentage of delinquent accounts or the percentage of total balances on which payments are late. Both account-based and dollar-weighted aggregate measures indicate that delinquencies on mortgages rose substantially from the third quarter of 2007 to the third quarter of 2010, from 3.0 percent to 8.7 percent of accounts and from 2.8 percent to 10.8 percent of dollar-weighted accounts. Over the 2007–10 period, the percentage of delinquent automobile loans declined slightly, while the corresponding dollar-weighted measure rose but remained relatively low at 2.8 percent. On net, a dollar-weighted delinquency measure for other closed-end loans rose from 2.5 percent in the third quarter of 2007 to 3.4 percent in the third quarter of 2010. Delinquency measures for credit cards also differed by whether the measure was based on dollar volume or delinquent accounts, as the account-weighted delinquency rate fell from 4.2 percent to 3.6 percent between the third quarter of 2007 and the third quarter of 2010, while the dollar-weighted delinquency rate edged up from 4.4 percent to 4.6 percent over the same period.[64]

A related measure of delinquency is collected in the SCF. Families that have any debt at the time of their interview are asked whether they have been behind in any of their loan payments in the preceding year. This measure differs conceptually from the aggregate delinquency rates in that the survey counts multiple occasions of late payments as one, counts families instead of balances or accounts, and includes all types of loans; because it counts individual families, not their balances, it is closer in spirit to aggregate measures based on the numbers of delinquent accounts than to those based on the amounts of delinquent balances. The survey shows a large increase from 7.1 percent in 2007 to 10.8 percent in 2010 in the proportion of debtors who were 60 or more days late with their payments on any of their loans in the preceding year. This measure rose for families in each of the income groups, but proportionately the changes were largest for higher-income groups; the percentage also rose across net worth groups. The share of families with debt that were at least 60 days late on a payment during the preceding year rose across all age groups and for both homeowners and renters.[65] For families with a payment-to-income ratio of 40 percent or more, 22.0 percent missed a debt payment by 60 days or more (up from 13.8 percent in 2007); by comparison, 9.1 percent of debtor families with lower ratios had fallen behind in debt repayment (up from 6.0 percent in 2007).

Summary

Data from the 2007 and 2010 SCF show that median income fell substantially and that mean income fell somewhat faster, an indication that income losses, at least in terms of levels, were larger for families in the uppermost part of the distribution. Overall, both median and mean net worth also fell dramatically over this period—38.8 percent and 14.7 percent, respectively. Changes in housing wealth and business equity were key drivers in those wealth changes. The preceding three years had seen only small changes in median and mean income and in median net worth, but a sizable gain in mean net worth.

Although the median and mean of families' holdings of financial assets decreased overall from 2007 to 2010, financial assets rose as a share of total assets, reversing an earlier trend. The offsetting decline in the share of nonfinancial assets was most strongly driven by the decline in real estate prices and the value of business equity. The homeownership rate,

[64] The most commonly used such measures are from the Consolidated Reports of Condition and Income (Call Report), the American Bankers Association, and Moody's Investors Service.

[65] For families with home-secured debt, the result is very similar to that for homeowners overall. The proportion with payments late 60 days or more in 2007 was 4.8 percent after rising to an estimated 5.6 percent in 2004 (data not shown in the tables).

which had risen noticeably between the 2001 and 2004 surveys, continued to trend downward, by 2010 retracing the path to the level seen in 2001. Declines in unrealized capital gains were an important part of the decrease in assets; in 2010, 24.5 percent of total assets were attributable to unrealized capital gains, a share more than 11 percentage points below that in 2007; the decline was primarily due to changes in the value of holdings of real estate or private business equity.

Debt fell more slowly than assets over the recent three-year period. Thus, overall indebtedness as a share of assets rose markedly. Home-secured debt fell slightly as a share of total family debt, but in 2010 it remained by far the largest component of family debt. The share of borrowing for residential real estate other than the primary residence fell slightly, but in 2010 it stayed high by historical standards. The percentage of families using credit cards for borrowing dropped over the period; the median balance on their accounts fell 16.1 percent, and the mean fell 7.8 percent. Use of education-related borrowing continued to increase in the recent period, as the fraction of families with education-related debt rose from 15.2 percent to 19.2 percent, the mean balance among those with such debt rose 14.0 percent, and the median balance increased 3.4 percent.

Declining consumer loan interest rates between 2007 and 2010 helped offset the fact that debt rose relative to income for many families. As a result, the median ratio of loan payments to family income for debtors, a common indicator of debt burden, fell slightly over the period to 18.1 percent in 2010; this measure remains above the values seen in the 2001 SCF and earlier. Data from the recent three-year period also show a decrease of 1.0 percentage point in the proportion of debtors with loan payments exceeding 40 percent of their income, a level traditionally considered to be high; the share of families with payment ratios this high peaked at 14.8 percent in 2007. The fraction of debtors with any payment 60 days or more past due climbed from 7.1 percent in 2007 to 10.8 percent in 2010.

Appendix: Survey Procedures and Statistical Measures

Detailed documentation of the Survey of Consumer Finances (SCF) methodology is available elsewhere.[66] The 2010 data used here are derived from the final internal version of the survey information. Data from this survey, suitably altered to protect the privacy of respondents, along with additional tabulations of data from the surveys beginning with 1989, are expected to be available in June 2012 on the Federal Reserve's website at www.federalreserve.gov/econresdata/scf/scf_2010survey.htm. Links to the data used in this article for earlier periods are available on that site. Results reported in this article for earlier surveys may differ from the results reported in earlier articles because of additional statistical processing, correction of data errors, revisions to the survey weights, conceptual changes in the definitions of variables used in the articles, and adjustments for inflation.

As a part of the general reconciliations required for this article, the survey data were compared with many external estimates, a few of which are mentioned in the text. Generally, the survey estimates correspond fairly well to external estimates. One particularly important comparison is between the SCF and the Federal Reserve's flow of funds accounts for the household sector. This comparison suggests that when the definitions of the variables

[66] See Arthur B. Kennickell (2000), "Wealth Measurement in the Survey of Consumer Finances: Methodology and Directions for Future Research" (Washington: Board of Governors of the Federal Reserve System, May), www.federalreserve.gov/econresdata/scf/scf_workingpapers.htm; Arthur B. Kennickell (2001), "Modeling Wealth with Multiple Observations of Income: Redesign of the Sample for the 2001 Survey of Consumer Finances" (Washington: Board of Governors of the Federal Reserve System, October), www.federalreserve.gov/econresdata/scf/scf_workingpapers.htm; and references cited in these papers.

in the two sources can be adjusted to a common conceptual basis, the estimates of totals in the two systems tend to be close. The data series in the SCF and in the flow of funds accounts usually show very similar growth rates.[67] In general, the data from the SCF can be compared with those of other surveys only in terms of the medians because of the special design of the SCF sample.

Adjustment for Inflation

In this article, all dollar amounts from the SCF are adjusted to 2010 dollars using the "current methods" version of the consumer price index (CPI) for all urban consumers. In an ongoing effort to improve accuracy, the Bureau of Labor Statistics has introduced several revisions to its CPI methodology. The current-methods index attempts to extend these changes to earlier years to obtain a series as consistent as possible with current practices in the official CPI.[68] To adjust assets and liabilities to 2010 dollars and to adjust family income for the preceding calendar year to 2010, the figures given in the following table were applied:

Table A.1

Survey year	Adjustment factor for assets and debts in the survey year	Adjustment factor for income in the calendar year before the survey year
2001	1.2254	1.2598
2004	1.1507	1.1817
2007	1.0477	1.0774
2010	1.0000	1.0165

Definition of "Family" in the SCF

The definition of "family" used throughout this article differs from that typically used in other government studies. In the SCF, a household unit is divided into a "primary economic unit" (PEU)—the family—and everyone else in the household. The PEU is intended to be the economically dominant single person or couple (whether married or living together as partners) and all other persons in the household who are financially interdependent with that economically dominant person or couple.

This report also designates a head of the PEU, not to convey a judgment about how an individual family is structured but as a means of organizing the data consistently. If a couple is economically dominant in the PEU, the head is the male in a mixed-sex couple or the older person in a same-sex couple. If a single person is economically dominant, that person is designated as the family head in this report.

Percentiles of the Distributions of Income and Net Worth

Throughout this article, references are made to various percentile groups of the distributions of income or net worth. For a given characteristic, a percentile can be used to define a family's rank relative to other families. For example, the 10th percentile of the distribution of income is the amount of income received by a family for whom just less than 10 percent

[67] For details on how these comparisons are structured and the results of comparisons for earlier surveys, see Rochelle L. Antoniewicz (2000), "A Comparison of the Household Sector from the Flow of Funds Accounts and the Survey of Consumer Finances" (Washington: Board of Governors of the Federal Reserve System, October), www.federalreserve.gov/econresdata/scf/scf_workingpapers.htm.

[68] For technical information about the construction of this index, see Kenneth J. Stewart and Stephen B. Reed (1999), "Consumer Price Index Research Series Using Current Methods, 1978–98," *Monthly Labor Review*, vol. 122 (June), pp. 29–38.

of families have lower income and 90 percent have higher income. The percentiles of the distributions of income and net worth used to define the income and net worth groups in the tables in the article are given in the following table:

Table A.2

Item	Survey year			
	2001	2004	2007	2010
Percentile of income				
20	20,600	21,800	21,500	20,400
40	37,800	39,000	38,200	35,600
60	63,000	61,700	62,500	57,800
80	100,800	102,800	102,900	94,600
90	145,600	148,900	147,600	142,300
Percentile of net worth				
25	15,700	15,300	14,800	8,300
50	106,100	107,200	126,400	77,300
75	351,800	378,800	390,600	301,700
90	907,000	959,600	955,600	952,500

The groups that are created when a distribution is divided at every 10th percentile are commonly referred to as deciles. Similarly, when a distribution is divided at every 20th (25th) percentile, the groups are known as quintiles (quartiles). Families in the first income decile, for example, are those with income below the 10th percentile.

Racial and Ethnic Identification

In this article, the race and ethnicity of a family in the SCF are classified according to the self-identification of that family's original respondent to the SCF interview. The questions underlying the method of classification used in the survey were changed in both 1998 and 2004. Starting in 1998, SCF respondents were allowed to report more than one racial identification; in surveys before then, only one response was recorded. For maximum comparability with earlier data, respondents reporting multiple racial identifications were asked to report their strongest racial identification first. In the 2010 SCF, 6.1 percent of respondents reported more than one racial identification, up from 5.4 percent in 2007 and 2.3 percent in 2004.

Beginning with the 2004 survey, the question on racial identification is preceded by a question on whether respondents consider themselves to be Hispanic or Latino in culture or origin; previously, such ethnic identification was captured only to the extent that it was reported as a response to the question on racial identification. The sequence of these two questions in the 2004 SCF is similar to that in the Current Population Survey (CPS). When families in the March 2004 CPS are classified in the way most compatible with the SCF, the proportion of Hispanic families is 10.5 percent; the 2004 SCF estimate is 11.2 percent. Differences in these proportions are attributable to sampling error and possibly to differences in the wording and context of the questions.

For greater comparability with the earlier SCF data, the data reported in this article ignore the information on ethnic identification available in the surveys since 2004, but respondents reporting multiple racial identifications in the surveys starting with 1998 are classified as "nonwhite or Hispanic." Of those who responded affirmatively to the question on Hispanic or Latino identification in 2010, 89.5 percent also reported "Hispanic or Latino" as one of their racial identifications, and 82.3 percent reported it as their primary racial identification. Because the question on Hispanic or Latino ethnicity precedes the one on racial

identification in the surveys from 2004 through 2010, the answer to the second of these two questions may have been influenced by the answer to the first.[69]

The Sampling Techniques

The survey is expected to provide a core set of data on family income, assets, and liabilities. The major aspects of the sample design that address this requirement have been constant since 1989. The SCF combines two techniques for random sampling. First, a standard multistage area-probability sample (a geographically based random sample) is selected to provide good coverage of characteristics, such as homeownership, that are broadly distributed in the population.

Second, a supplemental sample is selected to disproportionately include wealthy families, which hold a relatively large share of such thinly held assets as noncorporate businesses and tax-exempt bonds. Called the "list sample," this group is drawn from a list of statistical records derived from tax returns. These records are used under strict rules governing confidentiality, the rights of potential respondents to refuse participation in the survey, and the types of information that can be made available. Persons listed by *Forbes* magazine as being among the wealthiest 400 people in the United States are excluded from sampling.

Of the 6,492 interviews completed for the 2010 SCF, 5,012 were from the area-probability sample, and 1,480 were from the list sample; for 2007, 2,914 were from the area-probability sample, and 1,507 were from the list sample. The number of families represented in the surveys considered in this article is given by the following table:

Table A.3

Year	Number of families represented (millions)
2001	106.5
2004	112.1
2007	116.1
2010	117.6

The Interviews

Aside from the addition of new questions in the 2010 survey to address the financial relationships of businesses that are not publicly traded, the survey questionnaire has changed in only minor ways since 1989, except in a small number of instances in which the structure was altered to accommodate changes in financial behaviors, in types of financial arrangements available to families, and in regulations covering data collection. In these cases and in all earlier ones, every effort has been made to ensure the maximum degree of comparability of the data over time. Except where noted in the article, the data are highly comparable over time.

The generosity of families in giving their time for interviews has been crucial to the SCF. In the 2010 SCF, the median interview length was about 90 minutes. However, in some particularly complicated cases, the amount of time needed was substantially more than three hours. The role of the interviewers in this effort is also critical. Without their dedication and perseverance, the survey would not be possible.

[69] For a comprehensive discussion of standards for defining race and ethnicity, see Executive Office of the President, Office of Management and Budget (2002), "Provisional Guidance on the Implementation of the 1997 Standards for Federal Data on Race And Ethnicity," Executive Office of the President, www.whitehouse.gov/omb/fedreg_race-ethnicity.

The SCF interviews were conducted largely between the months of May and December in each survey year by NORC, a social science and survey research organization at the University of Chicago. The majority of interviews were obtained in person, although interviewers were allowed to conduct telephone interviews if that was more convenient for the respondent. Each interviewer used a program running on a laptop computer to administer the survey and collect the data.

The use of computer-assisted personal interviewing has the great advantage of enforcing systematic collection of data across all cases. The computer program developed to collect the data for the SCF was tailored to allow the collection of partial information in the form of ranges whenever a respondent either did not know or did not want to reveal an exact dollar figure.

The response rate in the area-probability sample is more than double that in the list sample. In both 2007 and 2010, about 70 percent of households selected for the area-probability sample actually completed interviews. The overall response rate in the list sample was about one-third; in the part of the list sample likely containing the wealthiest families, the response rate was only about one-half that level.

Weighting

To provide a measure of the frequency with which families similar to the sample families could be expected to be found in the population of all families, an analysis weight is computed for each case, accounting both for the systematic properties of the sample design and for differential patterns of nonresponse. The SCF response rates are low by the standards of some other major government surveys, and analysis of the data confirms that the tendency to refuse participation is highly correlated with net worth. However, unlike other surveys, which almost certainly also have differential nonresponse by wealthy households, the SCF has the means to adjust for such nonresponse. A major part of SCF research is devoted to the evaluation of nonresponse and adjustments for nonresponse in the analysis weights of the survey.[70]

Sources of Error

Errors may be introduced into survey results at many stages. Sampling error—the variability expected in estimates based on a sample instead of a census—is a particularly important source of error. Such error can be reduced either by increasing the size of a sample or, as is done in the SCF, by designing the sample to reduce important sources of variability. Sampling error can be estimated, and for this article, we use replication methods to do so.

Replication methods draw samples, called replicates, from the set of actual respondents in a way that incorporates the important dimensions of the original sample design. In the SCF, weights were computed for all of the cases in each of the replicates.[71] For each statistic for which standard errors are reported in this article, the weighted statistic is estimated using the replicate samples, and a measure of the variability of these estimates is combined with a measure of the variability due to imputation for missing data to yield the standard error.

[70] The weights used in this article are adjusted for differential rates of nonresponse across groups. See Arthur B. Kennickell (1999), "Revisions to the SCF Weighting Methodology: Accounting for Race/Ethnicity and Homeownership" (Washington: Board of Governors of the Federal Reserve System, January), www.federalreserve.gov/econresdata/scf/scf_workingpapers.htm.

[71] See Arthur B. Kennickell (2000), "Revisions to the Variance Estimation Procedure for the SCF" (Washington: Board of Governors of the Federal Reserve System, October), www.federalreserve.gov/econresdata/scf/scf_workingpapers.htm.

Other errors include those that interviewers may introduce by failing to follow the survey protocol or misunderstanding a respondent's answers. SCF interviewers are given lengthy, project-specific training and ongoing coaching to minimize such problems. Respondents may introduce error by interpreting a question in a sense different from that intended by the survey. For the SCF, extensive pretesting of questions and thorough review of the data tend to reduce this source of error.

Nonresponse—either complete nonresponse to the survey or nonresponse to selected items within the survey—may be another important source of error. As noted in more detail earlier, the SCF uses weighting to adjust for differential nonresponse to the survey. To address missing information on individual questions within the interview, the SCF uses statistical methods to impute missing data; the technique makes multiple estimates of missing data to allow for an estimate of the uncertainty attributable to this type of nonresponse.

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Use of Financial Services by the Unbanked and Underbanked and the Potential for Mobile Financial Services Adoption

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Mobile phone use has become a standard aspect of daily life for many Americans in the last decade. The increased use of these devices coupled with the evolution of technologies that enable consumers to conduct financial transactions using their mobile phones has the potential to change how consumers manage their finances as new services and tools emerge. In addition, innovative financial service technologies may help foster financial access and inclusion in the mainstream financial system for underserved consumers—those who are unbanked or underbanked. For these reasons, the Federal Reserve Board has been monitoring trends and developments in mobile financial services such as mobile banking and payments. In late December 2011 and early January 2012, the Board's Division of Consumer and Community Affairs (DCCA) conducted a survey in order to better understand consumers' use of and opinions about mobile financial services.[1]

Key Findings

Using data from the Board's Survey of Consumers and Mobile Financial Services (SCMFS), this article provides a description of unbanked and underbanked consumers, and examines their use of financial products and services (see Appendix A: Survey Data Collection). The article further explores how unbanked and underbanked consumers are making use of emerging mobile financial services technologies. The potential for mobile banking and mobile payments to expand access and inclusion to the mainstream financial system is also examined. Several key findings from the survey stand out:

- Approximately 11 percent of U.S. consumers are unbanked, and another 11 percent are underbanked.

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[1] See Matthew B. Gross, Jeanne M. Hogarth, and Maximilian D. Schmeiser (2012), "Consumers and Mobile Financial Services," report (Washington: Board of Governors of the Federal Reserve System, March), www.federalreserve.gov/econresdata/mobile-devices/files/mobile-device-report-201203.pdf.

- Unbanked and underbanked consumers are more likely than fully banked consumers to have lower incomes and be younger, minority, female, unmarried, unemployed, and unwilling to take financial risks.
- Unbanked and underbanked consumers are also more likely to use alternative financial service providers, such as check cashers; payday, title, and pawn lenders; or rent-to-own services.
- Sixty-three percent of unbanked consumers have a mobile phone, and 91 percent of underbanked consumers have a mobile phone.
- The most frequent mobile banking activity reported by respondents overall was checking account balances or recent transactions (90 percent), while the most frequent type of mobile payment activity was paying a bill online (47 percent).
- Underbanked consumers make comparatively heavy use of both mobile banking and mobile payments—28 percent have used mobile banking and 17 percent have used mobile payments in the past 12 months, compared with 21 and 12 percent, respectively, of fully banked consumers.

Why the Focus on Financially Underserved Groups?

Consumers' access to financial accounts and inclusion in the mainstream financial marketplace have long been on the minds of policymakers, who have explored ways to reduce barriers and increase access to mainstream financial services in order to encourage cost savings, public safety, disaster preparedness, and asset building for underserved groups.[2] For example, the EFT '99 initiative (developed to implement the Debt Collection Improvement Act of 1996) included a provision requiring selected federal payments to be made by direct deposit, spurring an interest in bringing unbanked households into the financial mainstream.[3] And in December 2010, the Treasury Department's Financial Management Service published rules requiring recipients of federal nontax payments, including many unbanked benefit recipients, to receive payment by electronic funds transfer. Those without a bank account for direct deposit will be issued a prepaid debit card as part of the Go Direct program.[4]

Data from the Federal Reserve Board's 2010 Survey of Consumer Finances (SCF) show that 7.5 percent of households (about 8.8 million households) have no transaction accounts (that is, no checking, savings, money market deposit accounts, money market mutual funds,

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[2] Signe-Mary McKernan and Michael Sherraden (2008), *Asset Building and Low-Income Families* (Washington: Urban Institute Press); and Michael Barr (2012), *No Slack: The Financial Lives of Low-Income Americans* (Washington: Brookings Institution). For example, the Department of the Treasury has an Office of Financial Education and Financial Access and the Federal Deposit Insurance Corporation has an Advisory Committee on Economic Inclusion.

[3] For a description of the EFT '99 initiative, see Jeanne M. Hogarth and Kevin H. O'Donnell (1999), "Banking Relationships of Lower-Income Families and the Governmental Trend toward Electronic Payment," *Federal Reserve Bulletin*, vol. 87, pp. 459–73, www.federalreserve.gov/pubs/bulletin/1999/0799lead.pdf.

[4] 31 CFR 208; see 73 *Fed. Reg.* 80315 (December 22, 2010), www.gpo.gov/fdsys/pkg/FR-2010-12-22/pdf/2010-32117.pdf. For information on Go Direct, see www.godirect.gov/gpw/index.gd. The rule requires anyone applying for benefits on or after May 2011 to receive all payments electronically via direct deposit to a deposit account at a depository institution or via a prepaid card. Treasury has contracted with a commercial bank to make Direct Express® Debit MasterCard® prepaid card accounts available to recipients who will not be receiving benefits via direct deposit; these cards can be used like other debit cards, and funds that recipients receive through the card are FDIC insured. There is no cost to sign up for the card and no monthly fee, although there are fees for some optional transactions (such as making more than one ATM withdrawal in a single month, receiving a paper statement and getting a replacement card). Recipients currently receiving benefits via checks will be required to switch to an electronic payment method by March 2013.

or call or cash accounts at brokerages).[5] In comparison, the 2011 Federal Deposit Insurance Corporation (FDIC) National Survey of Unbanked and Underbanked Households found that 8.2 percent of U.S. households (approximately 10 million households) were unbanked.[6] Thus, while the proportion of unbanked households may seem small, the absolute number of these households is quite large.

Being unbanked in today's financial marketplace can be problematic for consumers. Consumers who operate on a cash-only basis may face fees for cashing checks and for money orders needed to pay some bills. For example, the cost of using a check-cashing service can range from about 2 percent of the face value of the check when regulated by states to 4 or 5 percent when not.[7] In addition, conducting transactions only in cash presents financial and personal risks, since there is no recourse when cash is lost or stolen. Further, consumers who prefer cash may not be building a financial identity through consumer and credit reporting agencies. Finally, many of the consumer protections available to fully banked consumers, such as FDIC insurance and protections provided to credit and debit card users under the Truth in Lending Act and the Electronic Fund Transfer Act, are not available to consumers who use alternative financial services. For these reasons, there may be some benefits for consumers to connect with mainstream banking and financial services.

In addition to unbanked consumers, there is a segment of consumers with bank accounts who also use alternative financial service providers, such as check cashers, money order providers, payday lenders, pawn shops, auto title lenders, or rent-to-own merchants. The FDIC survey report estimates that 20.1 percent of households are underbanked; that is, they use one or more of these alternative financial services. These service providers often charge higher implicit interest rates or fees than banks might charge and may lack some consumer protections. Again, there may be some benefit for consumers to conduct more transactions with mainstream financial services.[8]

Who Are the Unbanked and Underbanked?

In this article, we define an unbanked consumer as someone who does not have a checking, savings, or money market account; also, the consumer's spouse or partner does not have such an account. An underbanked consumer is someone who has a checking, savings, or money market account but who also has used at least one alternative financial service in the past 12 months, such as an auto title loan, payday loan, check-cashing service, or payroll card. By contrast, we refer to a consumer who has a bank account and does not use alternative financial services as "fully banked."

The proportions of respondents who report being unbanked or underbanked in this survey are similar to those found in previous national studies, and differences can be explained in part by variation in the definitions. As estimated from the data collected in this study, the

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5 Jesse Bricker, Arthur B. Kennickell, Kevin B. Moore, and John Sablehaus (2012), "Changes in U.S. Family Finances from 2007 to 2010: Evidence from the Survey of Consumer Finances," *Federal Reserve Bulletin*, vol. 98 (2), pp. 1–80, www.federalreserve.gov/pubs/bulletin/2012/PDF/scf12.pdf.

6 Federal Deposit Insurance Corporation (2012), 2011 National Survey of Unbanked and Underbanked Households (Washington: FDIC, September), www.fdic.gov/householdsurvey.

7 Martha Perine Beard (2010), "Reaching the Unbanked and Underbanked," Federal Reserve Bank of St. Louis, *Central Banker*, vol. 20 (Winter), www.stlouisfed.org/publications/pub_assets/pdf/cb/2010/CB_winter_10.pdf.

8 Consumers may choose to use alternative financial services for a number of reasons (convenience, comfort, etc.); however, they pay a higher cost for these benefits. See William H. Greene, Sherrie L.W. Rhine, and Maude Toussaint-Comeau (2003), "The Importance of Check-Cashing Business to the Unbanked: Racial/Ethnic Differences," working paper (Chicago: Federal Reserve Bank of Chicago, August), www.chicagofed.org/digital_assets/publications/working_papers/2003/wp2003-10.pdf.

national proportion of unbanked consumers is about 11 percent of the U.S. adult population. This number compares with approximately 8 percent of households based on the 2011 FDIC National Survey of Unbanked and Underbanked Households and 7.5 percent of households based on the Federal Reserve Board's 2010 SCF. Moreover, the data for this study indicate that an additional 11 percent of the U.S. population is underbanked. This rate is well below the 20 percent underbanked rate found in the FDIC study; however, the definition of underbanked here is narrower than the FDIC's definition, as the latter includes consumers' use of services such as money orders when classifying an individual as underbanked.[9]

Respondents to the SCMFS report a variety of reasons for not having a bank account. Of the unbanked participants in the study, 24 percent say they do not like dealing with banks, and 24 percent indicate they do not write enough checks to make a bank account worthwhile. Another 13 percent say that the fees and service charges are too high, and 10 percent say that no bank will give them an account (see box 1, "Why Are the Unbanked Unbanked?").

Household Characteristics of the Unbanked and Underbanked

In general, unbanked and underbanked households tend to have low-to-moderate incomes (table 1). Unbanked households are most likely to be low income: 61 percent report incomes of less than $25,000. Underbanked households are more likely to have moderate incomes in the $25,000 to $39,999 range.[10]

Unbanked households are younger than others, with a median age of 39. More than one out of three (36 percent) are ages 18 to 29 while only 8 percent are over age 60. Nearly three-fourths of unbanked households (74 percent) report having a high school education or less, consistent with the lower income profile for this group. The unbanked are less likely to be homeowners, with only 42 percent owning their home, compared to 60 percent of the underbanked and 76 percent of the fully banked.

The survey question regarding banking status was worded as "Do you or does your spouse/partner currently have a checking, savings, or money market account?" Unbanked respondents are more likely to be unmarried, and in particular, they are more likely to have never married (consistent with being younger). Households with more people may mean there is greater opportunity for at least one person in the household to have an account.

Black respondents are more likely to report that their households are unbanked or underbanked, consistent with findings from other studies.[11] Respondents in the "other" race category and those reporting two or more races (but who are non-Hispanic), are more likely to be in unbanked households than non-Hispanic white respondents.

Individuals who are experiencing unemployment, but who are still in the labor force, are more likely to be unbanked. Nearly one out of three respondents who live in an unbanked household (32.5 percent) report that they are temporarily laid off or looking for work.

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[9] The FDIC defines the underbanked as those who have used nonbank money orders, nonbank check-cashing services, payday loans, rent-to-own agreements, pawn shops, refund-anticipation loans, or nonbank remittances within the last year. In defining unbanked, the FDIC and SCF surveys ask if anyone in the respondent's *household* has a bank account, whereas we only ask about the spouse/partner. Some of these differences may be due to the margins of error in the various surveys.

[10] All the differences in characteristics by banking status discussed in this section are statistically significant at the 5 percent level when controlling for other characteristics in a regression analysis. These results are available from the authors upon request.

[11] Hogarth and O'Donnell, "Banking Relationships"; and FDIC, 2011 National Survey.

Box 1. Why Are the Unbanked Unbanked?

According to several studies, the most frequently reported reason for a family not having an account with a deposit-taking institution is that they have little to no month-to-month financial savings to deposit in an account.[1] Other studies cite negative past experiences, mistrust of banks, and the greater convenience found in alternative financial services as reasons why consumers choose to be unbanked.[2] Finally, some consumers may choose to abstain from traditional bank services for cultural or other reasons. For example, a qualitative study of the unbanked and underbanked populations in the 10th Federal Reserve District (Kansas City) found differences between Hispanic and non-Hispanic consumers in their view of how they managed financial resources and how that affected their desire to have a checking account.

In both the survey discussed here and the Board's 2010 Survey of Consumer Finances (SCF), the top three reasons consumers gave for not having a bank account or a checking account were consistent: consumers reported that they did not like dealing with banks, they didn't think they wrote enough checks to make it worthwhile, and they thought the fees and service charges were too high (see table A). Respondents in this survey also reported that they did not think any bank would give them an account, while respondents in the SCF reported that they thought they did not have enough money or that they did not need or want an account. Minimum balance requirements were cited by 7 percent of the SCF respondents, but by an insignificant number of this survey's respondents, as a reason for not having an account.

Table A. Most important reason for not having a bank account

Percent

	Mobile Financial Services Survey[1]	2010 Survey of Consumer Finances[2]
I don't like dealing with banks	24.2	27.8
I don't write enough checks to make it worthwhile	23.5	20.3
The fees and service charges are too high	13.3	10.6
No bank will give me an account	10.2	...
The minimum balance is too high	*	7.4
No bank has convenient hours or location	*	...
Do not have enough money	...	10.3
Do not need/want an account	...	7.3
Cannot manage or balance a checking account	...	4.7
Credit problems	...	4.2
Other	17.8	7.4

1 See www.federalreserve.gov/econresdata/mobile-device-report-201203.pdf.

2 See www.federalreserve.gov/pubs/bulletin/2012/PDF/scf12.pdf.

... Not applicable (response was not provided in the survey instrument).

* Ten or fewer observations.

1 John Caskey (2005), "Reaching Out to the Unbanked," in M.W. Sherraden, ed., *Inclusion in the American Dream: Assets, Poverty, and Public Policy* (New York: Oxford University Press); Jeanne M. Hogarth, Christoslav E. Anguelov, and Jinkook Lee (2004), "Why Don't Households Have a Checking Account?" *Journal of Consumer Affairs*, vol. 38 (1), pp. 1–34; and Jeanne M. Hogarth, Christoslav E. Anguelov, and Jinkook Lee (2004), "Why Households Don't Have Checking Accounts," *Economic Development Quarterly*, vol. 17 (1), pp. 75–94.

2 Federal Reserve Bank of Kansas City (2010), "Unbanked and Underbanked Consumers in the 10th Federal Reserve District," report (Kansas City, MO: Federal Reserve Bank of Kansas City, May), www.kansascityfed.org/publicat/research/community/Unbanked.Report.pdf.

Use of Alternative Financial Services

Previous studies have shown that the underbanked and unbanked are more likely to use alternative financial service providers, such as check cashers; payday, title, and pawn lenders; or rent-to-own services, even though alternative financial service providers are often in

Table 1. Sample characteristics
Percent, except where noted

	Full sample	Fully banked	Underbanked	Unbanked
Observations	100	78	11	11
Income				
Less than $25,000	21.5	15.6	24.4	60.8
$25,000–$39,999	17.3	16.6	25.3	13.6
$40,000–$74,999	26.2	28.6	22.2	13.4
$75,000–$99,999	12.9	14.2	12.2	4.8
$100,000 or more	22.0	24.9	15.8	7.4
Age				
Average age (in years)	46.6	47.9	44.8	39.2
Median age (in years)	47.0	48.0	43.0	39.0
Age categories				
18–29	21.4	19.8	19.0	36.0
30–44	26.0	24.6	33.1	27.3
45–60	27.6	27.2	28.2	29.1
Over 60	25.1	28.4	19.7	7.6
Education				
Less than high school	12.7	9.4	11.8	35.7
High school or GED	30.4	28.5	34.4	39.0
Some college	28.8	29.9	31.3	18.5
Bachelor's degree or higher	28.2	32.2	22.6	6.8
Gender				
Female	51.6	50.8	60.6	48.4
Male	48.4	49.2	39.4	51.6
Marital Status				
Married	52.8	57.2	48.4	25.7
Widowed	4.2	4.3	*	5.2
Divorced	10.5	9.6	16.4	10.4
Separated	1.7	1.1	*	5.2
Never married	21.0	18.1	19.4	42.8
Living with partner	9.9	9.6	11.1	10.8
Race/ethnicity				
White, non-Hispanic	67.9	74.0	57.0	37.2
Black, non-Hispanic	11.6	7.8	20.7	29.0
Other, non-Hispanic	5.6	5.4	5.0	8.6
Hispanic	13.7	11.9	16.1	22.9
2 or more races, non-Hispanic	1.2	1.0	*	*
Employment status				
Working as a paid employee	48.7	50.2	54.7	31.8
Self-employed	6.9	6.9	8.4	4.9
On temporary layoff from a job	1.2	0.9	0.7	4.2
Looking for work	8.5	5.9	6.0	28.3
Retired	17.3	20.3	10.3	*
Disabled	8.0	6.1	12.4	17.7
Other	9.3	9.7	7.4	9.3
Region				
Northeast	18.4	19.6	14.9	14.3
Midwest	21.7	21.6	25.1	19.9
South	36.6	35.1	42.9	40.6
West	23.2	23.8	17.1	25.2
Own home	70.2	75.8	60.0	41.5
House size				
Mean number of persons	2.8	2.7	3.0	3.0
Median number of persons	2	2	2	3
Proportion of households with child under 18	35.8	33.9	42.9	43.1

* Ten or fewer observations.

Table 2. Experience with alternative financial services
Percent

	Full sample	Fully banked	Underbanked	Unbanked
Credit				
Use payday loan ever	11.2	6.0	42.6	15.5
Used payday loan in last 12 months	29.9	*	64.2	16.3
Use auto title loan	3.6	*	29.5	*
Use layaway	3.8	*	28.8	5.4
Payments				
Use check casher	4.1	*	26.8	10.1
Prepaid cards				
Gift card	48.0	51.5	48.8	22.0
General-purpose card	14.5	13.2	17.9	20.6
Payroll card	1.7	*	8.4	6.6
Government card	4.8	3.2	6.0	14.8
None	45.4	45.0	40.2	54.6
Reloaded prepaid card in last 12 months	59.7	33.3	53.7	65.1
Most recent reload				
Past 7 days	21.2	24.2	*	*
Past 30 days	41.1	35.4	53.3	44.6
Past 90 days	20.0	18.3	28.8	*
Past 12 months	17.1	21.1	*	*
More than 12 months ago	*	*	*	*

* Ten or fewer observations.

the same neighborhoods as financial institutions.[12] Responses to the SCMFS are consistent with these other studies. Two-fifths of underbanked households had used a payday loan; of these, two-thirds had used one within the past 12 months (table 2). In comparison, only about one out of six unbanked households had ever used a payday loan; this dropped to one in about twenty among fully banked households. Vehicle title loans and layaway were used less frequently; about three out of ten underbanked households report using these services.

The underbanked are also more likely than others to report using check cashers; about one out of four underbanked respondents report using this type of service. While it might seem surprising that the unbanked do not make more use of check cashers, there is some evidence that these households avoid check-cashing fees by cashing checks at grocery stores and some large retailers when making purchases.[13]

The use of prepaid cards has grown rapidly over the past several years.[14] General-purpose reloadable prepaid cards usually carry one of the major payment-card network logos and can act as a substitute for a transaction account in that funds from wages, tax refunds, government benefits, and other sources can be loaded onto the cards, which then can be used for payments online or in stores. One out of seven respondents report using a general-purpose reloadable card, while substantially fewer report using an employer's payroll card or

[12] FDIC, 2011 National Survey; Timothy Bates and Constance R. Dunham (2003), "Introduction to Focus Issue: Use of Financial Services by Low-Income Households," *Economic Development Quarterly*, vol. 17 (2), pp. 3–7; and Matt Fellowes and Mia Mabanta (2008), "Banking on Wealth: America's New Retail Banking Infrastructure and Its Wealth-Building Potential," research brief (Washington: Brookings Institution, January), www.brookings.edu/~/media/research/files/reports/2008/1/banking%20fellowes/01_banking_fellowes.pdf.

[13] Michael S. Barr, Jane K. Dokko, and Benjamin J. Keys (2009), "And Banking for All?" Finance and Economics Discussion Series Working Paper No. 2009-34 (Washington: Board of Governors of the Federal Reserve System, August).

[14] Javelin Strategy and Research (2012), "Prepaid Cards and Products in 2012: Enabling Financial Access for Underbanked and Gen Y Consumers," report (Pleasanton, CA: Javelin Strategy and Research).

Table 3. Financial capability measures
Percent responding correctly

	Full sample	Fully banked	Underbanked	Unbanked
Financial literacy questions[1]				
Imagine that the interest rate on your savings account was 1% per year and inflation was 2% per year. After 1 year, how much would you be able to buy with the money in this account?	70.4	74.8	65.5	44.7
Considering a long time period (for example 10 or 20 years), which asset normally gives the highest return?	55.8	60.9	46.4	29.9
If an investor who only owns two stocks right now decides to instead spread their money among many different assets (i.e., more stocks, add bonds, add real estate), their risk of losing money on their entire portfolio will:	52.4	55.9	46.6	34.2
If you were to invest $1,000 in a stock mutual fund for a year, it would be possible to have less than $1,000 when you withdraw your money.	76.0	80.8	67.7	50.5
Suppose you owe $1,000 on a loan and the interest rate you are charged is 10% per year compounded annually. If you didn't make any payments on this loan, at this interest rate, how many years would it take for the amount you owe to double?	34.2	37.7	28.7	14.1
Financial risk questions[2]				
Are you willing to take:				
Substantial risk for substantial gain	3.4	3.4	*	*
Above-average risk for above-average gain	15.0	16.3	14.8	6.3
Average risk for average gain	37.9	42.4	30.9	13.4
No risk	43.6	37.9	51.1	76.4

1 The exact wording of the financial literacy questions and their possible responses is provided in appendix B. Correct answers are bolded.

2 For financial risk questions, percent of affirmative responses.

* Ten or fewer observations.

some type of government benefits card. Underbanked and unbanked respondents are more likely to report using these reloadable cards than fully banked respondents.

Among those who used reloadable cards, half the underbanked and two-thirds of the unbanked report reloading funds onto their cards. The highest proportion report doing this within the past 30 days, consistent with government benefits payments and some employer pay cycles.

Measures of Financial Capability

The survey also tested the financial knowledge of respondents with a commonly used set of questions pertaining to interest rates, inflation, return on assets, portfolio diversity, mutual funds, and repayment methods (table 3; see appendix B for full text of financial literacy questions).[15] Unbanked households were less likely to give correct answers than underbanked or fully banked households.

Fewer than half of the unbanked respondents correctly answered a question about inflation, compared with two-thirds of the underbanked respondents and three-fourths of the fully banked respondents. About three out of ten unbanked households correctly answered

15 Annamaria Lusardi and Peter Tufano (2009), "Debt Literacy, Financial Experiences, and Overindebtedness," NBER Working Paper No. 14808 (Cambridge, MA: National Bureau of Economic Research, March); and Annamaria Lusardi, Olivia S. Mitchell, and Vilsa Curto (2010), "Financial Literacy among the Young," *Journal of Consumer Affairs,* vol. 44 (2), pp. 358–80.

a question about relative rates of return on savings accounts, government bonds, and stocks, compared with about half of the underbanked and three-fifths of the fully banked. Finally, about half of the unbanked households correctly answered a question about the risks associated with investing in stock mutual funds (that is, one could lose some of the principle). In comparison, two-thirds of the underbanked households and four-fifths of the fully banked households correctly answered this question.

Unbanked respondents were the most risk-averse among the three groups; three-fourths of them were unwilling to take any financial risk, compared with half of the underbanked respondents and just over one-third of the fully banked respondents. This risk aversion may be related to lack of experience with a range of financial products and services, and lack of experience may explain, in part, why the unbanked scored low relative to other respondents on the financial capability questions. The greater risk aversion among the unbanked may also reflect the fact that low-income individuals have little, if any, margin for error or loss in their finances.

Mobile Phone Ownership and Use

The survey examined respondents' ownership and use of mobile phones as well. Overall, 87 percent of respondents to the SCMFS said they had a mobile phone (table 4). The unbanked are less likely to have a mobile phone than their underbanked or fully banked counterparts. Among the unbanked, 63 percent have a mobile phone compared with 91 percent of the underbanked and 90 percent of the fully banked.

Among mobile phone owners, more than two-fifths have smartphones.[16] Underbanked households are more likely than their unbanked and fully banked counterparts to have smartphones. Among underbanked households with mobile phones, 57 percent have smartphones compared with 26 percent of unbanked and 44 percent of fully banked households (see box 2, "Smartphone Adoption").

Potential for Mobile Financial Services to Reach Underserved Consumers

Although consumers in the United States have been slow to adopt mobile financial services, the experiences of some developing countries offer a glimpse of the potential benefits that using mobile phones to conduct transactions and access services can bring to underserved populations as well as to the financial system.[17]

Globally, Kenya is a leader in mobile payments implementation and adoption. Kenya has received substantial international attention for the extent to which the M-PESA service has promoted financial inclusion through mobile banking and payments. World Bank Findex Data reveals that 60 percent of Kenyan adults over the age of 15 use mobile payments to send money, and 66 percent use mobile payments to receive money. Among the 144 countries surveyed, the use of mobile financial services in Kenya was 20 percentage points higher than in any other country.[18] A recent study of Kenya reveals that in 2011, nearly

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[16] This article uses *smartphone* to refer to mobile phones that can access the web, send e-mails, and interact with computers and *feature phone* to refer to more traditional mobile phones that lack such capabilities.

[17] Catherine J. Bell, Jeanne M. Hogarth, and Eric Robbins (2009), "U.S. Households Access to and Use of Electronic Banking, 1989–2007," *Federal Reserve Bulletin*, vol. 97, pp. A99–A121, www.federalreserve.gov/pubs/bulletin/2009/pdf/OnlineBanking09.pdf.

[18] Asli Demirguc-Kunt and Leora Klapper (2012), "Measuring Financial Inclusion: The Global Findex Database," World Bank Policy Research Working Paper 6025 (Washington: World Bank).

Table 4. Mobile phone ownership and mobile banking
Percent

	Full sample	Fully banked	Underbanked	Unbanked
Have mobile phone	87.1	89.7	91.4	63.4
Smartphone	43.9	43.9	56.9	26.3
Feature phone	55.9	55.9	43.1	73.3
Use mobile banking—all mobile phone users				
Now	20.9	20.8	28.4	9.7
In next 12 months	11.3	9.0	22.4	18.7
Ever	17.0	16.6	25.5	11.3
Use mobile banking—smartphone owners				
Now	42.0	42.7	44.3	*
In next 12 months	22.9	20.1	35.3	*
Ever	27.3	25.4	39.2	*
Use mobile banking—feature phone owners				
Now	4.3	3.9	*	*
In next 12 months	5.9	3.9	12.4	15.8
Ever	13.2	13.5	17.4	*
Used mobile banking for				
Check balance in account	90.1	90.6	88.6	91.3
Download bank app	48.1	49.8	43.1	*
Transfer money between accounts	41.7	38.9	54.9	*
Set up text message alert	33.4	35.7	30.0	*
Low-balance alert	66.4	65.3	71.5	*
Payment due alert	31.7	32.1	*	*
Savings reminder	*	*	*	*
Fraud alert	30.3	30.9	*	*
Action after receiving alert				
Transferred money into account	57.6	58.7	*	*
Deposited money into account	16.3	*	*	*
Reduced spending	41.2	45.4	*	*
Payment alerts improved paying on time				
Yes, by a lot	37.3	30.6	*	*
Yes, by a little	40.5	43.7	*	*
No	*	*	*	*
Satisfaction with mobile banking				
Very satisfied	63.7	62.7	60.8	97.4
Somewhat satisfied	33.0	33.5	37.8	*
Somewhat dissatisfied	*	*	*	*
Very dissatisfied	*	*	*	*

* Ten or fewer observations.

$10 billion—about 30 percent of Kenya's GDP—was transferred through mobile payments.[19] More than 20 other countries report having a strategy for mobile banking and payments as part of the innovations in their payment systems.[20]

The international success of the microfinance industry in developing nations has demonstrated that with appropriate products and services, even those individuals in extreme poverty can be bankable.[21] In India, mobile financial services are viewed as a means of extending financial access to the roughly 43 percent of the population who are unbanked, with

[19] Anjana Ravi and Eric Tyler (2012), "Savings for the Poor in Kenya," report by the Savings for the Poor Innovation and Knowledge Network (Washington: New American Foundation, May).

[20] Bank for International Settlements (2012) "Innovations in Retail Payments," Committee on Payment and Settlement Systems, www.bis.org/publ/cpss102.pdf.

[21] Janine Firpo (2005), "Banking the Unbanked: Technology's Role in Delivering Accessible Financial Services to the Poor," SEMBA Consulting, www.sevaksolutions.org/docs/Banking%20the%20Unbanked.pdf.

Box 2. Smartphone Adoption

In the Survey of Consumers and Mobile Financial Services (SCMFS), a smartphone is defined as "a mobile phone with features that may enable it to access the web, send e-mails, and interact with computers. Smartphones include the iPhone, BlackBerrys, as well as Android and Windows Mobile powered devices." Data from the survey are compared with results from relevant reports by the Pew Research Center and Javelin Strategy and Research.[1]

Approximately 87 percent of respondents to the SCMFS have mobile phones, compared with 83 percent in the Pew survey and 85 percent in the Javelin survey. Of respondents who have mobile phones, approximately 44 percent have smartphones, compared with 42 percent in the Pew study and 45 percent in the Javelin study.

Among smartphone owners, 51 percent are women. Smartphone owners tend to be younger than the overall population: 32 percent of smartphone owners are between ages 18 and 29, 35 percent are between ages 30 and 44, 22 percent are between ages 45 and 59, and 11 percent are age 60 and over.

The racial composition of smartphone owners reflects that of the overall population except that Hispanics are slightly more likely to own smartphones. Among smartphone owners, 65 percent are white, 12 percent are black, 16 percent are Hispanic, and 6 percent are classified as other.

Smartphone owners seem to have higher educational attainment than the overall population: 28 percent have a high school degree or less, while 33 percent have completed some college and 39 percent have a bachelor's degree or higher.

Smartphone owners also have higher incomes. Among smartphone owners, 12 percent earn less than $25,000 a year; 14 percent earn between $25,000 and $39,999; 26 percent earn between $40,000 and $74,999; 14 percent earn between $75,000 and $99,999; and 33 percent earn $100,000 or more a year.

1 Aaron Smith (2011), "Smartphone Adoption and Usage," report (Washington: Pew Research Center, July), http://pewinternet.org/~/media//Files/Reports/2011/PIP_Smartphones.pdf; and Javelin Strategy and Research (2011), "Mobile Banking, Smartphone and Tablet Forecast 2011–2016: Mobile Banking Moves Mainstream to Mid-Sized, Community Banks, and Credit Unions," report (Pleasanton, CA: Javelin Strategy and Research).

telecom companies and banks working together to offer new services, such as mobile savings accounts or remittance payments.[22]

However, the challenges of many developing countries have been unique in that, in many cases, no physical banking or payments infrastructure existed in the first place, making banking in remote areas more difficult. In these countries, mobile financial services are filling a void. For the United States, the presence of a longstanding banking and payments infrastructure may mean different challenges in the diffusion of mobile financial services.[23] Ninety-two percent of the top 25 financial institutions by deposits already offer mobile banking services, while 17 percent of credit unions and 15 percent of community banks offer mobile banking, although the prevalence varies with the size of the institution.[24] As the comfort level with mobile financial services among the unbanked and underbanked

22 "Airtel, Axis Bank Join Hands for Mobile Banking," (2012) *Times of India*, May 16, www.timesofindia.indiatimes.com/business/india-business/Airtel-Axis-Bank-join-hands-for-mobile-banking/pmarticleshow/13174195.cms?prtpage=1.

23 Darin Contini, Marianne Crowe, Cynthia Merritt, Richard Oliver, and Steve Mott (2011), "Mobile Payments in the United States: Mapping Out the Road Ahead," report (Atlanta: Federal Reserve Bank of Atlanta), www.frbatlanta.org/documents/rprf/rprf_pubs/110325_wp.pdf.

24 Javelin Strategy and Research (2011), "2011 Mobile Banking Financial Institution Scorecard: Money Begins to Move on Mobile," report (Pleasanton, CA: Javelin Strategy and Research); and Independent Community

increases, the use of new and innovative ways to reach these marginalized populations creates opportunities for new relationships with financial institutions.

Use of Mobile Banking and Payments

Although a "digital divide" in computer Internet access still exists across the socioeconomic spectrum in the United States, this divide is significantly narrower for mobile phone access.[25] As noted earlier, a high proportion of unbanked and underbanked respondents to the SCMFS report having mobile phones (63 percent and 91 percent, respectively). The underbanked, in particular, already make substantial use of services such as mobile banking and mobile payments.

Mobile Banking

In the survey, mobile banking was defined as using "a mobile phone to access your bank account, credit card account, or other financial account. This can be done either by accessing your bank's web page through the web browser on your mobile phone, via text messaging, or by using an application downloaded to your mobile phone." Nearly 21 percent of the mobile phone owners say they have used some form of mobile banking in the past 12 months, and another 11 percent expect to use mobile banking in the next 12 months. Mobile banking is highly correlated with having a smartphone—42 percent of smartphone owners report using mobile banking compared with 4 percent of feature phone owners. Underbanked households are more likely than others to have used mobile banking (28 percent, compared with 10 percent and 21 percent for unbanked and fully banked respondents, respectively). Also, a higher proportion of underbanked respondents expects to use mobile banking in the next 12 months—22 percent, versus 9 percent of fully banked and 19 percent of unbanked. In comparison, more than two-thirds of fully banked and underbanked respondents report using online banking with a personal computer (see box 3, "Internet Access and Online Banking").

While it may seem counterintuitive for unbanked households to use their phones for banking, these respondents may have had a bank account within the past 12 months. They may be also referring to using their phones with another financial account, such as a prepaid or payroll card.

Across all levels of banking, nine out of ten mobile banking respondents use their phones to check balances and recent transactions in their accounts, the most-frequently reported mobile banking task. The next most-frequent use, reported by fewer than half the respondents, is to download a bank "app" to their phones. About half of fully banked respondents report downloading an app, compared with about two-fifths of underbanked respondents. More than half of the underbanked respondents report using mobile banking to transfer funds between accounts compared with nearly two-fifths of fully banked respondents.

Consumers who use mobile banking generally are satisfied with their mobile banking experience. The unbanked are the most satisfied with their mobile banking experience: close to 100 percent report being very satisfied. The underbanked and fully banked have similar satisfaction levels with their mobile banking experience: about three-fifths report being very

Bankers of America (2010), 2010 ICBA Community Bank Technology Survey, (Washington: ICBA), www.icba.org/files/ICBASites/PDFs/2010TechnologySurveyResults.pdf.

[25] Aaron Smith (2011), "Smartphone Adoption and Usage," report (Washington: Pew Research Center, July), http://pewinternet.org/~/media//Files/Reports/2011/PIP_Smartphones.pdf.

Box 3. Internet Access and Online Banking

Ninety-six percent of respondents to the Survey of Consumers and Mobile Financial Services report regular access to the Internet, and four out of five report accessing the Internet at home (see table A).[1] Those with bank accounts were also asked if they used online banking with a desktop, laptop, or tablet computer in the past 12 months; two-thirds of the fully banked and underbanked report using online banking.

Results from previous phone-based surveys show a smaller percentage of respondents with regular Internet access, generally ranging between 71 and 78 percent of the population.[2] Despite the widespread adoption of computers, tablets, and smartphones, a significant portion of consumers do not have access to the convenience of online banking due to the lack of regular Internet access. Moreover, the vulnerable groups that could potentially benefit from readier access to financial institutions through the Internet are those with low rates of Internet access.[3]

Table A. Internet access and online banking

Percent

	Full sample	Fully banked	Underbanked	Unbanked
Have regular access to the Internet at home or elsewhere	96.2	96.5	99.8	86.6
Place where consumer uses the Internet most often				
Home	81.4	80.6	80.4	85.8
Work	14.5	16.1	15.0	4.6
School	1.0	*	*	*
Library	1.4	*	*	*
Someone else's home	0.9	*	*	*
Use online banking with desktop, laptop, or tablet computer in past 12 months	67.8	67.9	68.7	*

Note: Accessing the Internet at school, libraries, or someone else's home were mentioned by fewer than 10 respondents in each category; access at Internet cafés was mentioned by fewer than 10 respondents.

* Ten or fewer observations.

[1] See appendix A for a detailed discussion of the survey methodology and the representativeness of the sample.

[2] M. Rebecca Blank and E. Lawrence Strickling (2011), "Exploring the Digital Nation," report (Washington: Department of Commerce), www.esa.doc.gov/sites/default/files/reports/documents/exploringthedigitalnation-computerandinternetuseathome.pdf; and Kathryn Zickuhr and Aaron Smith (2012), "Digital Differences," report (Washington: Pew Research Center, April), http://pewinternet.org/Reports/2012/Digital-differences/Overview.aspx.

[3] Zickuhr and Smith, "Digital Differences."

satisfied, while about one-third report being somewhat satisfied with their experience. These high levels of satisfaction are somewhat as expected, given that consumers are choosing to use mobile banking as a complement to other access channels (see box 4, "Why Aren't Consumers Using Mobile Banking and Payments?").

Text Messages

About one-third of all respondents who use mobile banking also use text message alerts. Text messages have the potential to help consumers manage their accounts by alerting them when balances are running low or when bill payments are due and to remind people of savings goals.[26] Furthermore, text messages work equally well with feature phones as with smartphones. The most common text message alert that respondents had set up was a low-balance alert—about two-thirds of all respondents who use text messaging had set up this type of alert. About one-third had also set up reminders for when bill payments were due, and nearly one-third report setting up fraud alerts.

[26] Dean Karlan and Jacob Appel (2011), *More Than Good Intentions* (New York: Penguin Books).

Box 4. Why Aren't Consumers Using Mobile Banking and Payments?

Among those individuals in our survey who do not use mobile banking, but do have a mobile phone, the primary reasons they gave for not using mobile banking were that their banking needs were already being met with existing services or that they have concerns about the security (see table A). Reasons for not adopting mobile banking are similar between the fully banked and underbanked. Not surprisingly, the reasons why the unbanked have not adopted mobile banking are significantly different from these other two groups. The most common reason for not adopting mobile banking, listed by 50 percent of the unbanked, was simply that they don't have a bank account. This reason was followed by security concerns and lack of trust in the technology (25 percent and 21 percent, respectively).

Among those respondents who do not use mobile payments, the most commonly cited reasons were concerns about security (42 percent), not seeing any benefits to using mobile payments (37 percent), and that it was easier to pay with another method such as cash or credit cards (36 percent). The primary reasons for not using mobile payments varied with banking status. While security was consistently the number one concern, the unbanked indicated significant lack of trust in the technology (31 percent) relative to the underbanked (16 percent) and the fully banked (19 percent). The unbanked also cited lacking the necessary feature on the phone as a major impediment to adoption (29 percent), as did the fully banked (32 percent). The underbanked were least likely to indicate that their phones lacked the necessary feature to perform mobile payments, with only 21 percent citing this reason. This is consistent with the underbanked having the highest rate of smartphone ownership among the three groups. Lastly, the unbanked were the least likely to indicate that they did not see any benefit from using mobile payments, with 15 percent citing this as a reason they do not use mobile payments, relative to 30 percent of the unbanked and 40 percent of the fully banked. This may indicate that the unbanked are open to using mobile technology as a means of performing financial transactions, provided their concerns about the security of the technology are addressed.

Table A. Reasons for not using mobile banking and mobile payments

Percent

	Full sample	Fully banked	Underbanked	Unbanked
Mobile banking				
Banking needs already met	57.5	63.0	57.5	10.2
Security concerns	48.0	50.3	51.6	25.2
I don't trust the technology	21.8	21.5	25.5	20.7
Data costs too high	18.3	20.0	16.8	*
Too difficult to see my phone's screen	16.6	16.5	21.9	12.0
Difficult/time consuming to set up	9.5	8.8	13.2	12.3
I don't have a bank account	8.8	5.0	*	50.4
Not offered by my bank/credit union	2.7	3.0	*	*
My bank charges a fee for mobile banking	2.2	1.9	*	*
Mobile payments				
Security concerns	41.5	42.7	38.1	36.2
I don't see any benefit	36.7	39.9	30.2	14.8
Easier to pay another way (for example, cash or credit card)	36.0	37.0	36.3	25.2
I don't have the necessary feature on my phone	30.8	32.4	20.9	29.4
I don't trust the technology	19.8	19.3	15.5	30.6
Data costs too high	15.3	16.0	15.4	8.5
Difficult/time consuming to set up	9.1	7.4	18.3	11.5
I don't know any stores that allow mobile payments	9.0	9.5	8.6	*
Not offered by my bank/credit union	4.3	4.2	*	*
My bank charges a fee for mobile payments	1.9	2.0	*	*

* Ten or fewer observations.

Respondents who use low-balance alerts were asked what actions they took as a result of receiving an alert. Responses varied by level of connection to the banking system. Fully banked respondents report that they transferred money into their accounts or they reduced spending. Underbanked respondents say they transferred money into the accounts or deposited money into the accounts. Unbanked respondents report that they reduced spending in response to these low-balance alerts.

Among respondents who receive payment-due alerts, three-fourths report that these alerts helped them pay their bills on time. Paying bills on time has the double benefit of maintaining or improving consumers' credit records and saving on late-payment fees. Virtually all of the underbanked who use payment-due alerts report improvements in paying on time.

Mobile Payments

In the survey, mobile payments were defined as "purchases, bill payments, charitable donations, payments to another person, or any other payments made using a mobile phone. You can do this either by accessing a web page through the web browser on your mobile device, by sending a text message (SMS), or by using a downloadable application on your mobile device. The amount of the payment may be applied to your phone bill (for example, Red Cross text message donation), charged to your credit card, or withdrawn directly from your bank account." Twelve percent of respondents use their mobile phones to make some type of payment; a higher proportion, 17 percent, of underbanked households report using mobile payments (table 5).

Among those who use mobile payments, the most common uses are paying a bill online (47 percent), making an online purchase (36 percent), and transferring money (21 percent). Person-to-person transfers are used by only a small proportion of respondents (8 percent of those who used mobile payments). Higher proportions of underbanked households report using mobile payments services.

Table 5. Payments using mobile phones
Percent

	Full sample	Fully banked	Underbanked	Unbanked
Use mobile payments	12.3	11.6	17.4	12.2
Paid bill online with mobile	47.1	44.9	61.7	*
Made online purchase	36.0	37.3	32.3	*
Transferred money	20.5	19.7	*	*
Received money from someone else	7.9	7.4	*	*
Made charitable donation by texting	5.1	*	*	*
Sent remittance to family in another country	*	*	*	*
Payment channel for mobile payments				
Billed to credit card, debited from prepaid card	66.4	60.4	81.4	93.8
Debited from bank account	45.4	46.7	53.4	*
PayPal, Google Wallet, iTunes, etc.	21.9	20.2	*	*
Charged to phone bill	8.4	9.5	*	*
Other	*	*	*	*
Satisfaction with mobile payments				
Very satisfied	59.4	63.6	45.5	*
Somewhat satisfied	35.4	32.5	45.2	*
Somewhat dissatisfied	*	*	*	*
Very dissatisfied	*	*	*	*

* Ten or fewer observations.

The majority of mobile payment users—60 percent of the fully banked, 81 percent of the underbanked, and 94 percent of the unbanked—report that the payment was charged to a credit card or a prepaid card. About half of the fully banked and underbanked also use mobile payments via a debit to a bank account. Approximately one out of five of all consumers make mobile payments through a third-party provider, such as PayPal, Google Wallet, or iTunes.

Consumers' satisfaction with their mobile payment experiences is more variable than their satisfaction with mobile banking. More than half of all respondents report that they are very satisfied with their experiences, and an additional third report that they are satisfied with their experience. However, satisfaction varies across the groups, with the fully banked having the highest proportions of very or somewhat satisfied respondents (see box 4).

Mobile Phones and Personal Financial Management

Mobile phones can provide consumers with just-in-time information on account balances and credit limits, which in turn can aid in consumer financial management and decisionmaking. Armed with this information, consumers can avoid overdrawing their accounts or going over their credit limits, both of which may trigger fees. Smartphones in particular can also be used to shop for products and services, enabling consumers to save money by finding lower prices or products that fit better with their needs.

About half the survey respondents report that they are responsible for "all or most" of their household's decisionmaking when it comes to budget management, paying bills, shopping, and saving and investing. Slightly higher proportions of underbanked respondents claim this level of responsibility, compared with substantially lower proportions of unbanked households (table 6).

Those who said they used mobile banking were asked if they used their mobile phones to check account balances or available credit before making a purchase. Two-thirds of these

Table 6. Mobile phones, shopping, and financial decisionmaking
Percent

	Full sample	Fully banked	Underbanked	Unbanked
All or most of the responsibility for the household's				
Budget management	49.3	50.8	58.3	39.9
Bill paying	52.9	54.8	60.4	31.9
Shopping	48.1	49.3	55.2	33.2
Saving and investing	41.7	42.1	49.2	32.3
Use mobile to check account balance or available credit before purchase	67.2	64.6	76.9	66.9
Decided not to buy something	59.2	58.3	58.3	*
Compare prices online before going to stores	58.4	62.2	59.0	28.9
Look at product reviews online before going to stores	57.6	62.0	57.2	24.7
Use mobile to comparison shop while at retail store	19.4	19.4	23.7	12.9
Use mobile for online shopping	16.4	16.2	22.3	9.4
Use mobile to read product reviews while at retail store	16.0	15.5	24.7	8.8
Changed which item you purchased	76.9	75.6	86.2	*
Use barcode scanning to shop for prices	12.3	11.7	20.2	*
Changed where you purchased	65.6	65.7	71.2	*

* Ten or fewer observations.

respondents report using their mobile phones to obtain this type of information. As a result of learning about their balances, three out of five respondents say they decided not to go ahead with a purchase.

All respondents in the survey were asked if they compared prices and looked at product reviews online before making a major purchase. Nearly three-fifths of the respondents indicate they do this type of online review and comparison; these activities are more prevalent among the fully banked and underbanked than among the unbanked.

Much lower proportions—generally between one out of eight and one out of five—have used their mobile phones to shop either online or in a retail store, with higher proportions of underbanked respondents reporting these activities. Among all respondents, one out of six report reading product reviews in the store; of those, a substantial proportion (about three-fourths) say they have changed their minds about the product they were purchasing as a result of reading a review. A smaller proportion, one in eight, report using barcode scanning applications on their mobile phones to shop for prices; among those, three-fourths changed where they purchased the item. Again, underbanked respondents are more likely to use these shopping activities and more likely to report that the information available through their mobile phones changed what they purchased or where they purchased it.

Mobile Phones as a Channel for Financial Inclusion

The widespread ownership of mobile phones by underbanked and unbanked consumers suggests that providing a full suite of mobile financial services (for deposits, payments, and personal financial management tools) may be a means to facilitate their access to, and inclusion in, the mainstream financial system. The data indicate that the unbanked and underbanked can be characterized as having lower levels of education and income; being younger, minority, female, not married, and unemployed; and not being willing to take risks.[27] The unbanked are less likely to have a mobile phone than their underbanked and fully banked counterparts, and they are also less likely than the underbanked to have a smartphone.

However, it is also the case that consumers with characteristics that typify the unbanked and underbanked—lower income, younger, minority, female, not married, and unemployed—are highly likely to have mobile phones and may be open to using this channel for financial services (table 7). For example, three-fifths of unbanked respondents with incomes less than $25,000 report that they have a mobile phone, and two-thirds of unbanked respondents between ages 18 and 29 report having a mobile phone. Half of unbanked Hispanic respondents and two-thirds of unbanked African American respondents have mobile phones, and 72 percent of unbanked females have a mobile phone. Three-fifths of unmarried unbanked respondents and three-fourths of unbanked unemployed respondents have mobile phones. Thus, access to the technology does not seem to be a barrier.

One of the most commonly cited reasons that consumers give for not having a bank account is that they "don't like dealing with banks." Mobile banking may provide sufficient separation from "dealing with banks" that consumers could feel comfortable using a bank

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[27] Willingness to take risks is measured using the financial risk-aversion question from the Survey of Consumer Finances. The question asks "Which of the following statements comes closest to describing the amount of financial risk that you are willing to take when you save or make investments?" The four possible responses are (1) "Take substantial financial risks expecting to earn substantial returns"; (2) "Take above average financial risks expecting to earn above average returns"; (3) "Take average financial risks expecting to earn average returns"; and (4) "Not willing to take any financial risks."

Table 7. Select consumer groups and their access to mobile phones
Percent

	Full sample	Fully banked	Underbanked	Unbanked
Income less than $25,000	74.6	81.0	76.2	62.2
Age 18–29	91.2	96.1	98.7	67.7
Hispanic	81.3	88.8	87.8	49.3
Black, non-Hispanic	85.1	92.4	89.5	67.1
Female	89.2	91.0	92.4	71.8
Not married	83.5	87.8	87.4	62.7
Unemployed	86.0	92.5	81.0	76.7

account (see box 1). Another common reason for not having an account is that consumers "don't write enough checks to make it worthwhile"; mobile banking and mobile payments allow for transferring funds or paying bills without writing checks.

The third most-cited reason for not having an account is that "fees and service charges are too high." Some financial institutions, however, are examining whether emerging technologies such as mobile banking have the potential to reduce costs. And, the financial interaction that mobile banking would provide may be particularly beneficial to budget-conscious consumers. For example, the use of text alerts has the potential to help consumers manage their finances with reminders about when bills are due or warnings about low balances that may trigger an overdraft. Since many unbanked consumers also make use of general-purpose reloadable cards (see table 2), using a mobile device to track balances on these cards—perhaps in conjunction with text alerts—could prove useful to these consumers.

Other concerns that unbanked consumers raised with the use of mobile banking and mobile payments were issues surrounding security and trust in the technology. Such issues need to be addressed if unbanked and underbanked consumers are to adopt mobile banking and payments. Financial service providers may want to consider developing a simple customer security toolkit showing consumers how to protect their mobile devices and payments data by creating passwords for login and access; using antivirus software to ensure the applications downloaded are safe from viruses and malware; loading software that enables the phone to be remotely wiped, locked, or deactivated if lost or stolen; and encouraging more consumers to set up fraud alerts.

Conclusion

The analysis of the Federal Reserve Board's SCMFS presented here suggests that mobile technologies offer the potential to better integrate the unbanked and underbanked into the mainstream financial system. Substantial majorities of both the unbanked and underbanked have mobile phones, and significant shares have smartphones. Thus, even if consumers aren't located near a bank or credit union branch, mobile banking technology could allow these consumers to perform many financial transactions through their phones. Moreover, with the emergence of these technologies, some financial institutions are exploring whether they can realize sufficient cost savings and better meet the needs of the unbanked. Because the technology and business models are so new and still evolving, it is unclear to what extent mobile services may ultimately complement, augment, or supplant more traditional means of delivering financial services to consumers, including consumers without banking relationships and those who are banked but also use alternative financial services.

Appendix A: Survey Data Collection

In consultation with a mobile financial services advisory group composed of key Federal Reserve System staff, the Consumer Research Section in the Federal Reserve Board's Division of Consumer and Community Affairs designed a survey instrument to examine consumers' usage of and attitudes towards mobile phones and mobile financial services.

The survey was administered by GfK Knowledge Networks, an online consumer research company, on behalf of the Board. The survey was conducted using a sample of adults ages 18 and over from KnowledgePanel®, a proprietary, probability-based web panel of more than 50,000 individuals. The KnowledgePanel is designed to be statistically representative of the entire U.S. population. Until 2009, the panel was selected using list-assisted random digit dialing methods. However, as more U.S. households became mobile-only households, Knowledge Networks switched to address-based sampling (ABS). ABS uses the U.S. Postal Service Delivery Sequence File to randomly recruit participants to the panel. If a randomly sampled household does not have a computer and/or Internet access, but is willing to participate in the panel, Knowledge Networks provides the household with a computer and Internet at no cost.

Knowledge Networks has conducted research to demonstrate the representativeness of its sample vis a vis U.S. Census Bureau benchmarks.[28] Other researchers have shown samples drawn from the Knowledge Networks panel yield similar estimates to those obtained from a larger random digit dialing survey.[29] As with any survey method, the possibility of bias exists. For example, given that this is an online survey about use of mobile phone technology, one could conceive of respondents predisposed to technology adoption having greater representation in our sample. However, the comparability of our estimates to those obtained in other surveys suggests that our sample displays little effects of bias.

The survey instrument was pre-tested on a sample of 50 respondents, and the full data collection effort for the survey began on December 22, 2011, and concluded on January 9, 2012. A total of 3,382 e-mail solicitations to participate in the survey were sent out to the KnowledgePanel, and the survey was kept open until 2,290 individuals had completed the survey, for a survey completion rate of 67.7 percent. Knowledge Networks sent e-mail reminders to non-responders on days three and six of the field period to prompt participation. The survey took a median time of 15 minutes to complete.

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[28] J. Michael Dennis (2010), "KnowledgePanel: Processes and Procedures Contributing to Sample Representativeness and Tests for Self-Selection Bias," research note (Menlo Park, CA: Knowledge Networks, Inc.), http://knowledgenetworks.com/ganp/docs/KnowledgePanelR-Statistical-Methods-Note.pdf. See also Don A. Dillman, Ulf-Dietrich Reips, and Uwe Matzat (2010) "Advice in Surveying the General Public Over the Internet," *International Journal of Internet Science*, vol. 5 (1), pp. 1–4.

[29] A list of research into the representativeness of the KnowledgePanel is available at http://knowledgenetworks-.com/ganp/reviewer-info.html.

Appendix B: Financial Literacy Questions

The Board included in its survey several questions pertaining to interest rates, inflation, return on assets, portfolio diversity, mutual funds, and repayment periods to gauge the financial literacy of respondents. Correct answers are in bold.

1. Imagine that the interest rate on your savings account was 1 percent per year and inflation was 2 percent per year. After 1 year, how much would you be able to buy with the money in this account?
   a. More than today
   b. Exactly the same
   c. **Less than today**
2. Considering a long time period (for example 10 or 20 years), which asset normally gives the highest return?
   a. Savings accounts
   b. U.S. Government bonds
   c. **Stocks**
3. If an investor who only owns two stocks right now decides to instead spread their money among many different assets (i.e., more stocks, add bonds, add real estate), their risk of losing money on their entire portfolio will:
   a. Increase
   b. **Decrease**
   c. Stay the same
4. If you were to invest $1,000 in a stock mutual fund for a year, it would be possible to have less than $1,000 when you withdraw your money.
   a. **True**
   b. False
5. Suppose you owe $1,000 on a loan and the interest rate you are charged is 10 percent per year compounded annually. If you didn't make any payments on this loan, at this interest rate, how many years would it take for the amount you owe to double?
   a. Less than 2 years
   b. Between 2 and 5 years
   c. **5 to 9 years**
   d. 10 years or more

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The Mortgage Market in 2011: Highlights from the Data Reported under the Home Mortgage Disclosure Act

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Since 1976, most mortgage lending institutions with offices in metropolitan areas have been required under the Home Mortgage Disclosure Act of 1975 (HMDA) to disclose detailed information about their home-lending activity each year. The Congress intended that HMDA achieve its legislative objectives primarily through the force of public disclosure.[1] These objectives include helping members of the public determine whether financial institutions are serving the housing needs of their local communities and treating borrowers and loan applicants fairly, providing information that could facilitate the efforts of public entities to distribute funds to local communities for the purpose of attracting private investment, and helping households decide where they may want to deposit their savings. The data have also proven to be valuable for research and are often used in public policy deliberations related to the mortgage market.

The 2011 HMDA data consist of information reported by more than 7,600 home lenders, including all of the nation's largest mortgage originators. Together, the home-purchase, refinance, and home-improvement loans reported represent the majority of home lending nationwide and thus are broadly representative of all such lending in the United States.[2] The HMDA data include the disposition of each application for mortgage credit; the type, purpose, and characteristics of each home mortgage that lenders originate or purchase during the calendar year; the census-tract designations of the properties related to those loans; loan pricing information; personal demographic and other information about loan applicants, including their race or ethnicity and income; and information about loan sales.[3]

On July 21, 2011, rulemaking responsibility for HMDA was transferred from the Federal Reserve Board to the newly established Consumer Financial Protection Bureau.[4] Federal Financial Institutions Examination Council (FFIEC) continues to be responsible for collecting the HMDA data from reporting institutions and facilitating public access to the

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1 A brief history of HMDA is available at Federal Financial Institutions Examination Council, "History of HMDA," webpage, www.ffiec.gov/hmda/history2.htm.

2 It is estimated that the HMDA data cover about 90 to 95 percent of Federal Housing Administration lending and between 75 and 85 percent of other first-lien home loans. See U.S. Department of Housing and Urban Development, Office of Policy Development and Research (2011), "A Look at the FHA's Evolving Market Shares by Race and Ethnicity," *U.S. Housing Market Conditions* (May), pp. 6–12, www.huduser.org/portal/periodicals/ushmc/spring11/USHMC_1q11.pdf.

3 A list of the items reported under HMDA for 2011 is provided in appendix A. The 2011 HMDA data reflect property locations using the census-tract geographic boundaries created for the 2000 decennial census. The 2012 HMDA data will use the census-tract boundaries constructed for the 2010 decennial census. Thus, in this article, census-tract population and housing characteristics reflect the geographies established for the 2000 census data.

4 For information about the Consumer Financial Protection Bureau, see www.consumerfinance.gov.

information.[5] In September of each year, the FFIEC releases summary tables pertaining to lending activity from the previous calendar year for each reporting lender as well as aggregations of home-lending activity for each metropolitan statistical area (MSA) and for the nation as a whole.[6] The FFIEC also makes available to the public a data file containing virtually all of the reported information for each lending institution.[7]

The main purpose of this article is to describe mortgage market activity in 2011 and in previous years based on the HMDA data.[8] Our analysis yields several key findings:

- The number of home loans of all types reported by covered lenders declined between 2010 and 2011 from about 7.9 million loans to slightly less than 7.1 million loans. Refinance loans fell more than home-purchase loans, although refinancings surged toward the end of 2011 as interest rates dropped. The total of 7.1 million loans reported in 2011 is the lowest number of loans reported in the HMDA data since 6.2 million in 1995.
- Government-backed loans originated under programs such as the Federal Housing Administration (FHA) mortgage insurance program and the Department of Veterans Affairs (VA) loan guarantee program accounted for a slightly smaller share of home-purchase loans in 2011 relative to 2010 but continue to make up a historically large part of the owner-occupant home-purchase mortgage market, at nearly 50 percent.
- Despite the surge in the government-backed share of home-purchase loans, which historically have gone to borrowers with relatively low credit scores, analysis of credit record data indicate that credit scores of home-purchase borrowers are considerably higher now than at any point in the past 12 years. The median score of such borrowers has risen about 40 points since the end of 2006, and the 10th-percentile score is up by about 50 points.
- Our analysis of the HMDA data suggests that, at the retail level, the mortgage market has not become much more concentrated over the past five years. The 10 most active organizations accounted for about 37 percent of all first-lien mortgage originations in 2011—only slightly higher than the 35 percent share for the top 10 organizations in 2006.
- Consistent with the overall decline in home-purchase and refinance lending, the HMDA data show that from 2010 to 2011, all income and racial or ethnic groups experienced a drop in home-purchase lending, although the extent of the decline varied some across groups. Only low-income borrowers avoided a fall in refinance lending.

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[5] The FFIEC (www.ffiec.gov) was established by federal law in 1979 as an interagency body to prescribe uniform examination procedures, and to promote uniform supervision, among the federal agencies responsible for the examination and supervision of financial institutions. The member agencies are the Board of Governors of the Federal Reserve System, the Consumer Financial Protection Bureau, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Office of the Comptroller of the Currency, and representatives from state bank supervisory agencies. Under agreements with these agencies and the Department of Housing and Urban Development, the Federal Reserve Board collects and processes the HMDA data.

[6] For the 2011 data, the FFIEC prepared and made available to the public 48,347 MSA-specific HMDA reports on behalf of reporting institutions. The FFIEC also makes available to the public similar reports about private mortgage insurance (PMI) activity. The costs incurred by the FFIEC to process the annual PMI data and make reports available to the public are borne by the PMI industry. All of the HMDA and PMI reports are available on the FFIEC's reports website at www.ffiec.gov/reports.htm.

The designation of MSAs is not static. From time to time, the Office of Management and Budget updates the list and geographic scope of metropolitan and micropolitan statistical areas. See Office of Management and Budget, "Statistical Programs and Standards," webpage, www.whitehouse.gov/omb/inforeg_statpolicy.

[7] The only reported items not included in the data made available to the public are the loan application number, the date of the application, and the date on which action was taken on the application.

[8] Some lenders file amended HMDA reports, which are not reflected in the initial public data release. A "final" HMDA data set reflecting these changes is created two years following the initial data release. The data used to prepare this article are drawn from the initial public release for 2011 and from the "final" HMDA data set for years prior to that. Consequently, numbers in this article for the years 2010 and earlier may differ somewhat from numbers calculated from the initial public release files.

- The HMDA data suggest that lending activity has not yet rebounded in neighborhoods experiencing high levels of distress. In fact, home-purchase lending in census tracts identified by the Neighborhood Stabilization Program (NSP) as being highly distressed declined by a larger percentage since 2010 than such lending in less-distressed tracts. This decline was particularly pronounced for lower- and middle-income borrowers in these neighborhoods.
- The incidence of higher-priced lending across all products in 2011 was about 3.7 percent, up from 3.2 percent in 2010. Similar to patterns observed in the past, black and Hispanic-white borrowers were more likely, and Asian borrowers less likely, to obtain higher-priced loans than were non-Hispanic white borrowers. These differences are significantly reduced, but not completely eliminated, after controlling for lender and borrower characteristics.
- Overall, loan denial rates in 2011 remained virtually unchanged from 2010, at about 23 percent of all applications. Denial rates vary across loan types and purposes, and across applicants grouped by race or ethnicity, as in past years. The HMDA data do not include sufficient information to determine the extent to which these differences reflect illegal discrimination.
- Comparing home-purchase borrower incomes reported in the HMDA data with income reported by homebuyers in household surveys suggests that incomes on mortgage applications may have been significantly overstated during the peak of the housing boom. In more recent years, there is no evidence of overstated incomes.
- The change from using data from the 2000 decennial census (Census 2000) to using data from the 2010 census and the 2006–10 American Community Survey (ACS) as the basis for deriving median family income will affect how banking institutions fare in Community Reinvestment Act (CRA) performance evaluations. Had the new census-tract relative-income classifications been used in 2011, there would have been a net increase in mortgage lending to low- and moderate-income (LMI) neighborhoods of about 150,000 loans, about 22 percent higher than the number of LMI loans in 2011 under current census-tract relative-income classifications.

A Profile of the 2011 HMDA Data

For 2011, a total of 7,632 institutions reported on their home-lending activity under HMDA: 4,497 banking institutions; 2,017 credit unions; and 1,118 mortgage companies, 812 of which were not affiliated with a banking institution (these companies are referred to in this article as "independent mortgage companies") (table 1). The number of reporting institutions changes some from year to year. Some of the fluctuation is due to changes in reporting requirements, primarily related to increases in the minimum asset level used to determine coverage.[9] Mergers, acquisitions, and failures also account for some of the year-over-year changes. Finally, periodic changes in the number and geographic footprints of metropolitan areas influence reporting over time, as HMDA's coverage is limited to institutions that have at least one office in an MSA. For 2011, the number of reporting institutions fell nearly 4 percent from 2010, continuing a downward trend since 2006, when HMDA coverage included just over 8,900 lenders.[10]

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[9] For the 2012 reporting year (covering lending in 2011), the minimum asset size for purposes of coverage was $40 million. The minimum asset size changes from year to year with changes in the Consumer Price Index for Urban Wage Earners and Clerical Workers. See the FFIEC's guide to HMDA reporting at www.ffiec.gov/hmda/ guide.htm.

[10] There were 138 institutions that ceased operations and did not report lending activity for 2011, but these nonre-

Table 1. Distribution of reporters covered by the Home Mortgage Disclosure Act, by type of institution, 2000–11
Number

Year	Depository institution			Mortgage company			All institutions
	Banking institution	Credit union	All	Independent	Affiliated[1]	All	
2000	4,721	1,691	6,412	981	332	1,313	7,725
2001	4,686	1,714	6,400	962	290	1,252	7,652
2002	4,698	1,799	6,497	986	310	1,296	7,793
2003	4,675	1,903	6,578	1,171	382	1,553	8,131
2004	4,962	2,030	6,992	1,317	544	1,861	8,853
2005	4,878	2,047	6,925	1,341	582	1,923	8,848
2006	4,846	2,037	6,883	1,334	685	2,019	8,902
2007	4,847	2,019	6,866	1,132	638	1,770	8,636
2008	4,855	2,026	6,881	957	550	1,507	8,388
2009	4,810	2,017	6,827	925	399	1,324	8,151
2010	4,677	2,041	6,718	848	371	1,219	7,937
2011	4,497	2,017	6,514	812	306	1,118	7,632

Note: Here and in all subsequent tables, components may not sum to totals because of rounding.

1 Subsidiary of a depository institution or an affiliate of a bank holding company.

Source: Here and in subsequent tables and figures, except as noted, Federal Financial Institutions Examination Council, data reported under the Home Mortgage Disclosure Act (www.ffiec.gov/hmda).

Reporting Institutions by Size and Mortgage Lending Activity

Most institutions covered by HMDA are small, and most extend relatively few loans. For 2011, 57 percent of the depository institutions (banking institutions and credit unions) covered by HMDA had assets under $250 million, and 76 percent of them reported information on fewer than 100 loans (data derived from table 2). Among all depository institutions, nearly 55 percent reported on fewer than 100 loans. Across different types of lenders, mortgage companies tend to originate larger numbers of loans on a per-reporter basis than the other institutions (38 percent of the mortgage companies reported more than 1,000 loans, a share equal to about six times that for depository institutions).

In the aggregate, reporting institutions submitted information on 11.7 million applications for home loans of all types in 2011 (excluding requests for preapproval), down about 10 percent from the total reported for 2010 and far below the 27.5 million applications processed in 2006, just before the housing market decline (data derived from table 3.A). The majority of loan applications are approved by lenders, and most of these approvals result in extensions of credit. In some cases, an application is approved but the applicant decides not to take out the loan; for example, in 2011, about 5 percent of all applications were approved but not accepted by the applicant (data not shown in tables). Overall, about 60 percent of the applications submitted in 2011 resulted in an extension of credit (data derived from tables 3.A and 3.B), a share little changed from 2010. The total number of loans reported in 2011, 7.1 million (as shown in table 3.B), was about 10 percent lower than in 2010 and is the lowest number of mortgage loans reported under HMDA since about 6.2 million loans were reported in 1995 (data prior to 2000 not shown in tables).

porting companies accounted for only 0.89 percent of the 2010 loan application records submitted under HMDA.

Table 2. Number and distribution of home lenders, by type of lender and by number of loans, 2011

Type of lender, and subcategory (asset size in millions of dollars)	Less than 50		50–99		100–249		250–499		500–999		1,000 or more		All	
	Number	Percent of subcategory[1]	Number	Percent of subcategory[1]	Number	Percent of subcategory[1]	Number	Percent of subcategory[1]	Number	Percent of subcategory[1]	Number	Percent of subcategory[1]	Number	Percent of subcategory[1]
Depository institution														
Banking Institution														
Less than 250	1,215	51.6	509	21.6	463	19.7	126	5.4	24	1.0	17	.7	2,354	100
250–499	231	24.9	131	14.1	317	34.2	173	18.6	56	6.0	20	2.2	928	100
500–999	106	17.7	61	10.2	120	20.0	150	25.0	119	19.9	43	7.2	599	100
1,000 or more	66	11.1	25	4.2	67	11.3	68	11.4	129	21.7	239	40.2	594	100
All	1,618	36.2	726	16.2	967	21.6	517	11.6	328	7.3	319	7.1	4,475	100
Credit Union														
Less than 250	783	58.5	301	22.5	207	15.5	36	2.7	11	.8	0	.0	1,338	100
250–499	42	13.9	52	17.2	111	36.6	70	23.1	25	8.3	3	1.0	303	100
500–999	16	7.8	14	6.9	49	24.0	58	28.4	48	23.5	19	9.3	204	100
1,000 or more	0	.0	4	2.4	13	7.9	28	17.1	40	24.4	79	48.2	164	100
All	841	41.9	371	18.5	380	18.9	192	9.6	124	6.2	101	5.0	2,009	100
All depository institutions														
Less than 250	1,998	54.1	810	21.9	670	18.1	162	4.4	35	.9	17	.5	3,692	100
250–499	273	22.2	183	14.9	428	34.8	243	19.7	81	6.6	23	1.9	1,231	100
500–999	122	15.2	75	9.3	169	21.0	208	25.9	167	20.8	62	7.7	803	100
1,000 or more	66	8.7	29	3.8	80	10.6	96	12.7	169	22.3	318	42.0	758	100
All	2,459	37.9	1,097	16.9	1,347	20.8	709	10.9	452	7.0	420	6.5	6,484	100
Mortgage company[2]														
All	185	17.0	68	6.2	133	12.2	135	12.4	149	13.7	419	38.5	1,089	100
All institutions	**2,644**	**34.9**	**1,165**	**15.4**	**1,480**	**19.5**	**844**	**11.1**	**601**	**7.9**	**839**	**11.1**	**7,573**	**100**

1 Distribution sums horizontally. For example, the second column, first row shows that 51.6 percent of banking institutions with assets of less than $250 million originated less than 50 loans in 2011.

2 Independent mortgage company, subsidiary of a depository institution, or affiliate of a bank holding company.

The HMDA data also include information on loans purchased by reporting institutions during the reporting year, although the purchased loans may have been originated at any point in time. For 2011, lenders reported information on 2.9 million loans that they had purchased from other institutions, a decline of nearly 9 percent from 2010. Finally, lenders reported on roughly 186,000 requests for preapproval of home-purchase loans that did not result in a loan origination (table 3.A); preapprovals that resulted in loans are included in the count of loan extensions cited earlier.

Home-Purchase and Refinance Lending

In June 2006, the peak month for home-purchase lending that year, nearly 712,000 home-purchase loans were extended, compared with only 254,000 such loans in June 2011, the most active month that year (figure 1).[11] On an annual basis, the number of home-purchase loans (including both first and junior liens) reported in HMDA in 2011 was down about 5 percent from 2010 and was 64 percent lower than in 2006 (data derived from table 3.B).

One factor that may help explain the drop in home-purchase lending between 2010 and

11 Lenders report the date on which they took action on an application. For originations, the "action date" is the closing date or date of origination for the loan. This date is used to compile data at the monthly level. Generally, the interest rate on a loan is set at an earlier point, known as the "lock date." The interest rate series in the figure is constructed from the results of a survey of interest rates being offered by lenders to prime borrowers. Since a loan's pricing likely reflects the interest rate available at the time of the lock date, the timing of the loan volume and interest rate series may be slightly misaligned in the figure.

Table 3. Home loan activity of lending institutions covered under the Home Mortgage Disclosure Act, 2000–11

A. Applications, requests for preapproval, and purchased loans

Number

Year	Applications received for home loans, by type of property				Requests for preapproval[1]	Purchased loans	Total
	1–4 family			Multifamily			
	Home purchase	Refinance	Home improvement				
2000	8,278,219	6,543,665	1,991,686	37,765	n.a.	2,398,292	19,249,627
2001	7,692,870	14,284,988	1,849,489	48,416	n.a.	3,767,331	27,643,094
2002	7,406,374	17,491,627	1,529,347	53,231	n.a.	4,829,706	31,310,285
2003	8,179,633	24,602,536	1,508,387	58,940	n.a.	7,229,635	41,579,131
2004	9,792,324	16,072,102	2,202,744	61,895	332,054	5,146,617	33,607,736
2005	11,672,852	15,898,346	2,539,158	57,668	396,686	5,874,447	36,439,157
2006	10,928,866	14,045,961	2,480,827	52,220	411,134	6,236,352	34,155,360
2007	7,609,143	11,566,182	2,218,224	54,230	432,883	4,821,430	26,702,092
2008	5,017,998	7,729,143	1,404,008	42,792	275,808	2,921,821	17,391,570
2009	4,216,589	9,982,768	831,504	26,141	216,865	4,301,021	19,574,888
2010	3,847,796	8,433,333	670,147	25,550	170,026	3,229,295	16,376,147
2011	3,630,284	7,390,690	686,788	35,048	185,943	2,944,662	14,873,415

Note: Here and in subsequent tables, except as noted, data include first and junior liens, one- to four-family homes (site-built and manufactured properties), and owner- and non-owner-occupant loans.

[1] Consists of requests for preapproval that were denied by the lender or were accepted by the lender but not acted on by the borrower. In this article, applications are defined as being for a loan on a specific property; they are thus distinct from requests for preapproval, which are not related to a specific property. Information on preapproval requests was not required to be reported before 2004.

n.a. Not available.

2011 is the ending of the first-time homebuyer tax credit program in April 2010.[12] The

Table 3. Home loan activity of lending institutions covered under the Home Mortgage Disclosure Act, 2000–11

B. Loans

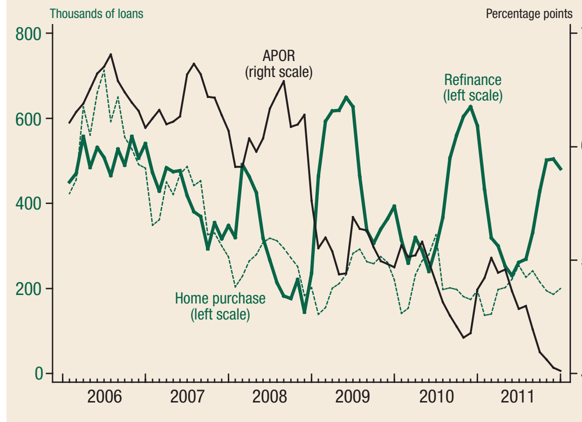
Number

Year	Loans, by type of property				Total
	1–4 family			Multifamily	
	Home purchase	Refinance	Home improvement		
2000	4,787,356	2,435,420	892,587	27,305	8,142,668
2001	4,938,809	7,889,186	828,820	35,557	13,692,372
2002	5,124,767	10,309,971	712,123	41,480	16,188,341
2003	5,596,292	15,124,761	678,507	48,437	21,447,997
2004	6,429,988	7,583,928	966,484	48,150	15,028,550
2005	7,382,012	7,101,649	1,093,191	45,091	15,621,943
2006	6,740,322	6,091,242	1,139,731	39,967	14,011,262
2007	4,663,267	4,817,875	957,912	41,053	10,480,107
2008	3,119,692	3,457,774	568,287	31,509	7,177,262
2009	2,792,939	5,772,078	389,981	18,974	8,973,972
2010	2,546,590	4,968,603	341,401	19,168	7,875,762
2011	2,416,854	4,311,870	339,427	27,111	7,095,262

[12] Those entering into binding contracts to purchase their homes by April 30, 2010, were eligible for the tax credit.

first-time homebuyer tax credit program likely stimulated homebuying in the first half of 2010 as individuals sought to purchase their homes before the sunset date.[13] Data from the National Association of Realtors (NAR) support this view: The NAR annual survey of home buyers and sellers indicates that first-time buyers accounted for about 47 percent of all home purchases in 2009 and half of home sales in 2010 before falling to a 37 percent share in 2011.[14]

Figure 1. Volume of home-purchase and refinance originations and average prime offer rate, by month, 2006–11



Note: The data are monthly. Loans are first- and second-lien mortgages excluding those for multifamily housing. The average prime offer rate (APOR) is published weekly by the Federal Financial Institutions Examination Council. It is an estimate of the annual percentage rate on loans being offered to high-quality prime borrowers based on the contract interest rates and discount points reported by Freddie Mac in its Primary Mortgage Market Survey (www.ffiec.gov/ratespread/newcalc.aspx).

To a greater extent than for home-purchase borrowing, the volume of refinance lending over time generally follows the path of interest rates (typically with a fairly short lag), expanding as mortgage rates fall and retrenching when rates rise. The interest rate environment over the past few years has generally been quite favorable for well-qualified borrowers who have sought to refinance. In some cases, the same individuals have refinanced on more than one occasion to take advantage of the declining interest rate environment. However, many other individuals with outstanding loans have not been able to refinance, either because they could not meet income-related or credit-history-related underwriting standards or because of collateral-related issues, including situations where the outstanding balance on the loan exceeds the home value.[15]

Compared with 2010, the number of reported refinance loans in 2011 was down about 13 percent (table 3.B). Although the total volume of refinancing in 2011 was down quite a bit from 2010, lenders experienced much higher demand in some months than others. In 2011, the peak month for refinance issuance was November, with nearly 504,000 loans, compared with only 230,000 loans in May (figure 1). The surge in refinance activity toward the end of 2011 reflects the steady drop in mortgage rates over the course of the year, which by November and December saw annual percentage offer rates on 30-year fixed-rate loans dip to about 4 percent.

For more information, see Internal Revenue Service, "First-Time Homebuyer Credit," webpage, www.irs.gov/newsroom/article/0,,id=204671,00.html.

[13] Our analysis in an earlier article suggested that one-half of the home-purchase loans in 2009 qualified under the first-time homebuyer tax credit program. See Robert B. Avery, Neil Bhutta, Kenneth P. Brevoort, Christa Gibbs, and Glenn B. Canner (2010), "The 2009 HMDA Data: The Mortgage Market in a Time of Low Interest Rates and Economic Distress," *Federal Reserve Bulletin*, vol. 96 (December), pp. A39–A77.

[14] See National Association of Realtors (2011), "NAR Home Buyer and Seller Survey Reflects Tight Credit Conditions," news release, November 11, www.realtor.org/news-releases/2011/11/nar-home-buyer-and-seller-survey-reflects-tight-credit-conditions.

[15] See analysis of the factors influencing refinance activity in Robert B. Avery, Neil Bhutta, Kenneth P. Brevoort, and Glenn B. Canner (2011), "The Mortgage Market in 2010: Highlights from the Data Reported under the Home Mortgage Disclosure Act," *Federal Reserve Bulletin,* vol. 97 (December), pp. 1–60.

Non-Owner-Occupant Lending

Individuals buying homes either for investment purposes or as second or vacation homes are an important segment of the housing market in general, and in some areas of the country, they are particularly important. In the current period of high foreclosures and elevated levels of short sales, investor activity helps reduce the overhang of unsold and foreclosed properties. In some cases, investors or second-home buyers are able to purchase their properties for cash; in other cases, they choose to borrow and finance their purchases. Surveys sponsored by the NAR find that in 2011, about half of investors paid cash for their purchases and 42 percent of vacation-home buyers paid cash for their properties.[16]

The HMDA data help document the role of non-owner-occupant lending over time. The data show a sharp increase in non-owner-occupant lending used to purchase one- to four-family homes (site-built and manufactured properties) during the first half of the previous decade (table 4). The volume of non-owner-occupant lending fell sharply beginning in 2007 and has remained at comparably low levels through 2011. Although non-owner-occupant lending in 2011 remained subdued compared with levels reached in the middle of the previous decade, such lending did pick up from 2010, increasing nearly 10 percent.

As shown in table 4, the post-2007 decline in non-owner-occupant lending has been more severe than that in owner-occupant lending. Between 2000 and 2005, the share of non-owner-occupant lending used to purchase one- to four-family homes rose, increasing over this period from about 9 percent to 16 percent (data derived from table 4).[17] The share fell to about 11 percent in both 2009 and 2010 but rebounded to 13 percent in 2011.

Conventional versus Government-Backed Loans

Although the total number of home-purchase loans has fallen substantially since 2005, virtually all of the decline has involved conventional lending; the volume of nonconventional home-purchase loans (sometimes referred to as "government backed" loans)—including loans backed by insurance from the FHA or by guarantees from the VA, the Farm Service Agency (FSA), or the Rural Housing Service (RHS)—has increased markedly since the mid-2000s. From 2006 to 2009, the total number of reported conventional home-purchase loans fell 77 percent, while the number of nonconventional home-purchase loans more than tripled (table 4). Although the number of nonconventional home-purchase loans has fallen since reaching its high mark in 2009, such loans still accounted for about 43 percent of home-purchase lending in 2011. The increase in nonconventional lending in recent years reflects several factors, such as increased loan-size limits allowed under the FHA and VA lending programs and reduced access (including more-stringent underwriting and higher prices) to conventional loans, particularly those that allow the borrower to finance more than 80 percent of the property value.[18]

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[16] See United Press International (2012), "Investor Purchases Soar 65 Percent," UPI.com, March 30, www.upi.com/Business_News/Real-Estate/News/2012/03/30/Investor-Purchases-Soar-65-Percent/9321333117717.

[17] Research using credit record data suggests that in states that experienced the largest run-up in home prices, investors accounted for about one-half of the home-purchase loans. See Andrew Haughwout, Donghoon Lee, Joseph Tracy, and Wilbert van der Klaauw (2011), "Real Estate Investors, the Leverage Cycle, and the Housing Market Crisis," Federal Reserve Bank of New York Staff Reports 514 (New York: Federal Reserve Bank of New York, September), www.newyorkfed.org/research/staff_reports/sr514.pdf.

[18] Nonconventional loans play a small role in certain segments of the home-purchase market. For example, nonconventional loans accounted for less than 1 percent of the loans extended to non-owner occupants for the purchase of a home in 2011. Also, nonconventional loans made up a relatively small share (about 24 percent) of the loans used to purchase manufactured homes (data derived from table 5).

Table 4. Home loan applications and home loans for one- to four-family properties, by occupancy status of home and type of loan, 2000–11
Number

Year	Applications				Loans			
	Owner occupied		Non-owner occupied		Owner occupied		Non-owner occupied	
	Conventional	Non-conventional[1]	Conventional	Non-conventional[1]	Conventional	Non-conventional[1]	Conventional	Non-conventional[1]
A. Home purchase								
2000	6,350,643	1,311,101	604,919	12,524	3,411,887	963,345	404,133	8,378
2001	5,776,767	1,268,885	627,598	19,688	3,480,441	1,003,795	440,498	14,128
2002	5,511,048	1,133,770	747,758	13,923	3,967,834	870,599	547,963	8,474
2003	6,212,915	1,014,865	943,248	8,623	4,162,412	761,716	667,613	4,560
2004	7,651,113	799,131	1,335,241	6,839	4,946,423	574,841	906,014	2,710
2005	9,208,214	610,650	1,850,174	3,814	5,742,377	438,419	1,199,509	1,707
2006	8,695,877	576,043	1,653,154	3,792	5,281,485	416,744	1,040,668	1,425
2007	5,960,571	599,637	1,044,112	4,823	3,582,949	423,506	655,916	896
2008	2,940,059	1,424,483	647,340	6,116	1,727,692	972,605	415,930	3,465
2009	2,017,982	1,966,335	442,409	6,711	1,174,648	1,323,966	290,560	3,765
2010	1,822,790	1,763,826	425,345	5,853	1,090,328	1,169,729	284,700	1,833
2011	1,791,526	1,558,447	461,481	4,768	1,076,446	1,025,827	313,138	1,443
B. Refinance								
2000	6,051,484	110,380	379,299	2,502	2,170,162	64,882	198,695	1,293
2001	12,737,863	705,784	823,748	17,592	6,836,106	524,228	516,616	12,181
2002	15,623,327	742,208	1,111,588	14,504	9,058,654	535,370	706,570	9,377
2003	21,779,329	1,236,467	1,563,430	23,310	13,205,472	895,735	1,007,674	15,871
2004	14,476,350	497,700	1,084,536	13,516	6,649,588	304,591	621,667	8,082
2005	14,494,441	262,438	1,135,929	5,538	6,336,004	158,474	603,914	3,257
2006	12,722,112	208,405	1,112,891	2,553	5,382,950	122,134	585,142	1,016
2007	10,173,282	375,860	1,012,827	4,213	4,123,507	196,897	496,577	894
2008	5,829,633	1,240,472	650,042	8,996	2,593,793	522,243	337,914	3,824
2009	7,290,061	2,058,210	619,286	15,211	4,414,509	1,000,911	349,147	7,511
2010	6,325,488	1,449,925	642,401	15,519	3,948,746	655,574	356,183	8,100
2011	5,550,634	1,136,045	682,769	21,242	3,401,097	512,839	384,911	13,023
C. Home improvement								
2000	1,833,277	91,575	65,286	1,548	843,884	10,896	37,047	760
2001	1,771,472	16,276	60,598	1,143	788,560	6,722	32,990	548
2002	1,459,049	11,582	58,080	636	676,515	4,878	30,533	197
2003	1,430,380	13,876	63,806	325	642,065	5,226	31,113	103
2004	2,081,528	11,887	109,105	224	904,492	5,557	56,341	94
2005	2,401,030	10,053	127,857	218	1,026,340	4,483	62,298	70
2006	2,335,338	12,645	132,694	150	1,067,730	6,115	65,842	44
2007	2,072,688	16,717	128,700	119	887,123	9,409	61,321	59
2008	1,294,162	26,544	83,036	266	516,612	12,347	39,170	158
2009	743,968	28,536	58,754	246	349,993	11,256	28,568	164
2010	583,892	34,449	51,415	391	303,344	11,810	26,190	57
2011	581,023	38,194	60,763	6,808	293,735	14,392	27,768	3,532

[1] Loans insured by the Federal Housing Administration or backed by guarantees from the U.S. Department of Veterans Affairs, the Farm Service Agency, or the Rural Housing Service.

Nonconventional lending has also garnered a larger share of the refinance market. In 2006, only 2 percent of refinance loans were nonconventional, compared with 12 percent in 2011.

Table 5. Loans on manufactured homes, by occupancy status of home and type of loan, 2004–11
Number

Year	Owner occupied		Non-owner occupied	
	Conventional	Nonconventional[1]	Conventional	Nonconventional[1]
A. Home purchase				
2004	107,686	23,974	16,243	125
2005	101,539	27,229	17,927	56
2006	102,458	30,530	19,105	257
2007	95,584	28,554	13,963	92
2008	68,821	27,615	11,392	93
2009	43,543	20,630	7,920	29
2010	44,856	17,086	7,655	29
2011	40,312	14,663	7,482	218
B. Refinance				
2004	79,838	6,922	6,507	57
2005	73,520	7,727	6,331	26
2006	64,969	11,750	6,240	68
2007	59,591	16,174	6,332	74
2008	44,342	21,926	6,817	177
2009	37,001	21,768	6,002	73
2010	26,340	9,751	5,024	69
2011	25,299	8,919	4,765	161
C. Home improvement				
2004	17,119	128	1,269	5
2005	20,239	219	1,372	3
2006	20,886	490	1,425	2
2007	19,428	889	1,494	2
2008	12,621	681	1,324	36
2009	9,781	439	1,116	1
2010	8,012	427	999	2
2011	8,244	349	972	75

[1] See table 4, note 1.

This share dropped some from 2010, as the number of nonconventional refinance loans fell about 21 percent (table 4).[19]

The Private Mortgage Insurance Market

In the conventional loan market, lenders typically require that a borrower seeking to purchase an owner-occupied property make a down payment of at least 20 percent of a home's value unless the borrower obtains some type of third-party backing, such as mortgage insurance. For a borrower seeking a conventional loan with a low down payment, a lender can require that the borrower purchase mortgage insurance from a private mortgage insurance company to protect the lender against default-related losses up to a contractually established percentage of the principal amount. As a form of protection for lenders against losses from defaulting borrowers, PMI competes with FHA insurance and VA loan guarantees.

[19] For more-detailed analysis on the rise of government-backed lending in recent years, see Avery and others, "The 2009 HMDA Data."

Table 6. Private mortgage insurance applications and issuance for one- to four-family properties, by occupancy status of home and type of property, 2000–11
Number

Year	Applications				Issuance			
	Owner occupied		Non-owner occupied		Owner occupied		Non-owner occupied	
	Site-built	Manufactured housing[1]	Site-built	Manufactured housing[1]	Site-built	Manufactured housing[1]	Site-built	Manufactured housing[1]
A. Home purchase								
2000	1,204,520	n.a.	95,549	n.a.	955,988	n.a.	75,473	n.a.
2001	1,266,440	n.a.	122,639	n.a.	1,002,385	n.a.	90,929	n.a.
2002	1,324,958	n.a.	153,277	n.a.	1,022,754	n.a.	115,573	n.a.
2003	1,315,221	n.a.	175,958	n.a.	1,021,476	n.a.	134,677	n.a.
2004	1,078,275	10,111	192,086	1,287	807,480	7,508	143,917	984
2005	886,749	10,470	174,174	1,480	676,758	7,512	130,945	1,171
2006	838,304	9,526	134,545	1,273	659,755	6,655	98,744	993
2007	1,260,666	7,928	148,057	1,113	1,015,240	5,531	109,772	774
2008	928,978	4,082	127,773	759	591,108	2,012	66,842	367
2009	341,311	535	14,372	92	206,878	125	5,208	29
2010	214,054	172	7,644	11	154,716	55	4,750	0
2011	245,677	219	11,547	8	193,215	89	8,272	0
B. Refinance[2]								
2000	259,245	n.a.	14,771	n.a.	185,721	n.a.	10,859	n.a.
2001	856,112	n.a.	29,870	n.a.	663,465	n.a.	17,453	n.a.
2002	1,056,788	n.a.	40,771	n.a.	775,020	n.a.	23,035	n.a.
2003	1,372,551	n.a.	46,139	n.a.	1,014,558	n.a.	27,116	n.a.
2004	597,353	6,037	31,352	233	389,563	3,956	17,243	138
2005	438,019	3,702	23,217	136	309,821	2,384	13,239	88
2006	346,978	2,554	24,201	121	234,587	1,567	14,187	78
2007	507,137	2,108	36,508	104	362,961	1,313	22,533	58
2008	454,405	1,442	33,822	123	257,189	695	11,519	34
2009	275,541	429	3,611	15	153,633	126	1,121	4
2010	145,953	135	1,437	2	99,598	56	587	0
2011	149,480	196	1,664	0	109,866	72	838	0

[1] Before 2004, property type was not collected; totals for site-built and manufactured housing are shown in the "Site-built" column.
[2] Includes home-improvement loans. Private mortgage insurance companies do not distinguish between refinance loans and home-improvement loans in reporting. Loan totals are the summation of refinance and home-improvement loans.
n.a. Not available.

The seven companies that reported data for 2011 dominate the PMI industry.[20] Thus, the reported data cover the vast majority of PMI written in the United States. For 2011, the seven PMI companies reported on nearly 409,000 applications for insurance leading to the issuance of 312,000 insurance policies, up from about 370,000 applications and 260,000 policies in 2010 (data derived from table 6). Reported volumes of PMI issuance in 2011, as in recent years, have been substantially smaller than levels prior to 2009. The large reduction in PMI issuance reflects several factors, including tighter underwriting adopted by the

[20] In 1993, the Mortgage Insurance Companies of America, a trade association, asked the FFIEC to process data from the largest PMI companies on applications for mortgage insurance. These data largely mirror the types of information submitted by lenders covered by HMDA. However, because the PMI companies do not receive all of the information about a prospective loan from the lenders seeking insurance coverage, some items reported under HMDA are not included in the PMI data. In particular, loan pricing information and requests for preapproval are unavailable in the PMI data. In the PMI data, the reported disposition of an application for insurance reflects the actions of the PMI companies or, in the case of a withdrawal of an application, the action of the lender.

PMI companies in response to elevated claims and losses experienced during the recent recession and the ongoing recovery.[21]

Overall, 64 percent of the PMI policies issued in 2011 covered home-purchase loans, and the remainder covered refinance mortgages (home-improvement loans are classified as refinance loans by the PMI reporters). Virtually all of the applications for PMI policies issued involved loans to purchase site-built properties, and almost all of the applications for PMI related to owner-occupied units.

The data reported by the PMI industry over the years have consistently shown that most applications for insurance are approved, as lenders are very familiar with the underwriting policies of the insurers and generally are not going to submit an application that is unlikely to be approved. Overall, about 5 percent of PMI insurance applications were denied in 2011, down from about 10 percent in 2010 and 12 percent in 2009 but still notably higher than in 2006 and 2007, when only about 2 percent of the requests for insurance were turned down (data not shown in tables).[22] As with the HMDA data, PMI companies report the reason for denial. The most commonly reported reason cited by lenders related to an issue with the collateral, most likely property value.

Junior-Lien Lending

Junior-lien loans can be taken out either in conjunction with the primary mortgage (a piggyback loan) or independently of the first-lien loan. As noted, piggyback loans can be used by borrowers to avoid having to pay for private or government mortgage insurance. Similarly, piggyback loans can also be used to reduce the size of the first-lien loan to be within the size limits required by Freddie Mac or Fannie Mae without requiring a larger down payment by the borrower. Junior-lien loans that are taken out independently of a first lien can be used for any number of purposes, including to finance home-improvement projects or, in the case of open-ended home equity lines of credit, to provide a readily available source of credit that can be drawn on at the time the borrower needs the funds. Under the regulations that govern HMDA reporting, most of these standalone junior-lien loans are not reported.[23]

In 2006, close to 1.3 million junior liens used for the purchase of owner-occupied properties were reported under HMDA (table 7). This number fell by more than one-half in 2007, dropped sharply again in each of the ensuing years, and decreased to less than 42,000 such loans in 2010 and 2011. More than 1 million junior-lien loans were taken out to refinance loans backed by owner-occupied properties in 2006, and this number also fell substantially starting in 2007 and continued to fall, reaching a low point of less than 74,000 in 2011.

The HMDA data also include information on junior-lien loans used for home-improvement purposes. In 2011, nearly 66,000 junior-lien loans were used for such a purpose, down some from about 80,000 reported in 2010. Both the 2010 and 2011 totals are sharply below the historic high mark of nearly 570,000 reached in 2006. Overall, junior-lien loans used for home improvement accounted for 35 percent of junior-lien loans reported under HMDA.

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[21] For a more detailed analysis of the decline in PMI issuance, see Avery and others, "The 2009 HMDA Data."

[22] For the other applications that did not result in a policy being written, either the application was withdrawn, the application file closed because it was not completed, or the request was approved but no policy was issued.

[23] Unless a junior lien is used for home purchase or explicitly for home improvements, or to refinance an existing lien, it is not reported under HMDA. Further, home equity lines of credit, many of which are junior liens, do not have to be reported in the HMDA data regardless of the purpose of the loan.

Table 7. Home loans for one- to four-family properties, by occupancy status of home, type of loan, and lien status, 2004–11
Number

Year	Owner occupied						Non-owner occupied					
	Conventional			Nonconventional[1]			Conventional			Nonconventional[1]		
	First lien	Junior lien	Unsecured[2]	First lien	Junior lien	Unsecured[2]	First lien	Junior lien	Unsecured[2]	First lien	Junior lien	Unsecured[2]
A. Home purchase												
2004	4,209,787	736,636	...	573,606	1,235	...	853,490	52,524	...	2,703	7	...
2005	4,520,378	1,221,999	...	437,552	867	...	1,049,555	149,954	...	1,685	22	...
2006	4,013,196	1,268,289	...	416,143	601	...	878,325	162,343	...	1,407	18	...
2007	3,031,606	551,343	...	422,450	1,056	...	605,714	50,202	...	888	8	...
2008	1,636,194	91,498	...	971,528	1,077	...	410,377	5,553	...	3,461	4	...
2009	1,132,424	42,224	...	1,322,489	1,477	...	288,526	2,034	...	3,756	9	...
2010	1,049,990	40,338	...	1,168,343	1,386	...	283,017	1,683	...	1,821	12	...
2011	1,036,112	40,334	...	1,024,696	1,131	...	311,831	1,307	...	1,438	5	...
B. Refinance												
2004	6,185,418	464,170	...	304,298	293	...	608,956	12,711	...	8,069	13	...
2005	5,607,642	728,362	...	158,198	276	...	578,491	25,423	...	3,236	21	...
2006	4,347,348	1,035,602	...	121,761	373	...	546,430	38,712	...	989	27	...
2007	3,462,944	660,563	...	196,544	353	...	473,336	23,241	...	879	15	...
2008	2,374,781	219,012	...	521,863	380	...	328,844	9,070	...	3,814	10	...
2009	4,300,322	114,187	...	1,000,422	489	...	342,410	6,737	...	7,495	16	...
2010	3,860,760	87,986	...	655,334	240	...	350,458	5,725	...	8,092	8	...
2011	3,327,415	73,682	...	512,629	210	...	379,519	5,392	...	13,004	19	...
C. Home improvement												
2004	357,618	395,582	151,292	2,697	2,243	617	40,028	8,153	8,160	30	54	10
2005	409,947	468,375	148,018	2,197	1,873	413	42,544	10,756	8,998	17	49	4
2006	360,321	553,152	154,257	3,957	1,735	423	43,913	13,739	8,190	18	20	6
2007	301,078	435,187	150,858	7,510	1,579	320	41,670	11,508	8,143	35	18	6
2008	179,506	181,402	155,704	10,477	1,610	260	26,482	5,473	7,215	135	13	10
2009	166,865	84,414	98,714	8,197	2,541	518	19,961	3,193	5,414	99	28	37
2010	134,370	74,941	94,033	8,218	2,663	929	17,777	2,486	5,927	35	17	5
2011	129,851	60,423	103,461	7,116	2,949	4,327	18,491	2,257	7,020	64	45	3,423

1 See table 4, note 1.
2 Unsecured loans are collected only for home-improvement loans under the Home Mortgage Disclosure Act.
... Not applicable.

Loan Sales

For each loan origination reported under HMDA in a given year, lenders report whether that loan was sold during the same year, and the type of institution to which the loan was sold.[24] Broadly, these purchaser types can be broken into those that are government related—Ginnie Mae, Fannie Mae, Freddie Mac, and Farmer Mac—and those that are not. Ginnie Mae and Farmer Mac focus on loans backed directly by government guarantees or insurance, while Fannie Mae and Freddie Mac purchase conventional loans that

24 Although one of the few sources of information on loan sales, the HMDA data tend to understate the importance of the secondary market. HMDA reporters are instructed to record loans sold in a calendar year different from the year originated as being held in portfolio, leading the reported loan sales to understate the proportion of each year's originations that are eventually sold.

meet certain loan-size and underwriting standards.

Overall, about 78 percent of the first-lien home-purchase and refinance loans for one- to four-family properties originated in 2011 were reported as sold during the year (data not shown in tables). The share of originations that are sold varies some from year to year and by type and purpose of loan (table 8).[25] For example, 69 percent of the conventional loans extended in 2011 for the purchase of owner-occupied one- to four-family dwellings were sold that year. In contrast, nearly 94 percent of the nonconventional loans used to purchase owner-occupied homes were reported as sold in 2011. The share of conventional loans made to non-owner occupants that are reported as sold is notably smaller than that of such loans made to owner occupants. Also, the vast majority of conventional loans extended for the purchase of manufactured homes are held in portfolio; only about 10 percent of such loans were sold in 2011.

Borrower Incomes and Loan Amounts

Under HMDA, lenders report the loan amount applied for and the applicant income that the lender relied on in making the credit decision, if income was considered in the underwriting decision. Lenders do not necessarily collect and report loan applicants' entire income, because in some cases borrowers have more income than is needed to qualify for the loan.

Borrower Income

The vast majority of loan applications and loans reported under HMDA include income information. For example, in 2011, income information was not reported for less than 1 percent of the borrowers purchasing a home with a nonconventional loan and for 3 percent of those using a conventional loan (data not shown in tables). Income information is reported less often for refinance loans, particularly those that are nonconventional (about one-third of the FHA loans and 63 percent of the VA loans), most likely because of streamlined refinance programs that do not require current income to be considered in underwriting.

While the available information on amounts borrowed and applicant income can be evaluated in many ways, we focus here on patterns by loan product and purpose. For home-purchase or refinance lending, borrowers using FHA and VA loans have lower mean or median incomes than borrowers using other loans, despite the fact that the FHA (and VA) loan limits were increased substantially in 2008, potentially allowing the program to be used much more widely than by the LMI households that have been the traditional focus of the program (table 9). Although the share of FHA home-purchase borrowers with incomes above $100,000 has roughly doubled since 2007 (the year before the increase in loan limits) to about 15 percent, the median income of borrowers getting FHA home-purchase loans was still about 30 percent lower than that of those getting conventional loans (data derived from table 9). The relatively low down-payment requirements on FHA-insured loans—the average loan-to-value ratio for FHA home-purchase loans was over 95 percent in 2011—may be continuing to attract lower-income borrowers.[26]

[25] Some loans recorded as sold in the HMDA data are sold to affiliated institutions and thus are not true secondary-market sales. In 2011, 8.6 percent of the loans recorded as sold in the HMDA data were sales to affiliates.

[26] See U.S. Department of Housing and Urban Development (2012), *Quarterly Report to Congress on FHA Single-Family Mutual Mortgage Insurance Fund Programs, FY 2011 Q4* (Washington: HUD, January 31), http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/rmra/oe/rpts/rtc/fhartcqtrly.

Table 8. Distribution of home loan sales for one- to four-family properties, by occupancy status of home and type of loan, 2000–11
Percent

Year	Owner occupied				Non-owner occupied			
	Conventional		Nonconventional[1]		Conventional		Nonconventional[1]	
	Share sold	Memo: Share sold to GSEs[2]	Share sold	Memo: Share sold to GSEs[2]	Share sold	Memo: Share sold to GSEs[2]	Share sold	Memo: Share sold to GSEs[2]
A. Home purchase								
2000	64.8	31.3	89.1	46.0	53.7	29.3	81.4	22.9
2001	66.8	34.6	86.1	46.2	57.9	34.0	92.2	23.0
2002	71.0	36.7	88.7	43.7	62.5	36.4	87.9	29.7
2003	72.3	33.1	91.2	40.7	63.1	31.8	80.8	21.6
2004	74.2	25.5	92.2	40.5	63.5	23.6	63.7	11.5
2005	75.9	18.7	89.9	32.6	69.7	18.0	49.7	16.3
2006	74.8	19.0	88.6	31.7	69.3	19.0	61.3	15.0
2007	70.1	29.1	87.6	32.5	61.4	26.9	74.9	27.6
2008	71.6	40.1	90.0	36.5	60.3	36.3	95.1	21.6
2009	70.1	40.1	91.4	35.0	56.4	34.7	88.9	35.2
2010	69.7	37.0	92.7	29.7	30.3	34.8	91.7	24.1
2011	68.9	34.2	93.5	33.4	61.9	34.5	80.3	35.2
B. Refinance								
2000	47.4	18.0	84.5	50.0	47.3	21.7	86.3	42.8
2001	61.3	37.2	85.0	51.5	61.2	38.4	92.1	33.2
2002	66.8	40.4	85.7	45.0	65.9	43.2	81.3	45.4
2003	74.2	44.8	93.8	48.0	69.8	40.4	87.4	50.7
2004	69.0	27.6	93.2	44.2	62.2	22.6	88.0	35.9
2005	69.9	19.7	89.3	33.5	64.7	16.6	85.7	40.1
2006	65.7	15.2	86.8	31.8	64.9	15.7	79.0	29.6
2007	61.7	21.9	85.1	34.5	61.1	23.9	86.9	23.9
2008	65.3	38.0	88.8	35.4	56.8	33.0	95.7	20.4
2009	79.4	52.8	89.7	37.9	61.2	40.1	93.5	36.0
2010	76.8	46.1	90.2	37.8	65.4	40.3	90.5	43.8
2011	72.7	46.4	91.3	49.8	66.4	43.5	89.5	57.6
C. Home improvement								
2000	6.3	1.1	15.6	4.7	4.4	.4	52.9	.5
2001	6.4	1.5	22.3	7.6	3.9	.8	73.7	1.1
2002	5.9	1.4	28.4	7.1	4.0	.9	55.3	3.6
2003	10.5	.8	43.8	6.7	6.5	.7	35.0	3.9
2004	23.6	6.0	48.7	23.5	23.1	7.5	20.2	7.4
2005	27.2	7.0	46.2	25.3	30.2	8.8	27.1	8.6
2006	22.0	5.3	60.4	31.8	29.4	8.9	29.5	15.9
2007	19.1	6.4	70.6	30.8	26.4	12.1	39.0	11.9
2008	14.7	8.7	80.0	49.2	20.0	14.5	74.7	6.3
2009	24.9	17.8	63.4	38.9	17.7	13.4	56.1	9.8
2010	21.2	13.2	60.6	34.7	18.3	12.6	47.4	28.1
2011	19.1	11.4	45.3	26.8	19.8	13.4	.3	.1

[1] See table 4, note 1.

[2] Loans sold to government-sponsored enterprises (GSEs) include those with a purchaser type of Fannie Mae, Freddie Mac, Ginnie Mae, or Farmer Mac.

Table 9. Cumulative distribution of home loans, by borrower income and by purpose and type of loan, 2011

Percent

Upper bound of borrower income (thousands of dollars)[1]	Home purchase					Refinance				
	FHA	VA	Conventional[2]	Total	Memo: Higher priced[3]	FHA	VA	Conventional[2]	Total	Memo: Higher priced[3]
24	5.3	1.1	3.2	3.7	9.5	3.5	2.3	2.4	2.4	10.2
49	41.5	23.2	25.4	31.0	48.3	28.2	19.5	16.6	17.4	41.5
74	69.4	56.7	47.0	55.9	72.2	58.1	48.0	36.8	38.4	67.2
99	84.9	77.0	62.6	71.9	83.9	77.8	69.3	54.9	56.6	81.8
124	92.5	88.4	73.9	81.9	89.8	88.6	83.1	68.9	70.4	89.4
149	96.1	94.0	81.3	87.8	92.9	93.9	90.5	78.2	79.4	93.2
199	98.7	98.2	89.6	93.7	95.9	98.0	96.6	88.4	89.2	96.4
249	99.4	99.4	93.7	96.3	97.2	99.2	98.7	93.1	93.6	97.7
299	99.7	99.7	95.8	97.5	98.0	99.6	99.4	95.4	95.8	98.3
More than 299	100	100	100	100	100	100	100	100	100	100
Memo: Borrower income, by selected loan type (thousands of dollars)[1]										
Mean	66.3	79.0	111.1	92.1	73.2	76.9	88.0	121.9	118.3	76.5
Median	56	69	79	68	51	67	76	92	90	56

Note: First-lien mortgages for owner-occupied, one- to four-family, site-built properties; excludes business loans. Business-related loans are those for which the lender reported that the race, ethnicity, and sex of the applicant or co-applicant are "not applicable." For loans with two or more applicants, lenders covered under the Home Mortgage Disclosure Act (HMDA) report data on only two. Income for two applicants is reported jointly.

1 Income amounts are reported under HMDA to the nearest $1,000.

2 Conventional loans plus some loans originated with a Farm Service Agency or Rural Housing Service guarantee.

3 Higher-priced loans are those with annual percentage rates 1.5 percentage points or more above the average prime offer rate for loans of a similar type published weekly by the Federal Financial Institutions Examination Council.

FHA Federal Housing Administration.

VA Department of Veterans Affairs.

Loan Amounts

Unlike the data on borrower incomes, loan amounts are provided for all applications and loans reported in the HMDA data. Loan amounts differ across loan types, with FHA or VA loans, on average, being smaller than conventional loans (which make up most of the "other" category in table 10). However, an upward shift in the distribution of loan amounts for both FHA and VA home-purchase loans has occurred in the past couple of years, continuing into 2011 (data for only 2011 shown in tables). The shift reflects several factors, including the higher loan limits allowed under these programs.

Application Disposition, Loan Pricing, and Status under the Home Ownership and Equity Protection Act

In tables 11 and 12, we categorize every loan application and request for preapproval reported in 2011 into 25 distinct product categories characterized by type of loan and property, purpose of loan, and lien and owner-occupancy status. Each product category contains information on the number of total and preapproval applications, application denials, originated loans, loans with prices above the reporting thresholds established by HMDA reporting rules for identifying higher-priced loans, loans covered by the Home Ownership and Equity Protection Act of 1994 (HOEPA), and the mean and median annual percentage rate (APR) spreads for loans reported as higher priced.

Table 10. Cumulative distribution of home loans, by loan amount and by purpose and type of loan, 2011
Percent

Upper bound of loan amount (thousands of dollars)[1]	Home purchase					Refinance				
	FHA	VA	Conventional[2]	Total	Memo: Higher priced[3]	FHA	VA	Conventional[2]	Total	Memo: Higher priced[3]
24	.1	.0	.5	.3	2.8	.1	.0	.5	.5	4.3
49	2.0	.4	3.2	2.5	13.9	1.6	.7	3.3	3.0	16.8
74	9.6	2.6	9.7	9.0	29.8	7.4	3.9	10.3	9.8	32.8
99	22.1	7.8	18.3	18.7	44.9	17.3	10.5	20.2	19.5	47.5
149	50.9	28.3	38.9	42.2	68.8	44.5	32.9	41.2	41.1	68.4
199	71.7	53.6	55.1	60.9	82.0	66.5	55.8	58.1	58.7	80.3
274	88.5	77.5	71.9	78.4	91.2	85.3	77.6	74.7	75.8	89.4
417	97.4	94.5	88.8	92.4	96.9	96.0	94.6	92.0	92.5	96.9
625	99.6	99.1	96.0	97.6	98.8	99.3	99.0	97.0	97.3	99.0
729	99.9	99.7	97.4	98.5	99.2	99.9	99.6	98.1	98.3	99.3
More than 799	100	100	100	100	100	100	100	100	100	100
Memo: Loan amount (thousands of dollars)										
Mean	170.2	217.2	234.7	210.1	141.6	185.3	212.9	220.3	217.0	141.6
Median[1]	147	191	180	167	109	160	185	173	172	104

Note: First-lien mortgages for owner-occupied, one- to four-family, site-built properties; excludes business loans. Business-related loans are those for which the lender reported that the race, ethnicity, and sex of the applicant or co-applicant are “not applicable.”

[1] Loan amounts are reported under the Home Mortgage Disclosure Act to the nearest $1,000.

[2] See table 9, note 2.

[3] See table 9, note 3.

FHA Federal Housing Administration.

VA Department of Veterans Affairs.

Disposition of Applications

As noted, the 2011 HMDA data include information on 11.7 million loan applications, nearly 86 percent of which were acted on by the lender (data derived from table 11). With respect to the disposition of applications, patterns of denial rates are largely consistent with what had been observed in earlier years.[27] Denial rates on applications for home-purchase loans are notably lower than those observed on applications for refinance or home-improvement loans. Denial rates on applications backed by manufactured housing are much higher than those on applications backed by site-built homes. For example, the denial rate for first-lien conventional home-purchase loan applications for owner-occupied site-built properties was 14.8 percent in 2011, compared with a denial rate of 52.7 percent for such applications for owner-occupied manufactured homes.

Under the provisions of HMDA, reporting institutions may choose to report the reasons they provide consumers whose applications are turned down. Reporting institutions may

[27] The information provided in the tables is identical to that provided in analyses of earlier years of HMDA data. Comparisons of the numbers in the tables with those in tables from earlier years, including statistics on denial rates, can be made by consulting the following articles: Avery and others, “The Mortgage Market in 2010”; Avery and others, “The 2009 HMDA Data”; and Robert B. Avery, Neil Bhutta, Kenneth P. Brevoort, Glenn B. Canner, and Christa N. Gibbs (2010), “The 2008 HMDA Data: The Mortgage Market during a Turbulent Year,” *Federal Reserve Bulletin,* vol. 96 (April), pp. A169–A211. Also see Robert B. Avery, Kenneth P. Brevoort, and Glenn B. Canner (2008), “The 2007 HMDA Data,” *Federal Reserve Bulletin*, vol. 94 (December), pp. A107–A146; Robert B. Avery, Kenneth P. Brevoort, and Glenn B. Canner (2007), “The 2006 HMDA Data,” *Federal Reserve Bulletin*, vol. 93 (December), pp. A73–A109; Robert B. Avery, Kenneth P. Brevoort, and Glenn B. Canner (2006), “Higher-Priced Home Lending and the 2005 HMDA Data,” *Federal Reserve Bulletin*, vol. 92 (September), pp. A123–A166; and Robert B. Avery, Glenn B. Canner, and Robert E. Cook (2005),“New Information Reported under HMDA and Its Application in Fair Lending Enforcement,” *Federal Reserve Bulletin*, vol. 91 (Summer), pp. 344–94.

Table 11. Disposition of applications for home loans, and origination and pricing of loans, by type of home and type of loan, 2011

Type of home and loan	Applications			
	Number submitted	Acted upon by lender		
		Number	Number denied	Percent denied
1–4 Family				
Nonbusiness related[3]				
Owner occupied				
Site built				
Home purchase				
Conventional				
First lien	1,438,327	1,260,646	186,025	14.8
Junior lien	57,851	50,569	7,915	15.7
Government backed				
First lien	1,450,709	1,274,493	203,893	16.0
Junior lien	1,930	1,407	233	16.6
Refinance				
Conventional				
First lien	5,367,738	4,595,645	1,021,597	22.2
Junior lien	122,890	113,873	36,232	31.8
Government backed				
First lien	1,115,624	829,981	264,225	31.8
Junior lien	354	262	57	21.8
Home improvement				
Conventional				
First lien	211,771	187,603	51,680	27.5
Junior lien	131,977	123,254	57,825	46.9
Government backed				
First lien	15,879	11,175	3,407	30.5
Junior lien	8,455	6,705	3,476	51.8
Unsecured (conventional or government backed)	230,011	224,145	113,447	50.6
Manufactured				
Conventional, first lien				
Home purchase	196,525	189,483	99,788	52.7
Refinance	51,727	46,960	18,555	39.5
Other	70,033	62,119	22,064	35.5
Non-owner occupied[4]				
Conventional, first lien				
Home purchase	417,027	368,926	58,290	15.8
Refinance	648,094	548,887	161,447	29.4
Other	98,538	88,891	36,593	41.2

cite up to three reasons for each denied application, although most of those that provide this information cite only one reason. An analysis of the reasons for denial provided to prospective borrowers whose applications for conventional credit for the purchase of owner-occupied homes were turned down finds that collateral-related issues and debt-to-income considerations were the two categories of reasons that have seen the largest increase since 2006 (data not shown in tables). Debt-to-income issues were also cited somewhat more often for applications for FHA or VA home-purchase loans, but collateral was the category that had the largest percentage increase. These relationships are not surprising, given the changes in underwriting practices and the widespread decline in home values since 2006.

Table 11. Disposition of applications for home loans, and origination and pricing of loans, by type of home and type of loan, 2011—*continued*

Type of home and loan	Loans originated											
	Number	Loans with APOR spread above the threshold[1]										
		Number	Percent	Distribution, by percentage points of APOR spread						APOR spread (percentage points)		Number of HOEPA-covered loans[2]
				1.5–1.99	2–2.49	2.5–2.99	3–3.99	4–4.99	5 or more	Mean	Median	
1–4 Family												
Nonbusiness related[3]												
Owner occupied												
Site built												
Home purchase												
Conventional												
First lien	995,061	38,660	3.9	41.6	22.0	13.3	14.6	5.8	2.9	2.5	2.1	…
Junior lien	39,943	5,465	13.7	…	…	…	38.6	48.1	13.3	4.5	4.2	…
Government backed												
First lien	1,009,654	28,592	2.8	71.3	21.5	3.2	1.1	2.1	.9	2.0	1.8	…
Junior lien	1,115	4	.4	…	…	…	25.0	50.0	25.0	5.2	4.8	…
Refinance												
Conventional												
First lien	3,299,037	51,664	1.6	46.8	16.6	11.0	13.6	6.0	6.1	2.6	2.1	735
Junior lien	71,341	9,550	13.4	…	…	…	30.0	38.9	31.2	4.8	4.5	201
Government backed												
First lien	503,259	29,744	5.9	31.7	26.0	20.5	19.6	1.7	.4	2.5	2.3	46
Junior lien	190	6	3.2	…	…	…	…	66.7	33.3	4.9	4.8	0
Home improvement												
Conventional												
First lien	126,491	10,663	8.4	29.0	16.8	13.8	17.8	7.9	14.8	3.2	2.6	366
Junior lien	59,607	6,781	11.4	…	…	…	30.8	33.5	35.7	4.9	4.5	187
Government backed												
First lien	6,846	1,723	25.2	18.8	23.0	26.2	25.5	2.8	3.7	2.8	2.6	10
Junior lien	2,914	2,472	84.8	…	…	…	3.0	5.9	91.1	7.0	7.1	0
Unsecured (conventional or government backed)	102,899	…	…	…	…	…	…	…	…	…	…	…
Manufactured												
Conventional, first lien												
Home purchase	39,960	32,623	81.6	4.5	3.4	5.3	13.8	16.2	56.7	5.7	5.4	…
Refinance	24,477	7,933	32.4	17.1	9.7	10.8	21.9	16.5	24.0	3.9	3.6	577
Other	33,238	5,777	17.4	32.9	15.6	9.9	14.0	10.6	17.0	4.1	2.6	214
Non-owner occupied[4]												
Conventional, first lien												
Home purchase	285,333	13,696	4.8	46.4	16.6	11.2	13.6	5.6	6.6	2.6	2.1	…
Refinance	355,243	13,207	3.7	59.1	14.9	8.6	10.3	4.5	2.7	2.3	1.8	32
Other	48,084	2,760	5.7	24.6	12.7	7.5	19.8	17.5	17.9	3.5	3.4	13

1 Average prime offer rate (APOR) spread is the difference between the annual percentage rate on the loan and the APOR for loans of a similar type published weekly by the Federal Financial Institutions Examination Council. The threshold for first-lien loans is a spread of 1.5 percentage points; for junior-lien loans, it is a spread of 3.5 percentage points.

2 Loans covered by the Home Ownership and Equity Protection Act of 1994 (HOEPA), which does not apply to home-purchase loans.

3 Business-related applications and loans are those for which the lender reported that the race, ethnicity, and sex of the applicant or co-applicant are "not applicable"; all other applications and loans are nonbusiness related.

4 Includes applications and loans for which occupancy status was missing.

… Not applicable.

Table 11. Disposition of applications for home loans, and origination and pricing of loans, by type of home and type of loan, 2011—*continued*

Type of home and loan	Applications: Number submitted	Acted upon by lender: Number	Number denied	Percent denied
Business related[3]				
Conventional, first lien				
Home purchase	30,458	29,464	1,066	3.6
Refinance	31,687	30,609	1,813	5.9
Other	10,157	8,904	983	11.0
Multifamily[5]				
Conventional, first lien				
Home purchase	10,146	9,367	1,106	11.8
Refinance	19,588	18,303	2,410	13.2
Other	5,314	4,904	719	14.7
Total	**11,742,810**	**10,086,575**	**2,354,846**	**23.3**

5 Includes business-related and nonbusiness-related applications and loans for owner-occupied and non-owner-occupied properties.

In addition to the application data provided under HMDA, nearly 430,000 requests for preapproval were reported as acted on by the lender in 2011, down about 3 percent from 2010 (table 12). The majority of requests for preapprovals involved conventional loans. About 30 percent of these requests for preapproval were denied by the lender in 2011, a proportion that is higher than in 2010. Not unexpectedly, the number of requests for preapproval is down substantially from the levels recorded at the height of the housing boom, when market conditions favored home sellers and preapproval letters were a factor that enhanced the position of prospective homebuyers. In 2006, covered institutions reported that they received nearly 1.2 million requests for preapproval on which they took action (data not shown in tables).

Table 11. Disposition of applications for home loans, and origination and pricing of loans, by type of home and type of loan, 2011—*continued*

Type of home and loan	Loans originated: Number	Loans with APOR spread above the threshold[1]: Number	Percent	Distribution, by percentage points of APOR spread: 1.5–1.99	2–2.49	2.5–2.99	3–3.99	4–4.99	5 or more	APOR spread (percentage points): Mean	Median	Number of HOEPA-covered loans[2]
Business related[3]												
Conventional, first lien												
Home purchase	27,589	564	2.0	24.8	24.5	22.9	24.3	2.7	.9	2.6	2.5	...
Refinance	28,177	549	1.9	25.7	21.0	26.6	18.9	6.4	1.5	2.6	2.5	2
Other	7,693	119	1.5	17.7	15.1	13.5	23.5	20.2	10.1	3.3	3.3	...
Multifamily[5]												
Conventional, first lien												
Home purchase	7,848	166	2.1	27.7	28.3	19.3	18.1	3.0	3.6	2.6	2.4	...
Refinance	15,238	229	1.5	27.5	26.2	18.3	15.7	6.6	5.7	2.7	2.4	1
Other	4,025	42	1.0	11.9	28.6	14.3	19.1	7.1	19.1	3.5	2.9	3
Total	**7,095,262**	**262,989**	**3.7**	**35.5**	**15.6**	**9.9**	**15.0**	**9.6**	**14.4**	**3.2**	**2.5**	**2,387**

Table 12. Home-purchase lending that began with a request for preapproval: Disposition and pricing, by type of home, 2011

Type of home	Requests for preapproval			Applications preceded by requests for preapproval[1]			Loan originations whose applications were preceded by requests for preapproval										
					Acted upon by lender			Loans with APOR spread above the threshold[2]									
										Distribution, by percentage points of APOR spread						APOR spread (percentage points)	
	Number acted upon by lender	Number denied	Percent denied	Number submitted	Number	Number denied	Number	Number	Percent	1.5–1.99	2–2.49	2.5–2.99	3–3.99	4–4.99	5 or more	Mean spread	Median spread
1–4 Family																	
Nonbusiness related[3]																	
Owner occupied																	
Site built																	
Conventional																	
First lien	217,757	57,848	27	123,940	19,888	16,177	81,794	1,771	2.2	44.5	19.6	10.1	11.2	9.9	4.7	2.6	2.1
Junior lien	7,396	945	13	5,820	354	147	5,184	1,058	20.4	…	…	…	29.1	61.8	9.1	4.3	4.3
Government backed																	
First lien	160,904	62,602	39	86,517	11,279	10,616	61,790	2,568	4.2	71.0	16.4	5.5	1.8	2.3	3.0	2.1	1.8
Junior lien	146	17	12	126	32	11	83	2	2.4	…	…	…	…	100	…	4.8	4.8
Manufactured																	
Conventional, first lien	3,392	1,008	30	2,282	322	469	1,252	729	58.2	5.2	2.6	5.6	8.4	10.3	67.9	6.9	6.5
Other	2,625	1,092	42	1,474	227	172	1,047	36	3.4	83.3	11.1	5.6	…	…	…	1.8	1.8
Non-owner occupied[4]																	
Conventional, first lien	35,912	7,019	20	22,454	3,355	2,372	15,514	502	3.2	50.6	18.5	9.6	11.4	6.4	3.6	2.4	2.0
Other	725	322	44	361	91	135	115	11	9.6	36.4	36.4	9.1	9.1	…	9.1	2.6	2.1
Business related[3]																	
Conventional, first lien	499	27	5	457	39	35	361	14	3.9	21.4	21.4	21.4	35.7	…	…	2.6	2.7
Other	90	12	13	77	10	22	42	1	2.4	100	…	…	…	…	…	1.5	1.5
Multifamily[5]																	
Conventional, first lien	70	2	3	65	6	10	48	5	10.4	…	40.0	20.0	40.0	…	…	2.9	2.6
Other	3	0	0	3	1	0	2	1	50.0	…	…	…	…	100	…	4.1	4.1
Total	**429,519**	**130,894**	**30**	**243,576**	**35,604**	**30,166**	**167,232**	**6,698**	**4.0**	**43.9**	**13.3**	**6.2**	**10.1**	**14.9**	**11.5**	**3.1**	**2.2**

1 These applications are included in the total reported in table 11.
2 See table 11, note 1.
3 See table 11, note 3.
4 See table 11, note 4.
5 See table 11, note 5.
… Not applicable.

The Incidence of Higher-Priced Lending

Price-reporting rules under HMDA since late 2009 define higher-priced first-lien loans as those with an APR of at least 1.5 percentage points above the average prime offer rate

(APOR) for loans of a similar type (for example, a 30-year fixed-rate mortgage).[28] The spread for junior-lien loans must be at least 3.5 percentage points to be considered higher priced. The APOR, which is published weekly by the FFIEC, is an estimate of the APR on loans being offered to high-quality prime borrowers based on the contract interest rates and discount points reported by Freddie Mac in its Primary Mortgage Market Survey (PMMS).[29]

The data show that the incidence of higher-priced lending across all products in 2011 was about 3.7 percent, up about 50 basis points, or 0.5 percentage point, from 2010 (table 11).[30] The incidence varies across loan types, products, and purposes. First, in almost all cases, nonconventional loans have a lower incidence of higher-priced lending than do comparable conventional loan products, although the differences in incidence are much smaller than in the period when many conventional loans were subprime or near prime. In 2011, among first-lien home-purchase loans for site-built homes, 3.9 percent of conventional loans had APRs above the price-reporting threshold, versus 2.8 percent of nonconventional loans. (Among nonconventional loans, those backed by VA guarantees have a particularly low incidence of being higher priced: In 2011, less than 0.04 percent of the VA-guaranteed first-lien home-purchase loans were higher priced.)

Second, with few exceptions, first-lien loans have a lower incidence of higher-priced lending than do junior-lien loans for the same purposes. For example, in 2011, the incidence of higher-priced lending for conventional first-lien refinance loans was 1.6 percent, whereas for comparable junior-lien loans it was 13.4 percent. This relationship is found despite the fact that the threshold for reporting a junior-lien loan as higher priced is 2 percentage points higher than it is for so reporting a first-lien loan. Third, manufactured-home loans exhibit the greatest incidence of higher-priced lending across all loan categories. For 2011, nearly 82 percent of the conventional first-lien loans used to purchase manufactured homes were higher priced.

The HMDA data also show that the incidence of higher-priced lending is related to borrower incomes and the amounts borrowed, with borrowers with lower incomes and those receiving smaller loans more likely to obtain a higher-priced loan. For example, 56 percent of home-purchase loans were extended to borrowers with incomes under $75,000, while such borrowers account for 72 percent of all higher-priced home-purchase loans (table 9). Across loan amounts, 19 percent of home-purchase loans were under $100,000, whereas 45 percent of higher-priced home-purchase loans were under $100,000 (table 10).

Rate Spreads for Higher-Priced Loans

In 2011, the mean APOR spread reported for higher-priced first-lien conventional loans for the purchase of an owner-occupied site-built home was about 2.5 percentage points, compared with about 2.0 percentage points for higher-priced first-lien nonconventional loans

[28] For more about the rule changes related to higher-priced lending, see Avery and others, "The 2009 HMDA Data."

[29] See Freddie Mac, "Weekly Primary Mortgage Market Survey (PMMS)," webpage, www.freddiemac.com/pmms; and Federal Financial Institutions Examination Council, "New FFIEC Rate Spread Calculator," webpage, www.ffiec.gov/ratespread/newcalc.aspx.

[30] In previous articles exploring the distortions created by the old loan pricing classification methodology (see Avery and others, "The 2009 HMDA Data"), we used an adjustment technique that tried to address those distortions. The adjustment technique was similar to the new reporting rules, though it was also clearly inferior to them and could not have been implemented without access to date information, which is not part of the public use file. Without this adjustment, comparison of higher-priced data for loans covered by the old reporting rules with such data for loans covered by the new ones is not appropriate. Even with the adjustment, it is not possible to adjust the data for loans reported under the old rules to make them fully comparable to data reported under the new rules. For this reason, we restrict our discussion here to the 2010 and 2011 data.

used for the same purpose (table 11). Average spreads for first-lien conventional and government-backed refinance loans were 2.5 percentage points and 2.6 percentage points, respectively.

It is worth noting that the vast majority of nonconventional loans reported as higher priced in 2011 exceeded the HMDA price-reporting thresholds by only a small amount: Specifically, 71 percent of the higher-priced nonconventional first-lien home-purchase loans had reported spreads within 50 basis points of the threshold. By comparison, only about 42 percent of the comparable conventional loans reported as higher priced had prices this close to the margin of reporting. In contrast, the share of higher-priced nonconventional refinancing loans with APORs close to the margin of reporting (32 percent) is a little less than the share of higher-priced conventional refinancing loans with such APORs (about 47 percent).

As expected, consistent with the higher reporting threshold of junior-lien lending, higher-priced junior-lien loan products have higher mean and median APOR spreads than do higher-priced first-lien loans. Higher-priced loans for manufactured homes differ from other loan products in that they generally have the highest mean spreads. In 2011, the typical higher-priced conventional first-lien loan to purchase a manufactured home had a reported spread of about 5.7 percentage points, compared with an average spread of roughly 2.5 percentage points for comparable higher-priced loans for site-built properties.

HOEPA Loans

The HMDA data indicate which loans are covered by the protections afforded by HOEPA. Under HOEPA, certain types of mortgage loans that have interest rates or fees above specified levels require additional disclosures to consumers and are subject to various restrictions on loan terms.[31] For 2011, 574 lenders reported extending 2,387 loans covered by HOEPA (table 11; data regarding lenders not shown in tables). In comparison, 655 lenders reported on about 3,400 loans covered by HOEPA in 2010. In the aggregate, HOEPA-related lending made up less than 0.05 percent of all the originations of home-secured refinancings and home-improvement loans reported for 2011 (data derived from tables).[32]

Lender Concentration in the Mortgage Market

Recent press accounts have highlighted the outsized role of a few larger lending organizations in the mortgage market.[33] Table 13 lists the top 10 mortgage originating organizations (inclusive of their reporting mortgage lending affiliates and subsidiaries) according to the HMDA data. Wells Fargo tops the list, having originated over 900,000 loans in 2011, which translates into a market share of about 13 percent.[34] JPMorgan Chase and Bank of America each had a market share of over 5 percent, followed by U.S. Bank and Quicken Loans with over 2 percent. Wells Fargo, JPMorgan Chase, and Bank of America had considerably larger market shares in 2011 than in 2006, in part because of their acquisitions of Wachovia, Washington Mutual, and Countrywide, respectively. The remainder of the top

[31] Unlike the threshold rules used to report higher-priced loans, the threshold rules used to identify HOEPA loans did not change between 2009 and 2010, and thus the 2011 number of HOEPA loans is comparable to those of earlier years.

[32] HOEPA does not apply to home-purchase loans.

[33] For example, see Dakin Campbell and Hugh Son (2012), "Wells Fargo Dominates Home Lending as BofA Retreats: Mortgages," Bloomberg, May 3, www.bloomberg.com/news/2012-05-03/wells-fargo-dominates-home-lending-as-bofa-retreats-mortgages.html.

[34] We include all first-lien originations recorded in the HMDA data, regardless of purpose, loan type, or property type.

Table 13. Home loan originations and purchases by top 10 originators, 2011 and 2006
Percent except as noted

Organization	Loans originated[1]								Loans purchased[2]			
	Number	Market share	Home purchase	Refi-nance	Conventional only				Number	Conven-tional	Conventional only	
					Home purchase (as a share of all home purchase)	Refinance (as a share of all refinance)	Held in portfolio[3]	Held in portfolio or sold to affiliate[3]			Held in portfolio[3]	Held in portfolio or sold to affiliate[3]
2011												
1. Wells Fargo & Co.	908,962	13.4	31.2	67.1	53.8	87.2	7.4	7.8	845,871	47.4	5.3	5.3
2. JPMorgan Chase & Co.	470,760	6.9	8.1	91.6	57.0	97.2	3.5	42.6	300,092	46.0	4.1	40.2
3. Bank of America Corp.	343,471	5.1	28.7	69.9	57.6	88.6	13.7	13.9	442,416	36.4	23.5	23.5
4. U.S. Bancorp	164,937	2.4	24.6	72.4	65.6	92.3	37.9	37.9	114,128	61.0	1.5	1.5
5. Quicken Loans, Inc.	143,870	2.1	8.4	91.6	42.6	64.2	.2	.2	0	n.a.	n.a.	n.a.
6. Citigroup	113,468	1.7	13.0	84.3	93.6	96.1	46.2	61.9	252,128	91.2	13.3	53.0
7. Fifth Third Bancorp	101,956	1.5	26.8	72.4	54.5	92.2	29.6	40.0	15,014	68.7	5.5	5.5
8. Flagstar Bank, FSB	92,875	1.4	39.2	58.8	49.8	82.0	.7	.7	32,249	43.2	6.4	6.4
9. Ally Financial	83,123	1.2	16.6	80.7	83.1	94.0	2.1	99.4	431,925	81.6	.5	38.3
10. SunTrust Bank	80,375	1.2	36.1	63.9	69.1	92.8	5.9	12.5	31,433	74.1	55.7	55.7
Total	2,503,797	36.9	23.7	74.9	57.4	89.3	11.7	25.5	2,465,256	56.8	8.3	27.4
Memo: All other organizations	4,284,175	63.1	41.7	55.4	56.7	86.3	34.9	36.8	479,406	61.4	21.2	21.6
2006												
1. Countrywide	872,732	8.1	50.4	45.9	92.1	98.6	3.5	13.5	1,409,623	95.6	8.0	29.5
2. Wells Fargo & Co.	697,593	6.5	58.8	37.0	89.7	96.2	24.4	24.8	411,346	72.4	17.0	17.0
3. Bank of America Corp.	356,300	3.3	57.5	34.9	97.7	99.1	41.6	41.8	193,761	99.9	58.6	58.6
4. Wachovia Corp.	341,218	3.2	29.7	64.4	95.6	99.5	48.4	64.0	61,525	99.8	55.0	83.3
5. JPMorgan Chase & Co.	317,755	3.0	44.6	52.1	91.1	98.0	6.0	100.0	204,632	89.0	37.8	99.4
6. National City Corp.	278,426	2.6	60.9	36.5	92.1	94.2	4.2	52.1	6,206	95.8	.0	95.2
7. Washington Mutual Bank, FSB	270,278	2.5	29.8	66.0	98.7	98.9	40.7	42.8	415,199	96.7	12.1	12.7
8. GMAC Bank	248,050	2.3	41.6	58.3	92.1	97.7	2.3	73.6	862,978	96.7	10.0	20.2
9. Citigroup	215,454	2.0	30.2	62.3	97.0	98.5	48.0	60.6	616,319	91.4	54.1	70.8
10. HSBC Holdings, PLC	194,308	1.8	27.7	58.0	95.5	99.4	40.7	48.8	306,585	100.0	64.4	66.8
Total	3,792,114	35.2	46.7	48.5	92.9	98.1	22.6	43.5	4,488,174	93.4	24.8	38.8
Memo: All other organizations	6,979,080	64.8	50.9	45.8	91.8	97.2	26.7	31.5	1,748,178	94.4	38.4	54.9

1 First-lien mortgages for owner-occupied one- to four-family homes.

2 All liens are included because lien status is not always available.

3 "Held in portfolio" refers to loans held beyond the year of origination or purchase; excludes loans originated or purchased during the last quarter of the year.

n.a. Not available.

10 organizations had market shares under 2 percent, and the top 10 collectively issued about 37 percent of all mortgage originations reported in the HMDA data in 2011, roughly the same as in 2006.

Notably, market shares derived from the HMDA data differ markedly from market shares recently reported in the press based on information compiled by Inside Mortgage Finance.

It is important to note that for HMDA reporting purposes, institutions report only mortgage applications in which they make the credit decision. Under HMDA, if an application is approved by a third party (such as a correspondent) rather than the lending institution, then that party reports the loan as its own origination and the lending institution reports the loan as a purchased loan. Alternatively, if a third party forwards an application to the lending institution for approval, then the lending institution reports the application under HMDA (and the third party does not report anything). In contrast, Inside Mortgage Finance considers loans to have been originated by the acquiring institution even if a third party makes the credit decision. Thus, many of the larger lending organizations that work with sizable networks of correspondents report considerable volumes of purchased loans in the HMDA data, while Inside Mortgage Finance considers many of these purchased loans to be originations.

To be sure, both market share numbers are important for understanding the supply side of the mortgage market. The HMDA data, by focusing on the entity that makes the approval decision, highlight that the mortgage market continues to be highly decentralized along certain dimensions, with a large number of relatively small entities operating at the retail level, working with mortgage applicants, evaluating their applications, and making lending decisions. That said, overall credit availability and pricing depend on a multitude of additional factors, such as government-sponsored enterprise and FHA practices, lenders' willingness and ability to take risk, competition between wholesale lenders, and general credit conditions and investor appetite for risk.

Table 13 shows that among the top 10 organizations, many of them reported a large number of purchased loans in 2011, particularly Wells Fargo, Bank of America, and Ally Financial. As discussed earlier, many of these purchases are likely to be from correspondents, though it is not possible from the HMDA data to determine how many. It is also worth noting that organizations often turn around and resell loans that they purchased (see last two columns of table 13).

Finally, the HMDA data indicate that the business strategies among the top 10 organizations appear to vary considerably. For example, around 30 percent of Wells Fargo's and Bank of America's originations were for home-purchase loans, compared with less than 10 percent for JPMorgan Chase and Quicken Loans. Citigroup and Ally Financial concentrated relatively more heavily on refinance loans than on home-purchase loans. These institutions also differ considerably in terms of the fraction of loans held in portfolio beyond the year of origination.[35] For example, U.S. Bancorp and Citigroup each held in portfolio 40 percent or more of the conventional loans they originated, compared with less than 10 percent for Wells Fargo and JPMorgan Chase. The HMDA data also reveal considerable variation across these larger lenders in the types of loans (conventional compared with FHA, VA, or FSA) they tend to extend. For example, about half of the home-purchase loans reported by Wells Fargo were conventional, whereas about 90 percent of those originated by Citigroup were of this type.

The Credit Scores of Home-Purchase Mortgage Borrowers

Additional information about individuals obtaining mortgages to purchase homes can be gained by a review of credit record data collected by credit-reporting agencies. These data can be used to identify individuals taking out mortgages to finance a home purchase and,

[35] For this analysis, we consider only those loans originated in the first three quarters of the year; loans originated in the last quarter of the year are less likely to be reported as sold simply because there is not much time to sell the loan.

among these, individuals who are first-time homebuyers. Because the credit record data used here include the credit scores of individuals, we can use this metric to gauge the credit risk profile of home-purchase borrowers.

The data are from the FRBNY/Equifax Consumer Credit Panel. The panel is a nationally representative longitudinal database of individuals with detailed information, at a quarterly frequency beginning in 1999, on consumer and mortgage debt and loan performance drawn from the credit records collected and maintained by Equifax, one of the three national credit bureaus.[36] The data include three key pieces of information with respect to this analysis: (1) details on each mortgage outstanding for a given consumer, including the year of origination; (2) each consumer's credit score as of the end of each quarter; and (3) each consumer's residential location at the level of the census block (a subunit of a census tract).[37] The data used here are through the end of 2011.

Home-purchase loans are not explicitly identified in credit record data, but the panel nature of the data used here allows us to follow a given individual over time and infer whether that borrower purchased a home during any particular period. Specifically, we classify an individual as a homebuyer if the credit record indicates that he or she took out a new mortgage and moved to a different location (the credit record shows that the individual moved from one census block to another). First-time home-purchase borrowers are identified in a similar manner, but their credit records must show no evidence of a previous mortgage. The credit record data show that for home-purchase borrowers in general, as well as for first-time homebuyers financing their purchase, the median credit score has increased about 40 points since 2006. Furthermore, median scores now exceed by a considerable margin the median scores for home-purchase borrowers at any time in the past 12 years (figure 2).

From the perspective of changes in access to credit, a particular group to focus on is that consisting of individuals with scores in the bottom decile of all home-purchase borrowers. Here the data show that the score that delineates the bottom decile has increased nearly 50 points since the end of 2006. Individuals with scores below this increased threshold are likely to have a very difficult time qualifying for credit and, if they manage to qualify for a loan, are likely to pay higher prices. Consistent with this observation, overall, the share of home-purchase borrowers with scores below 620, a traditional demarcation line for individuals who are typically characterized as having a credit history that would be considered subprime, fell from about 19 percent of borrowers at the end of 2006 to about 7 percent at the end of the third quarter of 2011 (data not shown in tables).

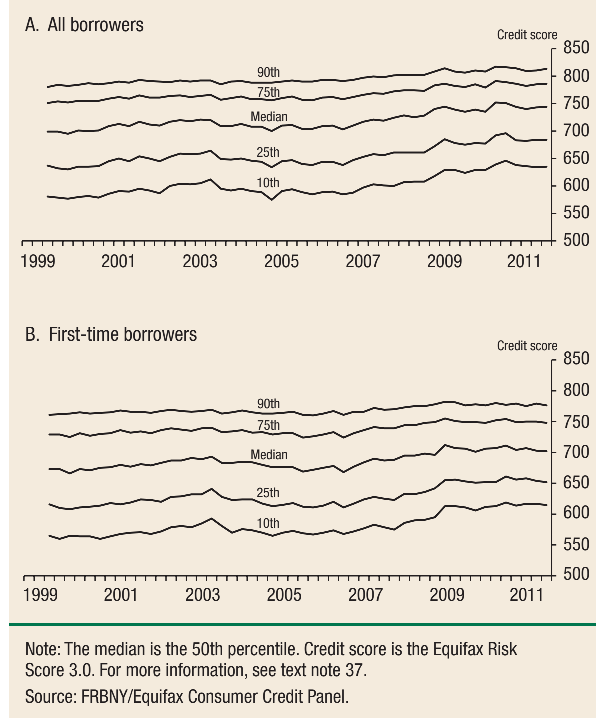
[36] The data are drawn using a methodology to ensure that the same individuals can be tracked over time, and that the data are representative of all individuals with a credit record as of the end of each quarter. For more information on these data, see Donghoon Lee and Wilbert van der Klaauw (2010), "An Introduction to the FRBNY Consumer Credit Panel," Federal Reserve Bank of New York Staff Reports 479 (New York: Federal Reserve Bank of New York, November), www.newyorkfed.org/research/staff_reports/sr479.pdf. It is important to note that all individuals in the database are anonymous: Names, street addresses, and Social Security numbers are not included in the data. Individuals are distinguished and can be linked over time through a unique, anonymous consumer identification number assigned by Equifax.

[37] This credit score is generated from the Equifax Risk Score 3.0 model. The Equifax Risk Score 3.0 is a credit score produced from a general-purpose risk model that predicts the likelihood an individual will become 90 days or more delinquent on any account within 24 months after the score is calculated. The Equifax Risk Score 3.0 ranges from 280 to 850, with a higher score corresponding to lower relative risk (for more information, see www.equifax.com). For the exercise here, we track the credit score of each individual as of the quarter before he or she took out a mortgage. Although the lender may have used a different score to underwrite the loan, it is likely that the scores used here are reflective of such scores.

Lending across Population Groups and Neighborhoods

One of the strengths of the HMDA data is that the annual data can be merged to track changes in lending activity across population groups and areas. In this section, we show changes in lending, from 2010 to 2011, to borrowers sorted by income, race, or ethnicity and by the income or minority population characteristics of the areas where they reside. We also present an analysis of lending in areas characterized by their degree of economic distress.

Figure 2. Credit scores of home-purchase borrowers, by selected credit score percentile, 1999–2011



Note: The median is the 50th percentile. Credit score is the Equifax Risk Score 3.0. For more information, see text note 37.

Source: FRBNY/Equifax Consumer Credit Panel.

Changes in Lending, 2010 to 2011

As noted earlier, both home-purchase and refinance lending fell from 2010 to 2011. Virtually all population segments experienced these declines, although the falloff in activity was more severe for some groups than for others (table 14, memo items).[38] Across racial or ethnic groups, all minority populations except Hispanic whites experienced relatively large declines in activity; Hispanic whites and non-Hispanic whites both experienced relatively smaller declines in activity. Lower-income borrowers, those purchasing homes in lower-income census tracts, and those residing in areas with larger minority populations also experienced relatively large reductions in home-purchase lending.

Patterns for refinancing differed from those for home-purchase lending, as the largest declines were among non-Hispanic whites, middle- and higher-income borrowers, and those residing in areas with smaller shares of minorities and populations with relatively higher incomes. The only group to experience an increase in refinance lending was low-income borrowers; refinance lending to this population segment increased about 3 percent from 2010 to 2011.

Populations differ considerably in their use of various loan products. Most notably, black, Hispanic white, and lower-income borrowers, and those residing in areas with larger shares of minority populations, use nonconventional loans to purchase homes to a greater extent than other groups. Greater reliance on nonconventional loans may reflect the relatively low down-payment requirements of the FHA and VA lending programs. The HMDA data indicate that all groups were a little less dependent on nonconventional loans in 2011 than in 2010. Reduced reliance on nonconventional loans occurred for both home-purchase and refinance lending.

[38] Changes in lending to different groups over the 2006–10 period were presented in an earlier article. See Avery and others, "The Mortgage Market in 2010."

Table 14. Home lending to different populations, by characteristic of borrower and of census tract and by type and purpose of loan, 2010–11

Percent except as noted

Characteristic of borrower and of census tract	2010				2011				Memo: Percentage change in number of loans, 2010–11
	Conventional	Non-conventional[1]	Total	Memo: Number of loans	Conventional	Non-conventional[1]	Total	Memo: Number of loans	
A. Home purchase									
Borrower									
Race other than white only[2]									
American Indian or Alaska Native	33.8	66.2	100	11,183	36.5	63.5	100	9,435	-15.6
Asian	73.4	26.6	100	119,762	74.3	25.7	100	104,626	-12.6
Black or African American	18.9	81.1	100	133,969	21.6	78.4	100	113,591	-15.2
Native Hawaiian or other Pacific Islander	32.4	67.6	100	7,671	35.1	64.9	100	6,661	-13.2
White, by ethnicity[2]									
Hispanic white	26.5	73.5	100	207,108	29.2	70.8	100	195,778	-5.5
Non-Hispanic white	50.3	49.7	100	1,504,464	53.3	46.7	100	1,417,339	-5.8
Income ratio (percent of area median)[3]									
Low	38.3	61.7	100	281,788	39.9	60.1	100	254,828	-9.6
Moderate	34.9	65.1	100	552,928	37.3	62.7	100	495,859	-10.3
Middle	41.4	58.6	100	567,223	43.9	56.1	100	519,898	-8.3
High	63.0	37.0	100	816,394	65.9	34.1	100	790,223	-3.2
Census tract of property									
Racial or ethnic composition (minorities as a percent of population)									
Less than 10	54.3	45.7	100	806,008	56.4	43.6	100	767,580	-4.8
10–49	45.6	54.4	100	1,105,335	48.8	51.2	100	1,025,746	-7.2
50–79	37.5	62.5	100	197,401	41.0	59.0	100	169,409	-14.2
80–100	31.4	68.6	100	109,589	33.7	66.3	100	98,073	-10.5
Income ratio (percent of area median)[4]									
Low	39.7	60.3	100	25,879	45.0	55.0	100	21,128	-18.4
Moderate	35.9	64.1	100	242,761	39.8	60.2	100	206,299	-15.0
Middle	41.6	58.4	100	1,107,033	44.3	55.7	100	1,029,115	-7.0
High	58.1	41.9	100	819,505	60.7	39.3	100	791,254	-3.4
B. Refinance									
Borrower									
Race other than white only[2]									
American Indian or Alaska Native	76.8	23.2	100	11,981	77.6	22.4	100	10,991	-8.3
Asian	95.3	4.7	100	232,177	95.8	4.3	100	204,917	-11.7
Black or African American	58.1	41.9	100	129,828	62.5	37.6	100	119,267	-8.1
Native Hawaiian or other Pacific Islander	75.5	24.5	100	9,925	77.3	22.8	100	8,595	-13.4
White, by ethnicity[2]									
Hispanic white	75.1	24.9	100	190,507	79.0	21.0	100	176,431	-7.4
Non-Hispanic white	86.3	13.7	100	3,359,573	87.7	12.3	100	2,826,443	-15.9
Income ratio (percent of area median)[3]									
Low	54.5	45.5	100	631,539	62.4	37.6	100	648,323	2.7
Moderate	85.6	14.4	100	635,461	87.9	12.1	100	529,877	-16.6
Middle	87.7	12.3	100	1,017,330	89.1	10.9	100	821,444	-19.3
High	93.2	6.8	100	2,231,764	93.7	6.3	100	1,840,400	-17.5

Note: First-lien mortgages for owner-occupied one- to four-family homes.

1 See table 4, note 1.

2 Categories for race and ethnicity reflect the revised standards established in 1997 by the Office of Management and Budget. Applicants are placed under only one category for race and ethnicity, generally according to the race and ethnicity of the person listed first on the application. However, under race, the application is designated as *joint* if one applicant reported the single designation of white and the other reported one or more minority races. If the application is not joint but more than one race is reported, the following designations are made: If at least two minority races are reported, the application is designated as *two or more minority races;* if the first person listed on an application reports two races, and one is white, the application is categorized under the minority race. For loans with two or more applicants, lenders covered under the Home Mortgage Disclosure Act report data on only two.

Table 14. Home lending to different populations, by characteristic of borrower and of census tract and by type and purpose of loan, 2010–11—*continued*

Percent except as noted

Characteristic of borrower and of census tract	2010				2011				Memo: Percentage change in number of loans, 2010–11
	Conventional	Non-conventional[1]	Total	Memo: Number of loans	Conventional	Non-conventional[1]	Total	Memo: Number of loans	
Census tract of property									
Racial or ethnic composition (minorities as a percent of population)									
Less than 10	87.5	12.5	100	2,014,629	88.6	11.4	100	1,662,511	-17.5
10–49	84.7	15.3	100	2,114,604	85.9	14.1	100	1,825,725	-13.7
50–79	81.6	18.4	100	266,896	83.5	16.5	100	241,937	-9.4
80–100	72.9	27.1	100	119,965	77.4	22.6	100	109,871	-8.4
Income ratio (percent of area median)[4]									
Low	74.6	25.4	100	23,202	79.9	20.1	100	20,390	-12.1
Moderate	77.0	23.0	100	301,623	80.3	19.7	100	264,107	-12.4
Middle	82.4	17.6	100	2,094,968	83.8	16.2	100	1,779,036	-15.1
High	90.0	10.0	100	2,066,948	90.7	9.3	100	1,753,976	-15.1
C. Home improvement[5]									
Borrower									
Race other than white only[2]									
American Indian or Alaska Native	96.2	3.8	100	1,749	96.7	3.3	100	1,787	2.2
Asian	98.0	2.0	100	5,771	97.4	2.6	100	5,857	1.5
Black or African American	91.3	8.7	100	17,993	93.0	7.0	100	17,964	-.2
Native Hawaiian or other Pacific Islander	95.9	4.1	100	764	95.9	4.1	100	752	-1.6
White, by ethnicity[2]									
Hispanic white	95.2	4.8	100	19,935	95.8	4.2	100	20,733	4.0
Non-Hispanic white	96.4	3.6	100	238,623	96.6	3.4	100	227,534	-4.6
Income ratio (percent of area median)[3]									
Low	93.9	6.1	100	46,348	93.0	7.0	100	45,672	-1.5
Moderate	96.2	3.8	100	63,060	95.1	4.9	100	61,778	-2.0
Middle	96.2	3.8	100	78,086	95.2	4.8	100	75,804	-2.9
High	97.2	2.8	100	127,660	96.4	3.6	100	124,873	-2.2
Census tract of property									
Racial or ethnic composition (minorities as a percent of population)									
Less than 10	97.2	2.8	100	160,410	96.2	3.8	100	154,798	-3.5
10–49	95.7	4.3	100	117,947	94.8	5.2	100	116,021	-1.6
50–79	95.2	4.8	100	17,870	92.8	7.2	100	17,742	-.7
80–100	92.9	7.1	100	18,927	93.4	6.6	100	19,566	3.4
Income ratio (percent of area median)[4]									
Low	92.2	7.8	100	3,263	87.5	12.5	100	3,393	4.0
Moderate	95.0	5.0	100	36,461	94.3	5.7	100	35,492	-2.7
Middle	96.1	3.9	100	177,310	95.7	4.3	100	170,938	-3.6
High	96.9	3.1	100	92,906	96.2	3.8	100	91,865	-1.1

[3] Borrower income is the total income relied on by the lender in the loan underwriting. Income is expressed relative to the median family income of the metropolitan statistical area (MSA) or statewide non-MSA in which the property being purchased is located. “Low” is less than 50 percent of the median; “moderate” is 50 percent to 79 percent (in this article, “lower income” encompasses the low and moderate categories); “middle” is 80 percent to 119 percent; and “high” is 120 percent or more.

[4] The income category of a census tract is the median family income of the tract relative to that of the MSA or statewide non-MSA in which the tract is located as derived from the 2000 census. “Low” is less than 50 percent of the median; “moderate” is 50 percent to 79 percent; “middle” is 80 percent to 119 percent; and “high” is 120 percent or more.

[5] Consists of first- and junior-lien loans and loans without a lien.

Credit Circumstances in Distressed Neighborhoods

Since the start of the housing downturn, access to mortgage credit has been an acute public policy concern, particularly for households with lower incomes or in neighborhoods that have been hardest hit by foreclosures. Mortgage originations have declined broadly since 2005, and, as we discussed in the review of last year's HMDA data, these declines have been greater in highly distressed neighborhoods. To determine if credit has yet begun to flow more freely in such neighborhoods, we use the HMDA data to compare mortgage credit flows from 2010 to 2011.

As in last year's review, we identify distressed neighborhoods using the scores produced by the Department of Housing and Urban Development (HUD) for the NSP.[39] The NSP was created by the Housing and Economic Recovery Act of 2008 to provide funds for state and local governments seeking to support neighborhoods with high levels of property abandonment and foreclosure. In deciding which neighborhoods to target, HUD uses a statistical model that estimates the likelihood that the neighborhood is experiencing high rates of foreclosure and mortgage delinquency. The outputs of this model are used to assign to each tract an NSP score ranging from 1 to 20, with a higher score indicating a greater likelihood of distress and with the scores scaled so that each score point is given to 5 percent of census tracts. While an evaluation of the success of the NSP itself is well beyond the scope of this article, we can use these scores to classify census tracts according to the degree of distress they face.

The change from 2010 to 2011 in home-purchase lending for owner-occupied properties, broken down by quintiles of the NSP score, is shown in table 15. Lending declined 7.2 percent overall, though the declines were substantially greater in high-distress neighborhoods. In tracts with NSP scores of 17 to 20, home-purchase lending decreased 13.8 percent, compared with 3.3 percent in tracts with NSP scores below 5. The steeper decline in mortgage credit flows to highly distressed areas continues a trend that has been observed since the onset of the housing market downturn.

Differences in the extent of decline are also observed across borrower income levels. Lending fell more substantially for lower- and middle-income borrowers (12.3 percent and 11.3 percent, respectively) than it did for high-income borrowers (3.8 percent). Indeed, for high-income borrowers, the decline in lending appears unrelated to the degree of neighborhood distress, as indicated by the nonmonotonic relationship between lending declines and NSP score quintile. However, for lower- and middle-income borrowers, the decreases were notably larger when neighborhood distress increased. Somewhat surprisingly, lending to middle-income borrowers fell more than it did for lower-income borrowers in the bottom three quintiles of the NSP score (scores of 1 to 12). In tracts with NSP scores above 12, lending to lower-income borrowers fell off by a larger percentage than it did for high-income borrowers.

Attributing these declines to supply- or demand-side factors is not straightforward. As shown in table 15, the number of applications for home-purchase loans fell by slightly more than the number of loan originations, a pattern that holds for almost all NSP quintiles. The sharper decline in applications suggests that reduced mortgage flows may primarily reflect a drop in demand; however, since potential applicants may have foregone applying because they suspected their application would be denied, the sharper fall in applications is insufficient to prove that these declines represent demand-side factors alone. Most likely, these changes reflect a combination of changes in supply and demand.

39 See Avery and others, "The Mortgage Market in 2010."

Table 15. Loan characteristics related to lending in areas grouped by Neighborhood Stabilization Program score, 2011

Percent change in home-purchase lending from 2010 to 2011

Characteristic	NSP score[1]					
	1–4	5–8	9–12	13–16	17–20	All
Memo						
Loans	-3.3	-7.1	-9.3	-9.9	-13.8	-7.2
Applications	-3.9	-7.3	-9.0	-10.1	-15.4	-7.8
Borrower						
Income ratio (percent of area median)[2]						
Lower	-7.4	-9.6	-11.4	-13.6	-19.6	-12.3
Middle	-8.4	-10.4	-12.2	-12.9	-16.5	-11.3
High	-1.6	-5.1	-6.8	-5.1	-5.7	-3.8
Minority[3]	-4.7	-10.1	-11.2	-13.1	-14.8	-10.1
Originating institution						
Bank	-2.9	-7.0	-9.7	-10.3	-17.6	-7.1
Thrift	-20.2	-28.1	-30.2	-26.4	-18.0	-24.1
Credit union	6.6	10.8	9.2	8.9	11.2	8.5
Independent mortgage bank	4.6	-.6	-3.2	-6.4	-11.2	-2.3
Top 10 organization	-14.4	-16.6	-19.3	-18.5	-22.6	-17.1
Non–top 10 organization	2.6	-2.9	-4.9	-6.1	-9.9	-2.6

Note: First and junior liens for owner-occupied one- to four-family properties in metropolitan areas. Data are the percent change in the dollar value of lending.

1 The Neighborhood Stabilization Program (NSP) score is based on the NSP3 score created by the Department of Housing and Urban Development. The NSP score classifies census tracts into 5 percent "buckets" on a range of 1 to 20, with 1 being the best tracts and 20 being the worst in terms of a variety of factors, such as foreclosure rates. NSP scores determine eligibility for NSP funding; census tracts with the highest scores are considered the tracts with the greatest need for support. See text for further details.

2 Borrower income is the total income relied upon by the lender in the loan underwriting. Income is expressed relative to the median family income of the metropolitan statistical area (MSA) or statewide non-MSA in which the property being purchased is located. "Lower" is less than 80 percent of the median; "middle" is 80 percent to 119 percent; and "high" is 120 percent or more.

3 See table 14, note 2. Minority borrowers are borrowers other than non-Hispanic whites.

Source: Department of Housing and Urban Development; Federal Financial Institutions Examination Council, data reported under the Home Mortgage Disclosure Act.

One supply factor that may be influencing how mortgage credit is flowing is the mix of lenders extending credit. In percentage terms, the largest changes involved thrift institutions, whose lending fell by almost one-fourth in 2011, and credit unions, whose lending increased by over 8 percent. While these institution types accounted for only a small share of lending in 2011 (13 percent; data not shown in table), in neither case was there a clear relationship between the change in lending and the degree of neighborhood distress. Instead, the more rapid decline in lending to distressed neighborhoods appears to involve lending by commercial banks and independent mortgage companies. Both institution types experienced larger declines in lending to tracts with higher NSP scores. While lending by commercial banks was down in 2011 for all NSP quintiles, lending by independent mortgage companies increased in tracts in the least amount of distress (the bottom quintile of NSP scores) in 2011 and fell 11 percent in tracts in the most distress. Nevertheless, both institution types had a spread of about 15 percentage points between the changes in lending in the highest and lowest NSP quintiles.

In addition to types of lenders, we can also examine lending activity by largest lenders. Home-purchase lending by the 10 largest lenders in 2011 fell more sharply in 2011 (17 percent) than lending by other financial institutions (2.6 percent). However, lending by both declined more in highly distressed neighborhoods than in neighborhoods experiencing less distress.

The results of this analysis suggest that highly distressed neighborhoods continue to experience reduced mortgage flows, which mirrors the pattern observed for the 2005–10 period discussed in last year's review. These declines were particularly pronounced for lower-income borrowers. And while it is difficult to apportion these declines to demand and supply considerations, the sharper declines in distressed areas appear, for the most part, to have been widespread across lenders.

Differences in Lending Outcomes by Race, Ethnicity, and Sex of the Borrower

One reason the Congress amended HMDA in 1989 was to enhance its value for fair lending enforcement by adding to the items reported the disposition of applications for loans and the race, ethnicity, and sex of applicants. A similar motivation underlay the decision to add pricing data for higher-priced loans in 2004, although such data serve other purposes, including to help identify lenders active in the higher-cost or higher-risk segments of the mortgage market and provide information on the volume and locations of borrowers receiving higher-priced loans.

Over the years, analyses of HMDA data have consistently found substantial differences in the incidence of higher-priced lending and in application denial rates across racial and ethnic lines, differences that cannot be fully explained by factors included in the HMDA data.[40] Analyses also have found that differences across groups in mean APR spreads paid by those with higher-priced loans were generally small.[41] Here we examine the 2011 HMDA data to determine the extent to which these differences persist.

The analysis here presents aggregated lending outcomes across all reporting institutions. Patterns for any given financial institution may differ from those shown, and for any given financial institution, relationships may vary by loan product, geographic market, and loan purpose. Further, although the HMDA data include some detailed information about each mortgage transaction, many key factors that are considered by lenders in credit underwriting and pricing are not included. Accordingly, it is not possible to determine from HMDA data alone whether racial and ethnic pricing disparities reflect illegal discrimination. However, analysis using the HMDA data can account for some factors that are likely related to the lending process. Given that lenders offer a wide variety of loan products for which basic terms and underwriting criteria can differ substantially, the analysis here can only be viewed as suggestive.

Comparisons of average outcomes (both loan pricing and denials) for each racial, ethnic, or gender group are made both before and after accounting for differences in the borrower-related factors contained in the HMDA data (income; loan amount; location of the property, or MSA; and presence of a co-applicant) and for differences in borrower-related factors plus the specific lending institution used by the borrower.[42] Comparisons for lend-

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[40] See Avery, Brevoort, and Canner, "The 2006 HMDA Data"; Avery, Brevoort, and Canner, "Higher-Priced Home Lending and the 2005 HMDA Data"; and Avery, Canner, and Cook, "New Information Reported under HMDA."

[41] See, for example, Andrew Haughwout, Christopher Mayer, and Joseph Tracy (2009), "Subprime Mortgage Pricing: The Impact of Race, Ethnicity, and Gender on the Cost of Borrowing," Federal Reserve Bank of New York Staff Reports 368 (New York: Federal Reserve Bank of New York, April), www.newyorkfed.org/research/staff_reports/sr368.pdf; and Marsha J. Courchane (2007), "The Pricing of Home Mortgage Loans to Minority Borrowers: How Much of the APR Differential Can We Explain?" *Journal of Real Estate Research*, vol. 29 (4), pp. 399–439.

[42] Excluded from the analysis are applicants residing outside the 50 states and the District of Columbia as well as applications deemed to be business related. Applicant gender is controlled for in the racial and ethnic analyses, and race and ethnicity are controlled for in the analyses of gender differences.

ing outcomes across groups are of three types: gross (or "unmodified"), modified to account for borrower-related factors (or "borrower modified"), and modified to account for borrower-related factors plus lender (or "lender modified").[43] The analysis here distinguishes between conventional and nonconventional lending, reflecting the different underwriting standards and fees associated with these two broad loan product categories.[44]

Incidence of Higher-Priced Lending by Race and Ethnicity and Sex

As noted earlier, 2010 was the first HMDA reporting year for which all of the loans subject to higher-priced loan reporting used the new Freddie Mac PMMS threshold (the PMMS threshold was also used for the last three months of 2009). Before October 1, 2009, a Treasury-based threshold was used. The change in threshold makes it problematic to compare the reported incidence of higher-priced lending in 2010 or 2011 with the incidence reported for previous years. Nevertheless, in previous articles, we have employed a methodology that adjusted the Treasury-based spread to a spread over the 30-year fixed-rate mortgage APOR reported in the PMMS. For almost all of the period from 2006 to 2009, this methodology gave a good approximation of the incidence of loans with APOR spreads more than 1.75 percentage points above the PMMS (25 basis points higher than the cutoff for higher-priced reporting in 2010). Calculations using the "adjusted spread" showed that the estimated incidence of loans more than 1.75 percentage points above the PMMS is significantly reduced from 2006 to 2008 for all racial and ethnic groups and that the differences across groups are considerably smaller since 2008 than in the years prior.[45] Data reported for the last three months of 2009 using the new threshold showed only modest differences across groups.

As noted earlier, the overall reported incidence of higher-priced lending was about 50 basis points higher in 2011 than in 2010 (data for 2010 not shown in tables). Pricing relationships observed in the 2011 HMDA data are very similar to those found in the 2010 data. The 2011 HMDA data indicate that black and Hispanic-white borrowers are more likely, and Asian borrowers less likely, to obtain conventional loans with prices above the HMDA price-reporting thresholds than are non-Hispanic white borrowers. These relationships hold both for home-purchase and refinance lending and for nonconventional loans (tables 16.A and 16.B). For example, for conventional home-purchase lending in 2011, the incidence of higher-priced lending was 7.8 percent for black borrowers, 7.3 percent for Hispanic white borrowers, and 1.3 percent for Asian borrowers, compared with 3.9 percent for non-Hispanic white borrowers.

The gross differences in the incidence of higher-priced lending between non-Hispanic whites and blacks or Hispanic whites in 2011 are significantly reduced, but not completely eliminated, after controlling for lender and borrower characteristics. For example, the gross 2011 difference in the incidence of higher-priced conventional lending for home-purchase loans between Hispanic whites and non-Hispanic whites of 3.4 percentage points falls to only about 0.55 percentage point when the other factors available within the HMDA data are accounted for. The large gap in pricing between blacks and non-Hispanic whites is similarly reduced when other factors are considered. The pricing disparities across groups are significantly lower than the higher-priced incidence disparities observed from 2004 to 2007 using both the old Treasury-based threshold and our PMMS-based adjusted spread.

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[43] For purposes of presentation, the borrower- and lender-modified outcomes shown in the tables are normalized so that, *for the base comparison group* (non-Hispanic whites in the case of comparison by race and ethnicity and males in the case of comparison by sex), the mean at each modification level is the same as the gross mean.

[44] Although results here are reported for nonconventional lending as a whole, the analysis controls for the specific type of government-backed loan program (FHA, VA, or FSA/RHS) used by the borrower or loan applicant.

[45] See Avery and others, "The 2008 HMDA Data."

Table 16. Incidence of higher-priced lending, unmodified and modified for borrower- and lender-related factors, by type and purpose of loan and by race, ethnicity, and sex of borrower, 2011

A. Conventional loan

Percent except as noted

Race, ethnicity, and sex	Number of loans	Unmodified incidence	Modified incidence, by modification factor		Number of loans	Unmodified incidence	Modified incidence, by modification factor	
			Borrower-related	Borrower-related plus lender			Borrower-related	Borrower-related plus lender
	Home purchase				Refinance			
Race other than white only[1]								
American Indian or Alaska Native	2,905	7.85	4.42	4.14	8,313	3.14	2.46	1.82
Asian	77,211	1.32	3.28	3.70	195,610	.31	.93	1.48
Black or African American	21,655	7.84	6.52	4.69	73,397	4.21	3.19	2.36
Native Hawaiian or other Pacific Islander	2,285	2.76	3.98	4.23	6,593	1.18	1.88	2.26
Two or more minority races	395	2.28	3.12	3.87	1,405	.85	2.06	1.96
Joint	15,158	2.91	4.17	4.16	48,823	.97	1.67	1.72
Missing	84,659	1.67	2.78	3.90	339,272	.74	1.09	1.64
White, by ethnicity[1]								
Hispanic white	43,569	7.25	5.68	4.40	110,493	2.41	2.09	2.00
Non-Hispanic white	736,713	3.85	3.85	3.85	2,496,791	1.62	1.62	1.62
Sex								
One male	274,116	3.92	3.92	3.92	655,790	1.79	1.79	1.79
One female	192,796	3.55	3.27	3.63	522,500	1.99	1.70	1.72
Two males	10,304	7.00	7.00	7.00	22,219	2.00	2.00	2.00
Two females	7,924	4.76	5.41	6.97	22,594	2.07	1.77	2.16

Note: First-lien mortgages for owner-occupied, one- to four-family, site-built properties; excludes business loans. Business-related loans are those for which the lender reported that the race, ethnicity, and sex of the applicant or co-applicant are "not applicable." For definition of higher-priced lending and explanation of modification factors, see text and table 9, note 3. Loans taken out jointly by a male and female are not tabulated here because they would not be directly comparable with loans taken out by one borrower or by two borrowers of the same sex.

[1] See table 14, note 2.

With regard to the gender of applicants, we find relatively small differences in the incidence of higher-priced lending between single applicants of different genders and dual applicants of different genders once all available factors are taken into account.

Rate Spreads by Race, Ethnicity, and Sex

The 2011 data indicate that among borrowers with higher-priced loans, the gross APOR spreads are similar across groups for both home-purchase and refinance lending. This result holds for both conventional (table 17.A) and nonconventional lending (table 17.B). For example, for conventional home-purchase loans, the gross mean APOR spread was 2.49 percentage points for black borrowers and 2.76 percentage points for Hispanic white borrowers, while it was 2.49 percentage points for non-Hispanic white borrowers and 2.41 percentage points for Asian borrowers. Accounting for borrower-related factors or the specific lender used by the borrowers has little effect on the differences across groups.

Denial Rates by Race, Ethnicity, and Sex

Analyses of the HMDA data in previous years have consistently found that denial rates vary across applicants grouped by race or ethnicity. This continues to be the case in 2011. As in past years, blacks and Hispanic whites had notably higher gross denial rates in 2011 than non-Hispanic whites, while the differences between Asians and non-Hispanic whites

Table 16. Incidence of higher-priced lending, unmodified and modified for borrower- and lender-related factors, by type and purpose of loan and by race, ethnicity, and sex of borrower, 2011

B. Nonconventional loan

Percent except as noted

Race, ethnicity, and sex	Number of loans	Unmodified incidence	Modified incidence, by modification factor		Number of loans	Unmodified incidence	Modified incidence, by modification factor	
			Borrower-related	Borrower-related plus lender			Borrower-related	Borrower-related plus lender
	Home purchase				Refinance			
Race other than white only[1]								
American Indian or Alaska Native	5,754	2.78	2.91	2.09	2,312	5.02	3.74	2.83
Asian	26,746	2.09	2.01	2.02	8,577	4.03	3.92	4.06
Black or African American	87,774	4.16	3.53	3.10	44,070	10.80	7.33	5.24
Native Hawaiian or other Pacific Islander	4,288	2.64	2.46	2.57	1,913	3.50	3.58	4.06
Two or more minority races	681	.88	1.35	1.59	308	4.55	5.33	4.21
Joint	15,364	1.75	2.37	2.51	9,617	2.67	4.50	4.58
Missing	74,377	2.89	3.57	2.30	55,264	2.32	3.06	4.64
White, by ethnicity[1]								
Hispanic white	120,229	4.78	2.79	2.59	28,384	6.50	4.20	4.23
Non-Hispanic white	660,368	2.35	2.35	2.35	344,076	5.94	5.94	5.94
Sex								
One male	359,311	2.91	2.91	2.91	147,966	4.72	4.72	4.72
One female	234,298	3.89	2.92	2.91	81,252	12.04	6.03	5.56
Two males	13,567	2.94	2.94	2.94	3,692	2.76	2.76	2.76
Two females	10,629	3.24	3.36	3.54	3,261	4.60	4.07	4.66

Note: See notes to table 16.A.

generally were fairly small by comparison (tables 18.A and 18.B). For example, the denial rates for conventional home-purchase loans were 30.9 percent for blacks, 21.7 percent for Hispanic whites, 14.8 percent for Asians, and 11.9 percent for non-Hispanic whites. The pattern was about the same for nonconventional home-purchase lending, although the gap in gross denial rates between blacks or Hispanic whites and non-Hispanic whites was notably smaller than for conventional home-purchase loans.

For both conventional and nonconventional home-purchase lending, controlling for borrower-related factors in the HMDA data generally reduces the differences among racial and ethnic groups. Accounting for the specific lender used by the applicant reduces differences further, although unexplained differences remain between non-Hispanic whites and other racial and ethnic groups. An analysis of refinance loans shows similar patterns, although the differences in gross denial rates between blacks and non-Hispanic whites and between Hispanic whites and non-Hispanic whites tend to be larger than for home-purchase lending. For example, the gross difference between black and non-Hispanic-white borrowers refinancing using a conventional loan was 20.5 percentage points.

Some Limitations of the Data in Assessing Fair Lending Compliance

Previous research and experience gained in the fair lending enforcement process show that unexplained differences in the incidence of higher-priced lending and in denial rates among racial or ethnic groups stem, at least in part, from credit-related factors not available in the HMDA data, such as credit history (including credit scores), loan-to-value ratios, and differences in loan characteristics. Differential costs of loan origination and the competitive

Table 17. Mean average prime offer rate spreads, unmodified and modified for borrower- and lender-related factors, for higher-priced loans on one- to four-family homes, by type and purpose of loan and by race, ethnicity, and sex of borrower, 2011

A. Conventional loan

Percent except as noted

Race, ethnicity, and sex	Home purchase: Number of higher-priced loans[1]	Home purchase: Unmodified mean spread	Home purchase: Modified mean spread, by modification factor: Borrower-related	Home purchase: Modified mean spread, by modification factor: Borrower-related plus lender	Refinance: Number of higher-priced loans[1]	Refinance: Unmodified mean spread	Refinance: Modified mean spread, by modification factor: Borrower-related	Refinance: Modified mean spread, by modification factor: Borrower-related plus lender
Race other than white only[2]								
American Indian or Alaska Native	228	2.93	2.80	2.70	261	2.71	2.55	2.58
Asian	1,016	2.41	2.49	2.46	601	2.43	2.36	2.49
Black or African American	1,698	2.49	2.67	2.54	3,087	2.99	2.91	2.66
Native Hawaiian or other Pacific Islander	63	2.26	2.95	2.63	78	2.42	2.62	2.61
Two or more minority races	9	2.68	3.61	2.52	12	1.98	2.34	2.67
Joint	441	2.49	2.48	2.49	476	2.48	2.56	2.56
Missing	1,415	2.29	2.29	2.48	2,514	2.52	3.13	2.56
White, by ethnicity[2]								
Hispanic white	3,160	2.76	2.71	2.55	2,660	2.84	2.56	2.55
Non-Hispanic white	28,356	2.49	2.49	2.49	40,456	2.53	2.53	2.53
Sex								
One male	9,073	2.54	2.54	2.54	10,679	2.72	2.72	2.72
One female	5,767	2.48	2.48	2.51	9,937	2.80	2.73	2.72
Two males	721	2.58	2.58	2.58	445	2.54	2.54	2.54
Two females	377	2.55	2.51	2.52	467	2.68	2.56	2.49

Note: For definition of higher-priced lending and explanation of modification factors, see text. Loans taken out jointly by a male and female are not tabulated here because they would not be directly comparable with loans taken out by one borrower or by two borrowers of the same sex. For definition of average prime offer rate spread, see table 11, note 1.

1 See table 9, note 3.

2 See table 14, note 2.

environment also may bear on the differences in pricing, as may differences across populations in credit-shopping activities.

Despite these limitations, the HMDA data play an important role in fair lending enforcement. The data are regularly used by bank examiners to facilitate the fair lending examination and enforcement processes. When examiners for the federal banking agencies evaluate an institution's fair lending risk, they analyze HMDA price data and loan application outcomes in conjunction with other information and risk factors that can be drawn directly from loan files or electronic records maintained by lenders, as directed by the Interagency Fair Lending Examination Procedures.[46] The availability of broader information allows the examiners to draw firm conclusions about institution compliance with the fair lending laws.

It is important to keep in mind that the HMDA data, as currently constituted, can be used only to detect differences in pricing across groups for loans with APRs above the reporting threshold; pricing differences may exist among loans below the threshold. This gap in the loan pricing information will be addressed in coming years as the Consumer Financial Protection Bureau implements the expanded data reporting requirements set forth in the

46 The Interagency Fair Lending Examination Procedures are available at www.ffiec.gov/PDF/fairlend.pdf.

Table 17. Mean average prime offer rate spreads, unmodified and modified for borrower- and lender-related factors, for higher-priced loans on one- to four-family homes, by type and purpose of loan and by race, ethnicity, and sex of borrower, 2011

B. Nonconventional loan

Percent except as noted

Race, ethnicity, and sex	Number of higher-priced loans[1]	Unmodified mean spread	Modified mean spread, by modification factor		Number of higher-priced loans[1]	Unmodified mean spread	Modified mean spread, by modification factor	
			Borrower-related	Borrower-related plus lender			Borrower-related	Borrower-related plus lender
	Home purchase				Refinance			
Race other than white only[2]								
American Indian or Alaska Native	160	1.78	1.91	1.95	116	2.49	2.50	2.53
Asian	558	2.10	1.96	1.93	346	2.35	2.30	2.38
Black or African American	3,651	1.94	1.93	1.96	4,758	2.63	2.55	2.49
Native Hawaiian or other Pacific Islander	113	1.91	1.95	1.95	67	2.44	2.47	2.24
Two or more minority races	6	2.07	1.89	2.01	14	2.25	2.23	2.22
Joint	269	1.97	2.00	1.97	257	2.36	2.59	2.45
Missing	2,151	2.21	2.18	1.98	1,281	3.33	4.42	2.32
White, by ethnicity[2]								
Hispanic white	5,749	1.88	1.92	1.96	1,845	2.47	2.39	2.44
Non-Hispanic white	15,531	1.96	1.96	1.96	20,442	2.44	2.44	2.44
Sex								
One male	10,449	1.93	1.93	1.93	6,977	2.60	2.60	2.60
One female	9,114	1.99	1.95	1.93	9,785	2.63	2.65	2.64
Two males	399	1.90	1.90	1.90	102	2.17	2.17	2.17
Two females	344	1.85	1.84	1.92	150	2.30	2.16	2.23

Note: See notes to table 17.A.

Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010, including the provision requiring the reporting of rate spread information for all loans.

Assessing the Accuracy of Borrower Income Reported in the HMDA Data

During the housing boom of the 2000s, one underwriting practice that proliferated was the granting of mortgages with little or no documentation of income and assets. To investigate the extent to which borrower incomes may have been overstated on mortgage applications as a result of such practices, we compare the incomes reported for home-purchase borrowers in the HMDA data with the incomes of homebuyers taking out mortgages reported in Census 2000 and the ACS for 2005 through 2010.[47] While incentives to overstate income on mortgage applications sometimes exist, no such incentive exists when reporting income for the census or ACS. Thus, the Census 2000 and ACS data may provide "true" measures of income of homebuyers with which to gauge the accuracy of income reported on mortgage applications.[48]

[47] Others have conducted similar research, comparing HMDA data with American Housing Survey data for the years 1995 through 2007. Our analysis confirms and expands on theirs by comparing HMDA data with a different data source and by extending the analysis through 2010. See McKinley L. Blackburn and Todd Vermilyea (2012), "The Prevalence and Impact of Misstated Incomes on Mortgage Loan Applications," *Journal of Housing Economics*, vol. 21 (June), pp. 151–68.

[48] There are circumstances when applicants for mortgages do not need to report all income to a prospective lender

Table 18. Denial rates on applications, unmodified and modified for borrower- and lender-related factors, by type and purpose of loan and by race, ethnicity, and sex of applicant, 2011

A. Conventional loan application

Percent except as noted

Race, ethnicity, and sex	Number of applications acted upon by lender	Unmodified denial rate	Modified denial rate, by modification factor		Number of applications acted upon by lender	Unmodified denial rate	Modified denial rate, by modification factor	
			Borrower-related	Borrower-related plus lender			Borrower-related	Borrower-related plus lender
	Home purchase				Refinance			
Race other than white only[1]								
American Indian or Alaska Native	4,165	23.8	21.3	16.1	14,554	36.2	35.0	28.8
Asian	99,848	14.8	14.8	13.5	266,844	19.3	23.1	23.4
Black or African American	34,475	30.9	24.2	21.3	138,918	40.5	36.3	32.1
Native Hawaiian or other Pacific Islander	3,130	20.3	16.1	15.1	10,738	31.9	31.6	28.6
Two or more minority races	576	24.0	24.7	19.7	2,349	32.8	36.7	31.3
Joint	18,679	12.1	14.3	12.9	65,079	18.7	23.5	22.1
Missing	115,081	18.6	18.7	14.9	529,019	29.2	28.6	24.4
White, by ethnicity[1]								
Hispanic white	60,885	21.7	16.2	15.7	179,810	32.0	28.5	26.6
Non-Hispanic white	894,159	11.9	11.9	11.9	3,362,076	20.0	20.0	20.0
Sex								
One male	353,445	16.0	16.0	16.0	987,535	26.7	26.7	26.7
One female	245,656	15.6	14.3	14.8	767,689	25.8	24.4	24.6
Two males	13,586	17.9	17.9	17.9	31,981	24.5	24.5	24.5
Two females	10,332	17.6	15.3	14.5	32,124	24.0	23.5	23.7

Note: First-lien mortgages for owner-occupied, one- to four-family, site-built properties; excludes business loans. Business-related loans are those for which the lender reported that the race, ethnicity, and sex of the applicant or co-applicant are "not applicable." For explanation of modification factors, see text. Applications made jointly by a male and female are not tabulated here because they would not be directly comparable with applications made by one applicant or by two applicants of the same sex.

[1] See table 14, note 2.

The Census Bureau annually conducts the ACS, a household survey gathering a wide variety of information, including overall family income, homeownership status, and mortgage status. Because the survey was conducted on a somewhat smaller scale prior to 2005, we use only ACS data for 2005 and after, and we use Census 2000 data to measure borrower income at the beginning of the decade.[49] For each year of the analysis, we compute average family income at the state level for home-purchase borrowers in the HMDA data and for families in the ACS and Census 2000 data that appear to have recently purchased their home with a mortgage (those that reported they own their home, have a mortgage, and moved in the past year).[50] We then compute the ratio of HMDA income to ACS income (or, from Census 2000, census income), state by state and for three different periods: 2000, 2005 to 2006, and 2009 to 2010. Ratios substantially greater than 1 imply widespread overstatement of income on mortgage applications.

in order to qualify for a home loan. As such, incomes reported on mortgage applications tend to be lower than actual total household income in the absence of deliberately overstated income.

[49] Census 2000 and ACS microdata were extracted from Steven Ruggles, J. Trent Alexander, Katie Genadek, Ronald Goeken, Matthew B. Schroeder, and Matthew Sobek (2010), Integrated Public Use Microdata Series: Version 5.0 (machine-readable database) (Minneapolis: University of Minnesota).

[50] We use data only for metropolitan counties reported in the ACS and census microdata. This restriction helps ensure comparability between the two data sources since the HMDA data provide much better coverage of mortgage originations in metropolitan areas. In addition, results were suppressed for states with fewer than 50 households contributing to the statewide figure.

Table 18. Denial rates on applications, unmodified and modified for borrower- and lender-related factors, by type and purpose of loan and by race, ethnicity, and sex of applicant, 2011

B. Nonconventional loan application

Percent except as noted

Race, ethnicity, and sex	Number of applications acted upon by lender	Unmodified denial rate	Modified denial rate, by modification factor		Number of applications acted upon by lender	Unmodified denial rate	Modified denial rate, by modification factor	
			Borrower-related	Borrower-related plus lender			Borrower-related	Borrower-related plus lender
	Home purchase				Refinance			
Race other than white only[1]								
American Indian or Alaska Native	7,408	16.7	18.8	18.0	4,115	35.6	37.7	32.6
Asian	35,278	18.6	17.1	15.6	14,906	32.6	33.6	32.3
Black or African American	120,493	22.0	20.2	19.2	83,469	38.9	39.6	36.5
Native Hawaiian or other Pacific Islander	5,554	17.2	17.4	17.4	3,165	30.5	33.1	32.5
Two or more minority races	939	20.0	19.5	18.5	632	39.6	39.8	31.0
Joint	18,604	12.3	14.3	13.4	14,265	24.6	32.0	31.0
Missing	101,560	20.7	21.4	18.0	110,551	42.6	40.9	31.1
White, by ethnicity[1]								
Hispanic white	157,053	17.9	15.9	15.6	48,034	31.4	33.0	32.3
Non-Hispanic white	796,284	12.7	12.7	12.7	538,897	28.9	28.9	28.9
Sex								
One male	453,381	15.9	15.9	15.9	253,578	33.8	33.8	33.8
One female	295,544	16.0	14.7	15.0	144,648	36.3	32.6	32.5
Two males	18,167	20.0	20.0	20.0	6,151	30.9	30.9	30.9
Two females	13,935	18.9	17.1	17.8	5,598	33.5	29.3	30.1

Note: See notes to table 18.A.

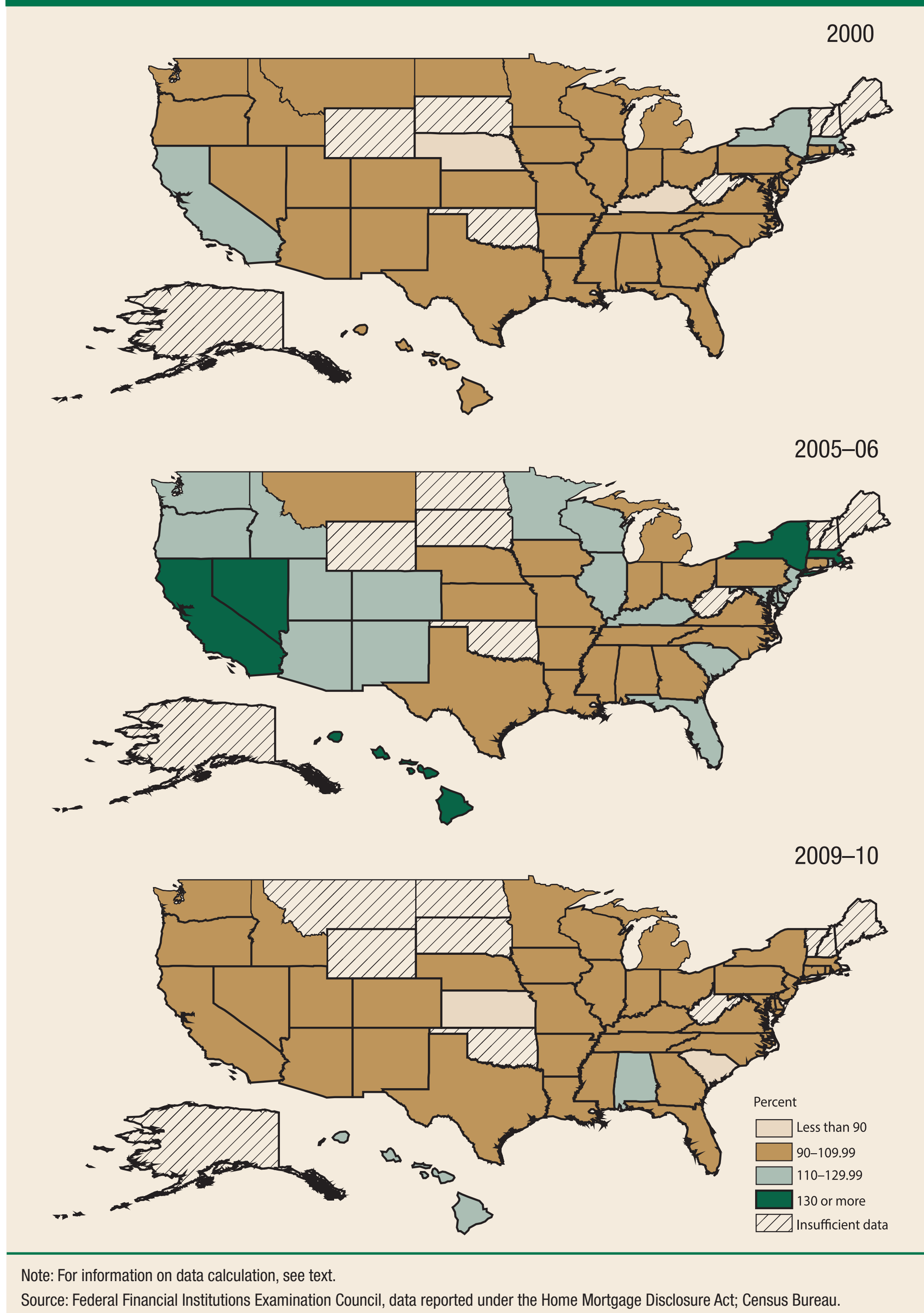
Figure 3 suggests that income on mortgage applications was widely overstated in a number of states in 2005 and 2006, particularly California, Hawaii, Massachusetts, Nevada, and New York. In these states, average borrower income as reflected in the HMDA data was 30 percent or more above the average ACS borrower income. In contrast, HMDA borrower income was no more than 10 percent above borrower income as reported in Census 2000 in almost all states. Finally, in 2009 and 2010, we observe a return to consistent incomes across data sources, with borrower incomes reported in HMDA and the ACS within 10 percent of each other in almost every state.

Users of the HMDA data should be aware that borrower income was likely significantly overstated during the peak of the housing boom, particularly in some areas of the country. One potential implication of this finding is that lending to lower-income borrowers, as measured in the HMDA data, may be attenuated around the peak of the housing market.

Transition to the 2010 Census Data and Revised Census-Tract Boundaries

Census data are used to evaluate the performance of lending institutions in complying with the CRA and the nation's fair lending laws. For example, family income data derived from the census are used to categorize census tracts by their relative median family income, and race and ethnicity data are used to characterize the minority population status of census

Figure 3. Ratio of average income for home-purchase borrowers, as reported under the Home Mortgage Disclosure Act, to average homebuyer income from Census 2000 and to that from the American Community Survey of 2005–06 and 2009–10, by state



Note: For information on data calculation, see text.

Source: Federal Financial Institutions Examination Council, data reported under the Home Mortgage Disclosure Act; Census Bureau.

tracts and other geographies.[51] In the CRA context, the relative income of census tracts is used to identify which census tracts are considered lower income (low or moderate income) and, as a consequence, a focus of CRA attention. In the fair lending enforcement context, census-tract minority population characteristics are used, for example, to help detect poten-

tial redlining behavior, where, for example, a lender has a policy or practice that results in little or no lending in a geographic area because of its racial or ethnic composition.

Using census sources to identify income, population, and housing characteristics of census tracts and broader areas has become more complicated recently. Unlike Census 2000, which used a survey questionnaire that asked a great many detailed questions (often referred to as the "long form"), the 2010 census used a brief questionnaire (referred to as the "short form"). In particular, the 2010 census focused on gathering household population counts and race, ethnicity, sex, and age characteristic information, but it provides relatively little other information—and no data on household or family income.

In lieu of collecting extensive detailed information from every household once a decade in conjunction with the decennial census, the Census Bureau now annually conducts the ACS. The ACS collects detailed population, income, and housing information from a representative sample of about 3 million households using a long-form questionnaire. Because of a relatively small sample size, the annual ACS data do not provide sufficient information to establish reliable estimates of census-tract characteristics. However, the Census Bureau aggregates ACS data across years and publishes data for each census tract based on the most recent five-year combined ACS data. The first five-year ACS aggregate data made available were derived from the 2005–09 annual surveys and used the census-tract boundaries established for Census 2000. The more recent 2006–10 combined ACS data were released to the public in December 2011 and are available from the FFIEC at its HMDA website. The 2006–10 ACS data use the census-tract boundaries created for the 2010 census. Using five-year aggregated data derived from the ACS, it is possible to categorize each census tract by its relative median family income.

FFIEC Treatment of Updated Census and ACS Data

The FFIEC has announced that, for purposes of preparing HMDA disclosure reports and for CRA performance evaluations, the 2006–10 ACS data will be used to classify census tracts by relative median family income and that these classifications will not be changed for a period of five years.[52] Five years hence, updated relative-income information will be derived from the combined 2011–15 ACS data, and census tracts will be reclassified according to their updated income profiles. Although, in principle, annual updates from the ACS could be used to reclassify census tracts by their relative incomes each year, the potential movement of census tracts from one relative-income category to another would greatly complicate CRA enforcement and make it difficult for lending institutions to plan and monitor their own activities.

A key aspect of the HMDA reporting rules is the requirement that lenders identify the census-tract locations of the properties involved in the applications and loans they report on each year. The 2011 HMDA data used census tracts as enumerated for Census 2000 and do not reflect any of the updated 2010 census or ACS data. Census-tract identifiers for the forthcoming 2012 HMDA data will be those enumerated for the 2010 census: Analysis of these data will use the 2010 census data and the 2006–10 ACS data.

[51] Relative income is the ratio of the census-tract median family income to the median family income of the broader area (either the MSA or the nonmetropolitan portion of the state) where the census tract is located.

[52] For a discussion of the shift to the 2006–10 ACS data for census-tract relative-income classification, see Federal Financial Institutions Examination Council (2011), "FFIEC Announces the Use of American Community Survey Data in Its Census Data Files," press release, October 19, www.ffiec.gov/press/pr101911_ACS.htm. The classification may change if the Office of Management and Budget (OMB) establishes new MSAs or alters the boundaries of existing MSAs. The OMB is scheduled to release new MSA delineations in 2013.

There were substantial changes in the number and boundaries of census tracts between the 2000 and 2010 censuses. As a consequence of population growth and migration, as well as other factors, such as new road construction, the 2010 census includes many more census tracts than Census 2000, and the geographic areas of many census tracts used for Census 2000 have been altered. Overall, Census 2000 included about 66,300 census tracts; the 2010 census includes about 74,000 census tracts. About 46 percent of the 2010 census tracts have the same geographic boundaries as in 2000, and about 72 percent have a land area that is 95 percent or more identical to the area in 2000. For purposes of this article, the census tracts that have 2010 areas that are 95 percent or more the same as in 2000 are referred to as "substantially similar" census tracts.

The shift from the 2000 to the 2010 census has important implications for those using the HMDA data. Perhaps most important is the possibility that a loan related to a given property may have been identified as being in a census tract in a particular relative-income group one year, but a loan on that same property may be reclassified into a different relative-income category the next year simply because of the shift from the income data based on Census 2000 to the income data based on the 2006–10 ACS. Reclassification could occur because the income profile of the population in the census tract has changed (altering the numerator in the relative-income calculation), because the income profile of the broader area has changed (altering the denominator in the relative-income classification), or both.

Evaluating the Effects of Census Data Changes

In order to gauge the potential effects of census data changes on the classification of lending activity, we undertook some simulations using the 2011 HMDA data. The analysis here focuses on the reclassification of *census tracts* due to changes in their relative family incomes and the reclassification of *home lending* (of all types) due to the reclassification of the census tracts where the properties associated with the loans are located. Because the location of branch offices may influence an institution's home-lending activity and because branch locations are an important component of CRA performance evaluations, we also assess the effects of the census data changes on *branch office* classification by census-tract income. Unlike lending, where an institution can potentially alter the geographic pattern of the home loan applications it receives by changes in marketing, outreach to real estate agents and homebuilders, and other techniques, branch office locations cannot be readily changed.

We evaluate the "pure" effects of updated population income estimates by comparing census-tract income classifications using Census 2000 data with classifications derived from the 2005–09 ACS surveys. Both Census 2000 and the 2005–09 ACS use the same census-tract boundaries. Also, to ensure that changes in MSA boundaries over the course of the past decade do not affect the analysis, we use the census-tract relative-income classifications as carried on the 2011 FFIEC HMDA data files. These files reflect the 2000 decennial estimates of median family income for each census tract but use current MSA boundary definitions. Thus, the only factors that can affect our estimates of income reclassifications are the updates to census-tract or broader area median family incomes that come about because of changes in family income estimates from shifting from Census 2000 to the more recent data based on the 2005–09 ACS.[53]

[53] Using the 2005–09 ACS income data in this exercise is not ideal since the actual income estimates used for CRA and HMDA purposes will be obtained from the 2006–10 ACS data. To address the possibility that the 2005–09 ACS income data and the 2006–10 ACS income data for individual census tracts differ significantly, and consequently affect reclassification estimates, we conducted a second analysis that is limited to the subset of census tracts that have substantially similar boundaries as defined for the 2000 and 2010 censuses. Results are in the final six columns of table 19. As shown in the table, the patterns are very similar whether the analysis is done

Table 19. Effect of the transition to updated census data on classification of census tracts, home lending, and branch offices, by census-tract relative-income reclassification

Census-tract relative-income reclassification[1]	Census 2000 to 2005–09 ACS						Census 2000 to 2006–10 ACS					
	Census tracts		Loans		Branch offices		Census tracts		Loans		Branch offices	
	Number	Percent	Number	Percent	Number	Percent	Number	Percent	Number	Percent	Number	Percent
Low to low	2,888	74	40,675	64	1,966	63	2,213	76	31,483	64	1,486	68
Low to moderate	860	22	16,682	26	718	23	624	21	13,270	27	478	22
Low to middle	110	3	2,910	5	157	5	58	2	2,441	5	118	5
Low to high	44	1	2,856	5	260	8	21	1	1,930	4	107	5
Memo: Total	**3,902**	**100**	**63,123**	**100**	**3,101**	**100**	**2,916**	**100**	**49,124**	**100**	**2,189**	**100**
Moderate to low	2,323	16	56,946	9	2,078	13	1,955	18	47,304	10	1,622	14
Moderate to moderate	9,208	65	410,331	65	10,624	66	7,060	65	301,313	65	7,912	67
Moderate to middle	2,411	17	151,120	24	3,171	20	1,813	17	104,672	23	2,139	18
Moderate to high	153	1	11,099	2	268	2	100	1	8,766	2	155	1
Memo: Total	**14,095**	**100**	**629,496**	**100**	**16,141**	**100**	**10,928**	**100**	**462,055**	**100**	**11,828**	**100**
Middle to low	108	0	2,430	0	159	0	80	0	1,795	0	113	0
Middle to moderate	4,777	15	314,565	9	6,993	14	3,784	16	237,760	11	4,967	14
Middle to middle	23,710	74	2,590,180	76	37,884	75	17,496	73	1,696,802	75	25,712	75
Middle to high	3,359	11	500,753	15	5,360	11	2,577	11	313,465	14	3,588	10
Memo: Total	**31,954**	**100**	**3,407,928**	**100**	**50,396**	**100**	**23,937**	**100**	**2,249,822**	**100**	**34,380**	**100**
High to low	8	0	64	0	21	0	0	0	0	0	0	0
High to moderate	36	0	1,342	0	71	0	23	0	1,042	0	47	0
High to middle	2,664	18	380,064	13	4,516	16	2,076	19	253,190	14	3,052	17
High to high	11,907	81	2,515,553	87	22,791	83	8,750	81	1,530,101	86	14,399	82
Memo: Total	**14,615**	**100**	**2,897,023**	**100**	**27,399**	**100**	**10,849**	**100**	**1,784,333**	**100**	**17,498**	**100**

Note: For an explanation of the transition to updated census data, see the text discussion "Transition to the 2010 Census Data and Revised Census-Tract Boundaries." Census tracts are as defined in the decennial censuses for 2000 (Census 2000) and 2010.

[1] For definitions of census-tract income categories, see table 14, note 4.

ACS American Community Survey.

Source: For census-tract locations of properties related to home loans, Federal Financial Institutions Examination Council, data reported under the Home Mortgage Disclosure Act; for branch office locations, data derived from the Summary of Deposits as of June 30, 2011.

Census-Tract Reclassification

Our analysis indicates that the transition from the Census 2000 to the 2005–09 ACS data for classifying census tracts by relative income would result in significant changes in census-tract income category classification. For example, 17 percent of the census tracts that were classified as moderate income using the 2000 income data would be reclassified as middle income, and 1 percent would be reclassified as higher income (table 19). Because these census tracts would no longer be classified as falling in the lower-income category, lending and other activities, including branch office locations, in these census tracts would no longer be a focus of CRA attention. However, about 15 percent of middle-income census tracts would be reclassified as moderate income, and activities in these census tracts would gain emphasis in CRA performance evaluations.

using the 2005–09 ACS data and the 2000 census-tract boundaries or the 2006–10 ACS data using only the substantially similar census tracts.

Loan Reclassification

Results are similar when the analysis considers reclassification of home loans instead of census tracts, but some of the transitions are more pronounced. An analysis using the Census 2000 and the 2005–09 ACS data indicates that about 24 percent of the home loans extended in 2011 and classified as falling in moderate-income census tracts would transition and be reclassified as falling in a middle-income census tract and that 2 percent of the loans would transition to a higher-income census tract. At the same time, about 9 percent of the loans falling in middle-income areas would be reclassified as falling in moderate-income areas. However, in terms of the absolute number of loans, had the new census-tract relative-income classifications been used in 2011, there would have been a net increase in mortgage lending to low- and moderate-income neighborhoods of about 150,000 loans, about 22 percent higher than the number of LMI loans in 2011 under current census-tract relative-income classifications (data derived from table 19).

Branch Office Reclassification

For our analysis of the effects of the transition from the Census 2000 to the ACS-based data on the classification of branch offices by census-tract relative income, we use the location of branch offices as reported in the Summary of Deposits (SOD) as of June 30, 2011. The SOD is an annual survey, compiled by the Federal Deposit Insurance Corporation (FDIC), of branch office deposits for all FDIC-insured banking institutions.[54] The data include the location (state, county, and census tract) of each branch (and headquarters) office and the dollar amount of deposits that are allocated to that branch by the banking institution. For this exercise, we excluded the locations of automated teller machines (ATMs). Although ATMs are considered in CRA performance evaluations under the "services test," it seems unlikely that ATM locations have much influence on home-lending activity, the main focus of this article.[55] In total, the branch office analysis included about 98,000 branch offices.

As in the analysis of census tracts and home lending described earlier, our analysis of branch office reclassification indicates that the switch from Census 2000 data to the more recent ACS-based income data would have a notable effect on the classification of branch offices by census-tract relative income. For example, 20 percent of the branch offices that were classified as located in a moderate-income census tract using the 2000 income data would be reclassified as middle income, and 2 percent would be reclassified as higher income, using the 2005–09 ACS data. Because these branch offices would no longer be classified as located in lower-income census tracts, they would no longer be a focus of CRA attention. However, about 14 percent of branches classified as being located in middle-income census tracts based on Census 2000 data would be reclassified as being located in moderate-income census tracts, and consequently, these offices would gain emphasis in CRA performance evaluations. Because there are more branch offices in middle-income census tracts than in low- or moderate-income census tracts, the transition to the updated census information will result in a net increase of about 3,400 branch offices in areas that are the focus of CRA attention.

[54] See Federal Deposit Insurance Corporation, "Summary of Deposits," webpage, www2.fdic.gov/sod.

[55] CRA compliance evaluations focus on three aspects of performance: lending, services, and investment. For more information, see Federal Financial Institutions Examination Council, "CRA Rating Search Frequently Asked Questions," webpage, www.ffiec.gov/craratings/ratings_faq.htm.

Appendix A: Requirements of Regulation C

The Federal Reserve Board's Regulation C requires lenders to report the following information on home-purchase and home-improvement loans and on refinancings:

For each application or loan

- application date and the date an action was taken on the application
- action taken on the application
  - — approved and originated
  - — approved but not accepted by the applicant
  - — denied (with the reasons for denial—voluntary for some lenders)
  - — withdrawn by the applicant
  - — file closed for incompleteness
- preapproval program status (for home-purchase loans only)
  - — preapproval request denied by financial institution
  - — preapproval request approved but not accepted by individual
- loan amount
- loan type
  - — conventional
  - — insured by the Federal Housing Administration
  - — guaranteed by the Department of Veterans Affairs
  - — backed by the Farm Service Agency or Rural Housing Service
- lien status
  - — first lien
  - — junior lien
  - — unsecured
- loan purpose
  - — home purchase
  - — refinance
  - — home improvement
- type of purchaser (if the lender subsequently sold the loan during the year)
  - — Fannie Mae
  - — Ginnie Mae
  - — Freddie Mac
  - — Farmer Mac
  - — private securitization
  - — commercial bank, savings bank, or savings association
  - — life insurance company, credit union, mortgage bank, or finance company
  - — affiliate institution
  - — other type of purchaser

For each applicant or co-applicant

- race
- ethnicity
- sex
- income relied on in credit decision

For each property

- location, by state, county, metropolitan statistical area, and census tract
- type of structure
  - — one- to four-family dwelling
  - — manufactured home
  - — multifamily property (dwelling with five or more units)
- occupancy status (owner occupied, non-owner occupied, or not applicable)

For loans subject to price reporting

- spread above comparable Treasury security for applications taken prior to October 1, 2010
- spread above average prime offer rate for applications taken on or after October 1, 2010

For loans subject to the Home Ownership and Equity Protection Act

- indicator of whether loan is subject to the Home Ownership and Equity Protection Act

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Consumers and Debt Protection Products: Results of a New Consumer Survey

Thomas A. Durkin (now retired) and Gregory Elliehausen, of the Board's Division of Research and Statistics, prepared this article.

Debt protection products help consumers pay off a debt or continue or suspend payments upon the occurrence of unfortunate and unpredictable events like death, disability, and involuntary unemployment. The credit insurance version is almost as old as familiar consumer credit itself, but there also are newer forms of debt protection called debt cancellation and debt suspension agreements that will be referred to here simply as credit protection products. Evidence shows that many consumers purchase debt protection when they enter into various kinds of credit arrangements.

Credit life insurance is a form of term life insurance that accompanies credit obligations and repays the debt if death occurs. Credit disability insurance (often referred to as credit accident and health, or credit A&H, insurance) is a form of accident and health insurance, while involuntary unemployment insurance (IUI) is casualty insurance that also can accompany credit arrangements. In the case of either disability insurance or IUI, the insurance company makes the payments during disability or involuntary unemployment up to some maximum benefit period.

As indicated, some other debt protection products like debt cancellation contracts and debt suspension agreements are newer. To differentiate their separate legal status from credit insurance, they are often generically referred to as credit protection products. Like credit insurance, they provide to consumers who purchase them either cancellation of the debt or the right to suspend or defer payment to the lender for a time if covered events occur. These latter products are an agreement between the consumer and the lender and do not involve the sale of insurance to a consumer by a third-party insurer. Despite this difference, from the consumer's standpoint credit insurance and credit protection products work basically the same way. Both kinds of protection typically are offered at the point of sale of a lending arrangement (or sometimes afterward), and they provide the same types of benefits. Debt cancellation and suspension agreements are the most common on open-end credit card plans offered by banks.

Despite availability of debt protection in the form of credit insurance for decades, there still has not been a great deal of consumer research on these products. In particular, consumers' experiences with and attitudes toward credit insurance have been documented only infrequently over a long period of time.[1] This article reexamines consumer experience with these products by reporting on new consumer survey results.

Note: The authors thank the Consumer Credit Industry Association for making the data available for analysis.

[1] The survey results are found in the following sources: Charles L. Hubbard, ed. (1973), *Consumer Credit Life and Disability Insurance* (Athens, Ohio: Ohio University); Joel Huber (1976), *Consumer Perceptions of Credit Insurance on Retail Purchases* (West Lafayette, Ind.: Purdue University); Thomas A. Durkin and Gregory E. Elliehausen (1978), *1977 Consumer Credit Survey* (Washington: Board of Governors of the Federal Reserve System); Anthony W. Cyrnak and Glenn B. Canner (1986), "Consumer Experiences with Credit Insurance: Some New Evidence," *Federal Reserve*

The next section of this article describes these products more fully and addresses why they have sometimes been viewed as controversial. The following section provides background for the survey approach to studying these products, and the next examines results of a new nationwide survey of consumers conducted in early 2012. The final section provides a brief summary and conclusion.

Debt Protection Products

Although some debt protection products are not, by legal standards, insurance, consumers see such protection, including both credit insurance and other products, as functionally similar to ordinary kinds of term life and disability insurance. The origin of debt protection products is in the anxiety sometimes felt that death, disability, or another unfortunate life event could cause an earner's family to have difficulty repaying debts or maintaining payments. Because these products' origins are in the lending arena, subsequent regulation has required that the basic nature of the insurance coverage is defined by the terms of the associated credit contract. This requirement has maintained and fostered some continuing differences between debt protections and ordinary insurance and has affected the specifics of related regulation.

One difference between debt protection and ordinary insurance is that the face amount of the debt protection in force is not constant for debt-related products; rather, it declines over the life of the debt as the credit is repaid (or fluctuates in the case of credit card credit). In contrast, most ordinary term insurance is sold in fixed amounts and remains at a constant face amount for the specified period of time.

A second difference arises from the heritage of debt protection in the automobile credit, furniture, appliance, and small cash loan industries rather than in the traditional insurance industry: the small size of typical debt protection contracts. Small sized credit contracts and related debt protection have caused the revenue streams from the protection products to be small as well, leading to highly simplified underwriting, marketing, and paperwork procedures.

In particular, debt protection products developed without a differentiating set of actuarially variable characteristics for pricing, such as sex, age, health, or smoking habits. Furthermore, they were and are still sold part time by lending officers and personnel in the process of booking and servicing consumer credit transactions. Because of account sizes, providers of debt protection have been both unwilling and unable to invest the sums necessary to have it carefully underwritten consumer by consumer or, in the case of credit insurance, sold by independent or ordinary-licensed, full-time insurance agents.

For credit insurance, the lender's personnel function as the sales agents for the insurer (with necessary state licensure if required). For debt cancellation or suspension, loan officers provide the credit protection products approved by their own lending institution. Because of the short term and generally small cash flows, lending officers normally have asked customers only one basic question: whether they want the protection coverage or not. If custom-

Bank of San Francisco Economic Review, (Summer), no. 3, pp. 5–20; John M. Barron and Michael E. Staten (1996), *Innovations in Financial Markets and Institutions*, vol. 10: *Consumer Attitudes toward Credit Insurance* (Norwell, Mass.: Kluwer Academic Publishers); and Thomas A. Durkin (2002), "Consumers and Credit Disclosures: Credit Cards and Credit Insurance," *Federal Reserve Bulletin*, vol. 88, pp. 201–13, www.federalreserve.gov/pubs/bulletin/2002/0402lead.pdf. See also Robert A. Eisenbeis and Paul R. Schweitzer (1979), *Tie-Ins between the Granting of Credit and Sales of Insurance by Bank Holding Companies and Other Lenders*, Staff Study 101 (Washington: Board of Governors of the Federal Reserve System, February), which discusses survey results.

ers do want protection coverage, there may be a secondary question to determine eligibility—for example, customer age. In some cases, there also might be a recommendation that the protection is a good idea.

As noted, there typically has been no pricing differentiation according to sex, age or actuarial mortality, or health characteristics of the customer population, except that credit life insurance coverage generally has been unavailable for those over age 65 (or, in some states, over age 70). This lack of pricing differentiation means, of course, that debt protection products are relatively more attractive for males, older consumers, those in poorer health, and those adopting certain lifestyle choices (smoking, for example). The resulting adverse selection against the insurer or lender, together with the small size of the protection contracts, has led to the argument for sales simplification in order to reduce production costs per dollar of protection.

Although generally required by subsequent regulation to be available to any debtor meeting the age requirements, the simplified marketing of debt protection products through lending personnel rather than through experienced agents has been at times controversial. Part of the contention has been that in the absence of any attempt to explore customers' insurance portfolio needs and their special risk characteristics, potential purchasers receive no professional aid in the purchase decision. Some observers have maintained that the marketing is so simplified that the products and their pricing are not even adequately explained. As a consequence, they contend, some consumers do not consider implications of the purchase adequately or sometimes even understand at all what they purchased or how it works.

Further, for credit insurance, in an effort to save on paperwork and recordkeeping and reduce the need for monthly payments to both the creditor and the insurer, the relatively small premium amounts frequently have been collected in a single premium at the outset and financed in the loan balance. In addition to reducing processing expenses, this approach has the advantage that the protection never lapses, even if the consumer becomes delinquent in making payments on the underlying credit obligation. Nonetheless, criticism of the single premium approach and financing it in the loan has led directly to more widespread prevalence in recent years of protection with a monthly fee instead of a single premium. This approach has become known as monthly outstanding balance protection (frequently abbreviated as MOB insurance or protection). Fees for debt cancellation agreements and suspension agreements also are collected monthly.

As outlined, controversy over credit insurance and credit protection products arises not so much from the usefulness of the products for the protection of assets, credit standing, and general financial well being in the case of personal disasters, as from the methods used in the distribution of debt protection. Critics have argued that the distribution method that takes place at the credit point of sale provides both the incentive and the opportunity for lending personnel to mislead consumers about the usefulness of the insurance or other products and even coerce them into purchasing these products.[2]

In contrast, product supporters have argued that the small size of the debt protection and the limited cash flow arising from small credit insurance and credit protection products

[2] That such opportunities exist is evidenced by a recent enforcement action against Capital One. In July 2012, Capital One settled an enforcement action brought by the Consumer Financial Protection Board (CFPB) involving the marketing of credit protection and other ancillary products by a third-party vendor. The CFPB charged that the vendors did not always inform credit card holders that the products were optional, did not always provide adequate information on the cost and terms of the product, and misled consumers that the product would improve their credit score or increase their credit limits. See Administrative Proceeding File No. 2012-CFPB-0001 (2012), http://files.consumerfinance.gov/f/201209_cfpb_0001_001_Consent_Order_and_Stipulation.pdf.

have not allowed either extensive careful underwriting or review of a consumer's full insurance and protection needs by trained insurance underwriters or financial planners. Rather, in their view, a very useful one-size-fits-all product line has evolved with no or few underwriting differentiations, in order to reduce costs. So as to avoid "cherry picking" or other possible unfair forms of discrimination for this limited set of offerings, law and regulation in this area have also evolved to the one-size-fits-all approach and now generally permit only very limited differentiation among customers (such as an overall age limit like 65 or 70). Under these circumstances, sales effort and review at the point of sale is going to be short and consumers are going to have to decide for themselves what their overall insurance and financial planning needs are.

Credit insurance has long been subject to regulation that varies by state but generally includes state approval of premium rates charged, policy forms, disclosures, the solvency of the insurance companies, and the sales approaches of producers. Newer debt cancellation and suspension products have been judged by federal banking regulators and by courts as legally a part of lending and not a form of insurance. They are offered by national and state banks as banking products under the National Bank Act and state banking parity laws and are not regulated as insurance under state insurance laws. Instead, they are governed by rules of national and state bank regulatory agencies, in particular rules of the Office of the Comptroller of the Currency (OCC), and are enforced by the OCC and other bank regulators. Despite the legal differences, it is common in public policy discussions of consumer protection to examine credit insurance and other debt protection products together. Although credit insurance is an insurance product and other forms of debt protection are considered banking products, from the consumer's standpoint they provide the same kinds of benefits and are close substitutes.

Both credit insurance and other forms of debt protection are also subject to the federal Truth in Lending Act (TILA). The concern that lenders could mislead and misdirect consumers at the point of sale of credit accounts led to a special provision in the law at its passage in 1968. A section of TILA excludes the charge for debt protection products from the finance charge if there is a separate disclosure of the voluntary nature of the purchase before the charge occurs (see 12 *CFR* 226.4(d)). This provision makes the voluntary nature of the purchase decision a key issue for consumer research.

Survey Background

Over the past few decades, the interest of researchers in consumers' reactions to these products has caused them to undertake a number of interview studies to explore consumer experiences of purchasing debt protection products, especially the sales pressure concern. Past studies have focused on credit insurance, the older form of debt protection. The working hypothesis of such efforts has been two-pronged. First, there may be instances where choice is limited by some abusive lenders. However, if the proportion of accounts with credit insurance or debt protection (the "penetration rate") is well short of universal, then it is difficult to conclude that consumers have no choice in the matter or to argue for changes to make true choice more widespread. Second, if consumers express favorable attitudes toward the protection products in question, then it is likewise difficult to conclude that there is widespread abusive pressure or requirements to purchase products they consider not useful.

Two basic kinds of survey approaches might be undertaken to explore these issues. The first is the geographic area approach—for example, a statewide or nationwide representation. This approach has an advantage in that results reflect the relevant geographic area as a whole, but it presents a challenge in that it is not a very efficient way to obtain feedback

about a relatively uncommon event. Such an approach can reveal statewide or nationwide penetration of debt protection purchases on credit accounts, for instance, but it takes a sizable number of expensive screening interviews to do so as not everyone is a credit user and those who are may not be a purchaser of debt protection.

The second approach is obtaining interviews under a sample design that is more limited in scope—for example, customers of a single supplier or a group of suppliers. Companies use this approach frequently when they survey their own customers for marketing purposes and to measure customer satisfaction. The difficulty, of course, is that this approach prevents interviews beyond the confines of the source list employed. A company surveying its own customer base, for instance, learns little or nothing about the customers of other companies. Certainly it is impossible to measure such things as the nationwide sales penetration rate with this approach.

In the past, the Federal Reserve has reported results of nationally representative samples of interviews with users of credit insurance undertaken as part of its program of interviewing consumers from time to time on a variety of financial matters. Surveys using similar questionnaires and the same interviewing organization took place in 1977, 1985, and 2001.[3] This article continues along the lines of Federal Reserve research, using a survey from early 2012 with similar interviews and undertaken by the same survey organization. The new survey uses many of the same questions employed in the late 2001 interviews reported in the *Federal Reserve Bulletin* in April 2002.[4] The differentiating factor of the 2012 survey is that there was an attempt to make sure that debt protection products that were not insurance were also included. There also were a few additional questions in 2012 and a few questions omitted from the 2001 questionnaire. Actual interviewing was conducted all four times by the Survey Research Center (SRC) of the University of Michigan.

New Survey

In January and March 2012, the SRC conducted a total of 1,006 interviews about consumers' experiences with credit insurance and other debt protection products. The SRC's research approach produced a nationwide probability sample of respondents that is representative of the contiguous 48 states within statistical confidence limits. The SRC coded the interview results and provided a machine-readable data set in SAS format. The authors wrote the necessary SAS computer program to produce the tables reported here.

The initial research question dealt with the trend in penetration rates over time, where the term "penetration" refers to the proportion of consumers using a type of credit who simultaneously purchase debt protection products of one kind or another. For analytical purposes, a credit user who indicated purchasing either the life or disability form of either credit insurance or the related banking-product cancellation or suspension forms of protection were counted as purchasers. By counting these individuals and forming a ratio of purchasers to total credit users, it was possible to examine recent penetration rates for various kinds of credit.

The penetration rate on closed-end consumer installment credit was 22 percent in early 2012, about the same as in 2001 (table 1). The rate both years was substantially below the corresponding rates of 64 and 65 percent found in 1977 and 1985, respectively, with similar

[3] See Durkin and Elliehausen (1978), Cyrnak and Canner (1986), and Durkin (2002) in note 1.

[4] See Durkin (2002) in note 1.

Table 1. Debt protection penetration rates, 1977–2012
Percentage distributions within groups of credit users

Debt protection status	Installment credit				Mortgage credit		Credit card	
	1977	1985	2001	2012	2001	2012	2001	2012
Have	63.9	64.7	22.7	22.0	32.1	23.9	20.1	14.0
Do not have	30.1	33.1	74.4	75.6	60.5	72.3	73.9	82.0
Do not know/refuse	6.0	2.2	2.9	2.4	7.4	3.8	6.0	4.0
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Note: Here and in subsequent tables, columns may not sum to totals because of rounding.
Source: For source information here and in subsequent tables, see text note 1.

research approaches. This decline is substantial and suggests that if widespread aggressive sales are being attempted, they are not very successful.

The penetration rate on mortgage credit appeared to be in the same general range as on closed-end consumer installment credit, especially in 2012. (Mortgage credit and credit card penetration were not measured in the 1977 or 1985 surveys.) Both years, penetration rates on credit cards were a little lower than on closed-end installment credit. The penetration rates on credit cards were somewhat higher than those measured by the Government Accountability Office (GAO) in 2011. The GAO measured penetration among card *accounts*, ascertained from the files of card issuers. The consumer survey approach should normally be expected to produce a higher penetration measurement, as consumers might have more than one account and not all accounts might have associated debt protection. If consumers have more than one account they are counted as a “yes” if any of their card accounts have debt protection, as was the case with this survey, then the rate measured across *consumers* would be higher than the rate measured across accounts.[5]

To look at the sales pressure issue, the first approach was to question respondents directly about their experience at the point of sale. Respondents with common closed-end consumer credit outstanding were asked about the debt protection offering at the point of sale and whether or not they had purchased any protection products. It appears that experience has changed sharply since 1977.

In 1977, the majority (72 percent) of closed-end consumer credit users who had purchased debt protection said that the creditor had either recommended the purchase or recommended it strongly (table 2). This proportion fell to 36 percent in 1985 and to 29 percent in 2001, before rising a bit to 38 percent in 2012. It is worth noting again that the penetration rate was also much lower in the latter two years. This decrease in the penetration rate means that among closed-end installment credit users, the proportion who both purchased and who noted receiving a recommendation to that effect fell sharply after 1977 due to both lower penetration rates and fewer experiences of a recommendation. In 1977, about 46 percent of closed-end installment credit users reported that they purchased and received a purchase recommendation from the creditor of varying intensity (that is, the 72.4 percent who said that debt protection was “recommended” or “strongly recommended/required” (table 2) of the 63.9 percent who purchased (table 1)). These percentages compare to only about 8 percent in 2012 (37.7 percent of purchasers who said that debt protection was “rec-

5 See Government Accountability Office (2011), *Credit Cards: Consumer Costs for Debt Protection Products Can Be Substantial Relative to Benefits but Are Not a Focus of Regulatory Oversight* (Washington: GAO, March). In this report, the GAO estimated the penetration rate among bank type credit card *accounts* (not among consumers) at about 7 percent.

Table 2. Recommendations concerning debt protection purchase at point of sale on installment credit, 1977–2012

Percentage distributions within groups of users of installment credit, with and without debt protection

Recommendation	Debt protection							
	1977		1985		2001		2012	
	With	Without	With	Without	With	Without	With	Without
Never mentioned	10.6	52.2	14.8	45.2	15.4	53.3	18.7	62.7
Offered	15.0	22.6	44.7	35.5	53.2	33.9	43.5	29.5
Recommended	33.1	17.0	16.4	12.9	12.2	4.1	17.6	0.5
Strongly recommended/required	39.3	2.3	20.1	2.6	16.6	3.4	20.1	0.9
Do not know/refuse	2.1	5.9	3.9	3.9	2.6	5.3	*	6.5
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

* Less than ½ of 1 percent.

ommended" or "strongly recommended/required" (table 2) of the 22 percent who purchased (table 1)). After 1977, the proportion of purchasers who indicated the product was merely offered rather than recommended rose sharply, from 15 percent in 1977 to about 53 percent in 2001 and 44 percent in 2012 (table 2).

In each of the survey years except 1985, more than one-half of those who did not purchase a protection product on closed-end consumer credit reported that protection products were not even mentioned by the lender. Even in the exception year 1985, the proportion of those surveyed not hearing any mention was about 45 percent. It seems difficult to argue that people are coerced into buying an add-on or ancillary product to a credit transaction if it is not even mentioned to them at the point of sale. (Some of the purchasers also indicated it was not mentioned, which must mean either they purchased it after some kind of follow-up or they requested it at the point of sale without mention by the lender.) The proportion of nonpurchasers who said the products were not mentioned approached two-thirds (63 percent) in 2012.

The second part of the hypothesis is that consumers who felt pressured to buy an add-on or ancillary product they did not want would probably not be very favorably inclined toward the add-on or ancillary product. To examine this possibility, consumers with and without debt protection were asked about their feelings toward buying the protection, specifically whether such purchase is a good idea or a bad idea.

Experience in 2012 confirms prior findings that the overwhelming majority of purchasers of debt protection on closed-end consumer credit consider the purchase to be a good idea. The proportion answering "good" or "good with some degree of qualification" exceeded 85 percent in each of the interview years (table 3). In contrast, the proportion responding "bad" was less than 10 percent in all but the most recent survey, in which the proportion reached 11 percent. The slightly higher incidence of this response in 2012 may be an artifact of the preceding lengthy recession. It seems possible that if consumers find themselves in a situation in which they realize after the fact that an expenditure on insurance or an insurance-like substitute did not result in a payoff, they may to some degree regret the expenditure at a time when budgets are tight. Of course, consumers did not suffer the loss they insured against either, and the peace of mind entailed with the protection purchase may still resonate with many of them.

Table 3 also demonstrates that attitudes are much different between purchasers and nonpurchasers of the protection products. For the nonpurchasers, attitudes toward the protec-

Table 3. Attitudes toward debt protection among users of installment credit, 1977–2012
Percentage distributions of users of installment credit, with and without debt protection

Attitude	Debt protection							
	1977		1985		2001		2012	
	With	Without	With	Without	With	Without	With	Without
Good	86.7	59.8	89.9	56.4	88.5	32.3	85.5	53.8
Good with qualifications	8.6	18.9	2.9	8.3	3.8	6.1	*	3.2
Neither good nor bad	2.1	9.1	1.9	6.4	3.2	13.9	3.1	1.8
Bad with qualifications	*	2.7	*	2.6	*	1.6	*	0.8
Bad	2.2	9.5	5.2	26.3	4.5	46.0	11.4	40.5
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

* Less than ½ of 1 percent.

tion products are decidedly less favorable than among purchasers, although certainly not unfavorable in every case. For those with closed-end consumer installment credit outstanding but who did not purchase debt protection, the view that purchasing protection is "good" or "good with qualifications" has fallen from over three-quarters (79 percent) of respondents in 1977 to 38 percent in 2001, before rebounding in 2012 again to a majority (57 percent). It is possible that this recent upturn is also due to heightened concerns about financial difficulties as a result of the recession. Nonetheless, a somewhat higher portion of nonpurchasers with an unfavorable attitude toward the protection products is consistent with their choices not to purchase.

The attitude measurement in 2012 among users of credit other than closed-end installment credit produced largely similar results. More than four-fifths (82 percent) of those who purchased debt protection on mortgage credit expressed a favorable attitude, and the favorable feeling among credit card holders with protection (77 percent) was almost as high (table 4). Not surprisingly, favorable views among nonpurchasers of protection again were somewhat less common on these kinds of credit, but they still reached 47 percent among mortgage credit users and 45 percent among credit card account holders. Likewise, 48 percent of those with no closed-end credit outstanding were not wholly predisposed against debt protection products (lower right grouping in table 4). Still, the differences in attitudes between purchasers and nonpurchasers of debt protection products suggest that the views of the former should be considered in assessing the value of these products. It seems unreasonable to give undue weight to the views of those not using the products in the first place.

Table 4. Consumer attitudes toward debt protection, 2012
Percent

Attitude	Installment credit		Mortgage credit		Bank card		No closed-end credit (no protection)
	With	Without	With	Without	With	Without	
Good	85.5	53.8	80.4	44.9	77.1	43.7	45.8
Good with qualifications	*	3.2	1.3	2.0	*	1.7	1.9
Neither good nor bad	3.1	1.8	*	2.7	1.6	1.9	2.3
Bad with qualifications	*	0.8	*	*	0.5	0.3	0.4
Bad	11.4	40.5	18.3	50.3	20.8	52.3	49.5
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

* Less than ½ of 1 percent.

Table 5. Satisfaction with purchase of debt protection, 2001 and 2012
Percentage distributions within groups of credit users

Satisfied with purchase?	Installment credit		Mortgage credit	
	2001	2012	2001	2012
Very	26.9	38.2	25.8	32.6
Somewhat	63.5	40.9	56.5	52.9
Subtotal: Satisfied	90.4	79.1	82.3	85.5
Neither satisfied nor dissatisfied	3.8	20.9	11.3	10.6
Somewhat dissatisfied	2.6	*	1.6	2.1
Very dissatisfied	*	*	*	1.9
Do not know/refuse	3.2	*	4.8	*
Total	**100.0**	**100.0**	**100.0**	**100.0**

* Less than ½ of 1 percent.

Attitudes were also measured in a related but somewhat different manner. Specifically, purchasers of debt protection were asked directly about their satisfaction with the protection product purchased. Obviously, this view could not be asked of nonpurchasers. Again, using this measurement, purchasers of debt protection expressed favorable views. Approximately four-fifths of purchasers expressed satisfaction in each of the years when measurements were undertaken (table 5). Relatively few expressed dissatisfaction, although some appeared indifferent. Again, it appears important to remember the views of users as well as nonusers in any discussion of the value of debt protection products.

Purchasers also expressed a high degree of willingness to purchase debt protection on future credit use. More than 70 percent of purchasers indicated a willingness to purchase again on both installment and mortgage credit in both 2001 and 2012 (table 6). While a favorable attitude now does not necessarily translate directly into a purchase later, it is also possible that actual purchases could be higher than the attitude expressed now. When entering into the next credit contract, financial anxieties may resurface and purchasing debt protection may again produce the peace of mind that it apparently did in many cases this time. None of these behaviors suggest the kind of unhappiness with a product that might arise if purchasers felt that they were being pushed into the purchase or that the product itself was not very useful.

Overall, favorable attitudes and willingness to purchase again among some consumers do not seem especially surprising, given the uncomfortable feeling that many consumers have when entering into credit arrangements. Evidence from the Federal Reserve Board's Survey of Consumer Finances demonstrates low levels of life insurance among many families. The most recent survey available (2010) shows that more than two-fifths (41 percent) of families at that time had less than $10,000 of life insurance but among them 30 percent had a mort-

Table 6. Willingness to purchase debt protection again, 2001 and 2012
Percentage distributions within groups of credit users

Purchase again?	Installment credit		Mortgage credit	
	2001	2012	2001	2012
Yes	94.2	74.6	71.0	71.2
No	5.8	24.4	24.2	28.0
Do not know/refuse	*	1.0	4.8	0.8
Total	**100.0**	**100.0**	**100.0**	**100.0**

* Less than ½ of 1 percent.

Table 7. Life insurance holding among families in 2010
Percent

Life insurance amount	Proportion of families	Median income of families	Proportion of these families with mortgage[1]	Proportion of these families with auto credit[1]
$10,000 or less	37	$ 27,000	30	20
$10,001 to $100,000	33	$ 40,000	39	28
$100,001 to $500,000	21	$ 74,000	65	43
$500,001 or more	8	$141,000	80	39
Total	**100**			

[1] Proportion of families with this amount of life insurance who have credit of this type outstanding.
Source: 2010 Survey of Consumer Finances.

gage loan outstanding and 20 percent had automobile credit. Median family income of this group was $27,000 (table 7). Another 33 percent of families had relatively small amounts of life insurance ($10,001 to $100,000) but 39 percent had a mortgage and 28 percent had auto credit. Median family income of this group was $40,000. It seems likely that many consumers entering into credit arrangements may well feel that their underinsured condition leaves them and their families vulnerable to unfortunate life events. The purchase of debt protection to cover this loan may provide protection against allowing this loan to add to potential future dislocation, even if it is not a comprehensive insurance or financial planning solution.

Conclusion

In sum, nationwide consumer survey results indicate that sales penetration of debt protection products has fallen over recent decades. It appears that at least part of this trend arises from the declining promotion of these products at the closing of loans. In contrast, consumer attitudes among purchasers have not changed from the high levels of favorable views of users in the past. Purchasers have always been favorably inclined to these products and the recent survey shows that they remain so. Attitudes of purchasers are relatively more favorable than among nonpurchasers, which likely at least partly explains why one group of consumers purchases and the other does not, but even many nonpurchasers remain favorably inclined toward these products.

It seems that the marketplace offers consumers a choice concerning the purchase of debt protection products and consumers exercise that choice as part of their financial decisions about borrowing. While there may be abusive practices among some lenders who operate outside the realm of ethical behavior with respect to the sale of debt protection products, survey evidence suggests that, in the views of consumers, such behavior is not the norm.

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Legal Developments: Fourth Quarter, 2011

Orders Issued Under Bank Holding Company Act

Orders Issued Under Section 3 of the Bank Holding Company Act

Banco do Brasil, S.A.
Brasilia, Brazil

Caixa de Previdência dos Funcionarios do Banco do Brasil
Rio de Janiero, Brazil

Order Approving the Acquisition of a Bank

Banco do Brasil, S.A. ("Banco do Brasil"), Brasilia, and Caixa de Previdência dos Funcionarios do Banco do Brasil ("Previ"), Rio de Janiero, both of Brazil (together, "Applicants"), have requested the Board's approval under section 3 of the Bank Holding Company Act of 1956, as amended ("BHC Act"),[1] to acquire EuroBank, Coral Gables, Florida ("EuroBank").

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published (76 *Federal Register* 36923 (2011)). The time for filing comments has expired, and the Board has considered the proposal and all comments received in light of the factors set forth in section 3 of the BHC Act.

Banco do Brasil, with total consolidated assets equivalent to $520.1 billion, is the largest banking organization in Brazil based on asset size.[2] Banco do Brasil also operates branches in New York, New York, and Miami, Florida; maintains representative offices in Washington, D.C., Orlando, Florida, and White Plains, New York; and wholly owns indirectly BB Money Transfers, Inc., a licensed money transmitter operating in 14 states. Banco do Brasil also maintains a securities broker-dealer subsidiary in New York, New York, Banco do Brasil Securities LLC, and owns 50 percent of the shares of Banco Votorantim, a Brazilian bank that owns a securities broker-dealer subsidiary in New York, New York, Banco Votorantim Securities, Inc.

Banco do Brasil is and would remain a qualifying foreign banking organization under the Board's Regulation K and is treated as a financial holding company under section 4(*l*) of the BHC Act. The Brazilian government owns approximately 59.1 percent of Banco do

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[1] 12 U.S.C. § 1842.

[2] Asset and ranking data are as of September 30, 2011, and are based on the exchange rate as of that date.

Brasil's shares.[3] Previ, the pension plan for Banco do Brasil employees, owns approximately 10.4 percent of Banco do Brasil's shares.[4]

EuroBank, with total consolidated assets of $83 million operates only in Florida and is the 245th largest depository organization in Florida, controlling deposits of approximately $81 million (less than 1 percent of deposits in the state).[5] Banco do Brasil does not currently operate an insured depository institution in Florida.

Competitive Considerations

Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or would be in furtherance of an attempt to monopolize the business of banking in any relevant banking market. The BHC Act also prohibits the Board from approving a proposed bank acquisition that would substantially lessen competition in any relevant banking market unless the anticompetitive effects of the proposal are clearly outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the community to be served.[6]

Banco do Brasil does not currently compete with EuroBank in any relevant banking market.[7] Accordingly, the Board concludes, based on all the facts of record, that consummation of the proposal would not have a significantly adverse effect on competition or on the concentration of banking resources in any relevant banking market and that competitive considerations are consistent with approval.

Financial, Managerial, and Other Supervisory Considerations

Section 3 of the BHC Act requires the Board to consider the financial and managerial resources and future prospects of the companies and banks involved in the proposal and certain other supervisory factors. The Board has carefully considered these factors in light of all the facts of record, including confidential supervisory and examination information from the U.S. banking supervisors of the institutions involved, and publicly reported and other financial information, including information provided by Applicants. In addition, the Board has consulted with Banco Central do Brasil ("BCB"), the agency with primary responsibility for the supervision and regulation of Brazilian banking organizations, including Banco do Brasil. The Board also has consulted with the Federal Deposit Insurance Corporation ("FDIC") and the Florida Office of Financial Regulation ("FOFR"), the federal and state agencies, respectively, with primary responsibility for the supervision and regulation of EuroBank.

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3 Banco do Brasil share ownership data are as of June 30, 2011.

4 Previ is a subsidiary of Banco do Brasil for purposes of the BHC Act because Banco do Brasil selects three of the six Previ directors; a Banco do Brasil appointee on the Previ board is granted tie-breaking voting power; and Banco do Brasil selects three of the six Previ executive board members (and each Previ executive board decision must be approved by at least one Banco do Brasil appointee). Previ is considered to be a parent of Banco do Brasil by virtue of its share ownership in Banco do Brasil and its disproportionate voting power to elect three of the seven directors on the Banco do Brasil board. Consequently, Previ has also applied for approval to acquire EuroBank. Previ is and would remain subject to all activity restrictions applicable to qualifying foreign banking organizations.

5 Asset data are as of September 30, 2011. Statewide deposit and ranking data are as of June 30, 2010.

6 12 U.S.C. § 1842(c)(1).

7 Banco do Brasil operates a branch office in the Miami banking market that does not offer insured deposits. On consummation of the proposal, Banco do Brasil's home state under the BHC Act would be Florida.

In evaluating the financial factors in proposals involving banking organizations, the Board reviews the financial condition of the applicants and the target depository institution.[8] In assessing financial resources, the Board consistently has considered capital adequacy to be especially important. The Board also evaluates the financial condition of the combined organization, including its capital position, asset quality, and earnings prospects, and the impact of the proposed funding of the transaction.

The Board has carefully considered the financial resources of the organizations involved in the proposal. The capital levels of Banco do Brasil exceed the minimum levels that would be required under the Basel Capital Accord and are considered to be equivalent to the capital levels that would be required of a U.S. banking organization seeking to acquire EuroBank. The proposed transaction is structured as a cash purchase of shares. Banco do Brasil would use existing resources to fund the purchase of shares. In light of the relative size of Banco do Brasil in relation to EuroBank, the transaction would have a minimal impact on Banco do Brasil's financial condition. Banco do Brasil has been profitable and would inject additional capital into EuroBank, causing EuroBank to be well capitalized. Based on its review of the record, the Board finds that Applicants have sufficient financial resources to effect the proposal.

The Board also has considered the managerial resources of the organizations involved and the proposed combined organization. The Board has reviewed the examination records of Banco do Brasil's U.S. operations and of EuroBank. In addition, the Board has considered its supervisory experience and that of other relevant banking supervisory agencies with the organizations and their records of compliance with applicable banking and anti-money-laundering laws. As noted, the Board has consulted with the BCB. The Board also has considered Banco do Brasil's plans for implementing the acquisition, including the proposed management after consummation.

Section 3 of the BHC Act provides that the Board may not approve an application involving a foreign bank unless the bank is subject to comprehensive supervision or regulation on a consolidated basis by the appropriate authorities in the bank's home country.[9] As noted, the BCB is the primary supervisor of Brazilian banks, including Banco do Brasil. The Board previously has determined that Banco do Brasil is subject to comprehensive supervision on a consolidated basis by its home country supervisor.[10] Banco do Brasil continues to be supervised by the BCB on substantially the same terms and conditions. Based on this finding and all the facts of record, including consultation with the BCB, the Board has concluded that Banco do Brasil continues to be subject to comprehensive supervision on a consolidated basis by its home country supervisor.

[8] A commenter expressed concerns about EuroBank's financial condition and management, including concerns based on a Notice of Charges and of Hearing issued by the FDIC on May 3, 2011. The Board has reviewed the financial and managerial factors in this proposal, including those comments, in the context of the financial and managerial condition of Applicants and the resulting organization. Moreover, as noted above, the Board has consulted with the FDIC and the FOFR.

[9] 12 U.S.C. § 1842(c)(3)(B). As provided in Regulation Y, the Board determines whether a foreign bank is subject to consolidated home country supervision under the standards set forth in Regulation K. *See* 12 CFR 225.13(a)(4). In assessing this standard under section 211.24 of Regulation K, the Board considers, among other indicia of comprehensive, consolidated supervision, the extent to which the home country supervisors: (i) ensure that the bank has adequate procedures for monitoring and controlling its activities worldwide; (ii) obtain information on the condition of the bank and its subsidiaries and offices through regular examination reports, audit reports, or otherwise; (iii) obtain information on the dealings with and relationship between the bank and its affiliates, both foreign and domestic; (iv) receive from the bank financial reports that are consolidated on a worldwide basis or comparable information that permits analysis of the bank's financial condition on a worldwide consolidated basis; (v) evaluate prudential standards, such as capital adequacy and risk asset exposure, on a worldwide basis. No single factor is essential, and other elements may inform the Board's determination.

[10] *See* Board letter to Kathleen A. Scott, Esq. dated April 13, 2010.

In evaluating this proposal, the Board also considered whether Previ is subject to comprehensive supervision or regulation on a consolidated basis by the appropriate authorities in its home country. The Board has previously determined that the system of comprehensive supervision or regulation of a company may vary, depending on the nature of the acquiring company and the proposed investment.[11] The Board believes that Previ may be found to be subject to an appropriate type and level of comprehensive regulation on a consolidated basis, given its nature, and structure, and the fact that Banco do Brasil would exercise effective control over and manage the operations of EuroBank. Previ is the pension plan for Banco do Brasil employees and, as such, is subject to regulation by the Superintendência Nacional de Previdência Complementar, the supervisor of pension funds in Brazil ("PREVIC"), and Comissão de Valores Mobiliários, the securities and exchange commission of Brazil ("CVM"). PREVIC and CVM conduct annual and periodic inspections of Previ, respectively, and require Previ to submit reports about its operations. Specifically, Previ files reports with PREVIC concerning its investments, benefits provided, actions taken to prevent and combat money laundering and concealment of assets, internal controls, and updates on new statutes and regulations applicable to Previ. Based on all the facts of record, the Board has determined that Previ is subject to comprehensive supervision on a consolidated basis by its appropriate home country authorities for purposes of this application.

Section 3 of the BHC Act also requires the Board to take into consideration the extent to which the proposed acquisition would result in greater or more concentrated risk to the stability of the U.S. banking or financial system.[12] The Board has carefully considered the proposal's potential impacts under the financial stability factor. Based on its review of the record, including consideration of the small size and scope of the operations of EuroBank, the Board finds that the proposed acquisition would not result in greater or more concentrated risk to the stability of the U.S. banking or financial system.

Based on all the facts of record, the Board has concluded that considerations relating to the financial and managerial resources and future prospects of the organizations involved in the proposal are consistent with approval, as are the other supervisory factors under the BHC Act.[13]

Convenience and Needs Considerations

In acting on a proposal under section 3 of the BHC Act, the Board is required to consider the effects of the proposal on the convenience and needs of the communities to be served and to take into account the records of the relevant insured depository institutions under

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[11] *See Chuo Mitsui Trust Holdings, Inc.*, 97 *Federal Reserve Bulletin* 30 (2011); *China Investment Corporation*, 96 *Federal Reserve Bulletin* B31 (2010).

[12] 12 U.S.C. § 1842(c)(7), *as added by* section 604(d) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111-203, 124 Stat. 1376.

[13] Section 3 of the BHC Act also requires the Board to determine that an applicant has provided adequate assurances that it will make available to the Board such information on its operations and activities and those of its affiliates that the Board deems appropriate to determine and enforce compliance with the BHC Act. 12 U.S.C. § 1842(c)(3)(A). The Board has reviewed the restrictions on disclosure in the relevant jurisdictions in which Banco do Brasil operates and has communicated with relevant government authorities concerning access to information. In addition, Banco do Brasil has committed that, to the extent not prohibited by applicable law, it will make available to the Board such information on the operations of its affiliates that the Board deems necessary to determine and enforce compliance with the BHC Act, the International Banking Act, and other applicable federal laws. Banco do Brasil also has committed to cooperate with the Board to obtain any waivers or exemptions that may be necessary to enable its affiliates to make such information available to the Board. Based on all facts of record, including the conditions in this order, the Board has concluded that Banco do Brasil has provided adequate assurances of access to any appropriate information the Board may request.

the Community Reinvestment Act ("CRA").[14] 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, 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 neighborhoods, in evaluating bank expansionary proposals.[15]

The Board has considered carefully all the facts of record, including evaluations of the CRA performance record of EuroBank,[16] data reported by EuroBank under the Home Mortgage Disclosure Act ("HMDA"),[17] other information provided by Applicants, confidential supervisory information, and public comment received on the proposal. The commenter alleged that EuroBank had engaged in disparate treatment of African American individuals in home mortgage lending.

A. CRA Performance Evaluations

As provided in the CRA, the Board has reviewed the convenience and needs factor in light of the evaluations by the appropriate federal supervisors of the relevant insured depository institution's CRA performance records. 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.[18]

EuroBank received a "Satisfactory" rating at its most recent CRA performance evaluation by the FDIC, as of March 17, 2009. The Board also has consulted with the FDIC regarding the activities of EuroBank since the 2009 CRA performance evaluation.

B. HMDA and Fair Lending Records

The Board has carefully considered the HMDA data for 2009 and 2010 reported by EuroBank in its assessment area and in the Miami metropolitan statistical area of concern to the commenter and has also considered the fair lending records of EuroBank, in light of public comment received on the proposal. Commenter alleged, based on HMDA data reported in 2009, that EuroBank had engaged in disparate treatment of African American individuals in home mortgage lending.

Although the HMDA data might reflect certain disparities in the rates of loan applications, originations, and denials among members of different racial or ethnic groups in certain local areas, they provide an insufficient basis by themselves on which to conclude whether or not EuroBank is excluding or imposing higher costs on any group on a prohibited basis. The Board recognizes that HMDA data alone, even with the recent addition of pricing information, provide only limited information about the covered loans.[19] HMDA data,

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[14] 12 U.S.C. § 2901 *et seq.*; 12 U.S.C. § 1842(c)(2).

[15] 12 U.S.C. § 2903.

[16] Banco do Brasil currently does not operate an insured depository institution in the United States. Accordingly, Banco do Brasil's U.S. operations are not subject to performance evaluations under the CRA.

[17] 12 U.S.C. § 2801 *et seq.*

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

[19] 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 whether an applicant who was denied credit was, in fact, creditworthy. In

therefore, have limitations that make them an inadequate basis, absent other information, for concluding that an institution has engaged in illegal lending discrimination.

The Board is nevertheless concerned when HMDA data for an institution indicate disparities in lending and believes that all lending institutions are obligated to ensure that their lending practices are based on criteria that ensure not only safe and sound lending but also equal access to credit by creditworthy applicants, regardless of their race or ethnicity. Because of the limitations of HMDA data, the Board has considered these data carefully and taken into account other information, including examination reports that provide on-site evaluations of compliance with fair lending laws by EuroBank.

The record of this proposal, including confidential supervisory information, indicates that EuroBank has taken steps to ensure compliance with fair lending and other consumer protection laws. EuroBank has in place a formal fair lending policy and program that includes its home mortgage and small business lending operations. EuroBank also provides internal compliance training, and the bank's staffs in bank management, line-of-business, and compliance attend outside conferences and seminars and other fair lending and consumer protection training sessions. Banco do Brasil has indicated that the combined institution would continue to have such policies and procedures on consummation of the proposal.

The Board also has considered the HMDA data in light of other information, including the overall performance record of EuroBank under the CRA. EuroBank's established efforts and records of performance demonstrate that the institution is not excluding individuals or geographies on a prohibited basis, contrary to the allegations of the commenter.[20] In fact, in the fair lending review conducted at the most recent CRA examination of EuroBank, the FDIC found no evidence of illegal credit discrimination. Moreover, the FDIC determined in the 2009 examination that the geographic distribution of the bank's small business loans reflected a strong performance in the assessment area.

C. Conclusion on Convenience and Needs and CRA Performance

The Board has considered carefully all the facts of record, including reports of examination of the CRA records of the institutions involved, information provided by Applicants, the public comment received on the proposal, and confidential supervisory information. Applicants represent that the proposal would result in increased credit availability and access to a broader array of financial products and services for customers of the combined organization. Based on a review of the entire record, and for the reasons discussed above, the Board concludes that considerations relating to the convenience and needs factor and the CRA performance records of the relevant insured depository institutions are consistent with approval of the proposal.

addition, credit history problems, excessive debt levels relative to income, and high loan amounts relative to the value of the real estate collateral (reasons most frequently cited for a credit denial or higher credit cost) are not available from HMDA data.

[20] Banco do Brasil has represented that EuroBank does not engage in extensive marketing of consumer credit products and that EuroBank's loans consist largely of commercial loans, including small business loans. As a result, EuroBank received a small number of HMDA-reportable loan applications, including applications from minority individuals, and made a small number of HMDA-reportable loans. The application and lending volumes were too small to draw any statistically significant conclusions.

Conclusion

Based on the foregoing, and in light of all the facts of record, the Board has determined that the application should be, and hereby is, approved.[21] In reaching its conclusion, the Board has considered all the facts of record in light of the factors that it is required to consider under the BHC Act and other applicable statutes.[22] Should any restrictions on access to information on the operations or activities of Banco do Brasil or any of its affiliates subsequently interfere with the Board's ability to obtain information to determine and enforce compliance by Banco do Brasil or its affiliates with applicable federal statutes, the Board may require termination of any of .Banco do Brasil's or its affiliates' direct or indirect activities in the United States. The Board's approval is specifically conditioned on compliance by Applicants with the conditions in this order and all the commitments made to the Board in connection with the proposal. For purposes of this action, these commitments and conditions are deemed to be conditions imposed in writing by the Board in connection with its findings and decision 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 by the Federal Reserve Bank of New York, acting pursuant to delegated authority.

By order of the Board of Governors, effective December 16, 2011.

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

Robert deV. Frierson
Deputy Secretary of the Board

Brookline Bancorp, Inc.
Brookline, Massachusetts

Order Approving the Acquisition of a Bank Holding Company

Brookline Bancorp, Inc. ("Brookline"), Brookline, Massachusetts, has requested the Board's approval under section 3 of the Bank Holding Company Act ("BHC Act")[1] to acquire Bancorp Rhode Island, Inc. ("BancorpRI") and its subsidiary bank, Bank Rhode Island ("BankRI"), both of Providence, Rhode Island.

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21 Commenter requested that the Board hold a public hearing on the proposal. Section 3(b) of the BHC Act does not require the Board to hold a public hearing on an application unless the appropriate supervisory authorities for the bank to be acquired make a timely written recommendation of denial of the application. 12 CFR 225.16(e). The Board has not received such a recommendation from the appropriate supervisory authorities. Under its regulations, the Board also may, in its discretion, hold a public hearing on an application to acquire a bank if necessary or appropriate to clarify factual issues related to the application and to provide an opportunity for testimony. 12 CFR 262.3(e) and 262.25(d). The Board has considered carefully the commenter's request in light of all the facts of record. In the Board's view, the commenter had ample opportunity to submit views and, in fact, submitted written comments that the Board has considered carefully in acting on the proposal. The request fails to identify disputed issues of fact that are material to the Board's decision that would be clarified by a public hearing. For these reasons, and based on all the facts of record, the Board has determined that a public hearing or meeting is not required or warranted in this case. Accordingly, the request for a public hearing on the proposal is denied.

22 The commenter also alleged that Banco do Brasil is funding environmentally harmful projects in Brazil. The comments concern matters that are beyond the statutory factors the Board is authorized to consider. *See Western Bancshares, Inc. v. Board of Governors*, 480 F.2d 749 (10th Cir. 1973).

1 12 U.S.C. § 1842.

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published (76 *Federal Register* 35893 (2011)). The time for filing comments has expired, and the Board has considered the application and all comments received in light of the factors set forth in section 3 of the BHC Act.

Brookline, with total consolidated assets of approximately $3.1 billion, is the 227th largest insured depository organization in the United States, controlling $2.2 billion in deposits.[2] Brookline controls two subsidiary insured depository institutions, Brookline Bank, Brookline, and The First National Bank of Ipswich ("FNBI"), Ipswich, both of Massachusetts, that operate only in Massachusetts. Brookline is the 15th largest depository organization in Massachusetts, controlling deposits of approximately $1.7 billion, which represent less than 1 percent of the total amount of deposits of insured depository institutions in the state.

BancorpRI, with total consolidated assets of $1.6 billion, controls BankRI, which operates only in Rhode Island. BankRI is the sixth largest insured depository institution in Rhode Island, controlling deposits of $1.1 billion.

On consummation of the proposal, Brookline would become the 165th largest depository organization in the United States, with total consolidated assets of approximately $4.7 billion. Brookline would control deposits of approximately $3.3 billion, which represent less than 1 percent of the total amount of deposits of insured depository institutions in the United States.

Interstate Analysis

Section 3(d) of the BHC Act allows the Board to approve an application by a bank holding company to acquire control of a bank located in a state other than the bank holding company's home state if certain conditions are met. For purposes of the BHC Act, the home state of Brookline is Massachusetts,[3] and BancorpRI is located in Rhode Island.[4]

Based on a review of all the facts of record, including relevant state statutes, the Board finds that the conditions for an interstate acquisition enumerated in section 3(d) are met in this case.[5] In light of all facts of record, the Board is permitted to approve the proposal under section 3(d) of the BHC Act.

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[2] Deposit data are as of June 30, 2011, updated to reflect mergers through that date. In this context, insured depository institutions include commercial banks, savings associations, and savings banks. National deposit data and rankings are as of June 30, 2011.

[3] *See* 12 U.S.C. § 1842(d). 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.

[4] For purposes of section 3(d) of the BHC Act, the Board considers a bank to be located in the states in which the bank is chartered or headquartered or operates a branch. *See* 12 U.S.C. §§ 1841(o)(4)–(7) and 1842(d)(1)(A) and 1842(d)(2)(B).

[5] 12 U.S.C. §§ 1842(d)(1)(A)–(B) and 1842(d)(2)–(3). Brookline is well capitalized and well managed, as defined by applicable law. BankRI has been in existence and operated for the minimum period of time required by Rhode Island law and for more than five years. *See* 12 U.S.C. § 1842(d)(1)(B)(i)–(ii). On consummation of the proposal, Brookline would control less than 10 percent of the total amount of deposits of insured depository institutions in the United States. 12 U.S.C. § 1842(d)(2)(A). Brookline also would control less than 30 percent of the total amount of deposits in insured depository institutions in Rhode Island. 12 U.S.C. § 1842(d)(2)(B)–(D). All other requirements of section 3(d) of the BHC Act would be met on consummation of the proposal.

Competitive Considerations

Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or would be in furtherance of any attempt to monopolize the business of banking in any relevant banking market. The BHC Act also prohibits the Board from approving a proposed bank acquisition that would substantially lessen competition in any relevant banking market unless the anticompetitive effects of the proposal are clearly outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the community to be served.[6]

Brookline and BancorpRI do not compete directly in any relevant banking market. Based on all the facts of record, the Board has concluded that consummation of the proposal would not have a significantly adverse effect on competition or on the concentration of banking resources in any relevant banking market and that competitive factors are consistent with approval of the proposal.

Financial, Managerial, and Other Supervisory Considerations

Section 3 of the BHC Act requires the Board to consider the financial and managerial resources and future prospects of the companies and banks involved in the proposal and certain other supervisory factors.[7] The Board has carefully considered those factors in light of all the facts of record, including confidential supervisory and examination information received from the relevant federal and state supervisors of the organizations involved in the proposal, other publicly available financial information, information provided by Brookline, and public comment received on the proposal.

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

The Board has considered the proposal carefully under the financial factors. Brookline, Brookline Bank, BancorpRI, and BankRI are well capitalized and will remain so on consummation of the proposal. FNBI is adequately capitalized and also will remain so on consummation of the proposal. The proposed transaction is structured as a partial share exchange and a partial cash purchase of shares. Brookline will fund the cash portion of the acquisition from a special dividend from Brookline Bank, which the Office of the Comptroller of the Currency ("OCC") has approved. Based on its review of the record, the Board finds that Brookline has sufficient financial resources to effect the proposal.

The Board also has considered the managerial resources of the organizations involved and of the proposed combined organization. The Board has reviewed the examination records of Brookline, BancorpRI, and their subsidiary depository institutions, including assessments of their management, risk-management systems, and operations. In addition, the Board has considered its supervisory experiences and those of other relevant bank supervi-

[6] 12 U.S.C. § 1842(c)(1).

[7] 12 U.S.C. § 1842(c)(2) and (3).

sory agencies with the organizations and their records of compliance with applicable banking and anti-money-laundering laws. Brookline and its subsidiary depository institutions are considered to be well managed. The Board has carefully considered the comment it received on the proposal.[8] The Board also has considered Brookline's plans for implementing the proposal, including the proposed management after consummation. In addition, the Board has considered the future prospects of the organizations involved in the proposal in light of financial and managerial resources and Brookline's proposed business plan.

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

Convenience and Needs Considerations and Financial Stability

In acting on a proposal under section 3 of the BHC Act, the Board must consider the effects of the proposal on the convenience and needs of the communities to be served and take into account the records of the relevant depository institutions under the Community Reinvestment Act ("CRA").[9] 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 neighborhoods, in evaluating bank acquisition proposals. Accordingly, the Board has carefully considered the convenience and needs factor and the CRA performance records of Brookline Bank, FNBI, and BankRI 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 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.[10] Brookline Bank, FNBI, and BankRI received "satisfactory" ratings at their most recent examinations for CRA performance by the Office of Thrift Supervision, the OCC, and the Federal Deposit Insurance Corporation, as of November 3, 2008, June 2, 2008, and June 25, 2010, respectively. Moreover, the facts of record do not reflect a subsequent decline in the CRA performance of any of the three institutions since those examinations.

[8] A commenter alleged that management of Brookline Bank is deficient because the bank used commenter's material regarding reverse mortgages in violation of copyright and trademark law. The commenter also alleged that Brookline Bank has not provided reverse mortgage candidates with counseling in violation of state law. Brookline represented that it was not subject to state approval requirements for reverse mortgage loan programs, has not made reverse mortgage loans since 2009, and has no plans to resume originating reverse mortgage loans. Brookline Bank also has replaced its chief executive officer, hired a full-time compliance officer, and added compliance staff since 2009, which should strengthen its monitoring procedures and compliance audit process. Moreover, Brookline noted that with the assistance of an independent compliance company, it is reviewing all relevant loans and will remedy any identified compliance issues to ensure that none of the borrowers has been or will be overcharged because of inadequate disclosure. In evaluating the financial and managerial factors that the Board must consider under section 3 of the BHC Act, the Board has considered these and other facts of record with respect to litigation involving the copyright and trademark matters, information provided by Brookline regarding its reverse mortgage loans, and confidential supervisory information, including records of compliance with consumer laws and regulations.

[9] 12 U.S.C. §§ 2901 *et seq.*; 12 U.S.C. § 1842(c)(2).

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

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.

The Board has also carefully considered information relevant to risks to the stability of the United States banking or financial system. The Board concludes that financial stability considerations in this proposal are consistent with approval.

Conclusion

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

The proposed transaction 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 Boston, acting pursuant to delegated authority.

By order of the Board of Governors, effective December 9, 2011.

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

Robert deV. Frierson
Deputy Secretary of the Board

Goering Management Company, LLC
Moundridge, Kansas

Goering Financial Holding Company Partnership, L.P.
Moundridge, Kansas

Bon, Inc.
Moundridge, Kansas

Order Approving the Acquisition of a Bank Holding Company

Goering Management Company, LLC ("Goering Management") and its subsidiaries, Goering Financial Holding Company Partnership, L.P. ("Goering Financial") and Bon, Inc. (collectively, "Bon"), all of Moundridge,[1] have requested the Board's approval under

1 Goering Management, Goering Financial, and Bon are bank holding companies under the BHC Act that have made effective elections to be financial holding companies. Goering Management and Goering Financial are bank holding companies because they control Bon, Inc., a bank holding company that directly controls one bank, The Citizens State Bank, also of Moundridge.

section 3 of the Bank Holding Company Act ("BHC Act")[2] to acquire Home State Bancshares, Inc.Home State Bancshares, Inc. ("Home State") and its subsidiary bank, Home State Bank & Trust Company ("Home State Bank"), both of McPherson, all of Kansas.

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published (76 *Federal Register* 56760 (2011)). The time for filing comments has expired, and the Board has considered the application and all comments received in light of the factors set forth in section 3 of the BHC Act.

Bon, with total consolidated assets of approximately $265 million, is the 2612th largest insured depository organization in the United States.[3] Bon's subsidiary bank, The Citizens State Bank, operates only in Kansas. Bon is the 57th largest insured depository organization in Kansas, controlling deposits of approximately $218.3 million, which represent less than 1 percent of the total amount of deposits of insured depository institutions in the state.

Home State, with total consolidated assets of $133 million, controls Home State Bank, which also operates only in Kansas. Home State Bank is the 110th largest insured depository institution in Kansas, controlling deposits of $105.4 million, which represent less than 1 percent of the total amount of deposits of insured depository institutions in the state.

On consummation of the proposal, Bon would become the 1754th largest insured depository organization in the United States, with total consolidated assets of approximately $398 million. Bon would control deposits of approximately $323.7 million, which represent less than 1 percent of the total amount of deposits of insured depository institutions in the United States. In Kansas, Bon would become the 38th largest depository organization and control less than 1 percent of deposits of insured depository institutions in the state.

Competitive Considerations

Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or would be in furtherance of any attempt to monopolize the business of banking in any relevant banking market. The BHC Act also prohibits the Board from approving a proposed bank acquisition that would substantially lessen competition in any relevant banking market unless the anticompetitive effects of the proposal are clearly outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the community to be served.[4]

The Citizens State Bank and Home State Bank compete directly in the McPherson, Kansas banking market.[5] The Board has reviewed carefully the competitive effects of the proposal in this banking market in light of all the facts of record. In particular, the Board has considered the number of competitors that would remain in the banking market, the relative shares of total deposits in depository institutions in the market ("market deposits") controlled by Bon and Home State,[6] the concentration levels of market deposits and the increase in those levels as measured by the Herfindahl-Hirschman Index ("HHI") under

2 12 U.S.C. § 1842.

3 Asset data are as of September 30, 2011. Deposit data are as of June 30, 2011. In this context, insured depository institutions include commercial banks, savings associations, and savings banks.

4 12 U.S.C. § 1842(c)(1).

5 The McPherson market is defined as McPherson County and the towns of Crawford, Little River, and Mitchell in Rice County, all in Kansas.

6 Deposit and market share data are as of June 30, 2011.

the Department of Justice Bank Merger Competitive Review guidelines ("DOJ Guidelines"),[7] and other characteristics of the market.

The structural effects that consummation of the proposal would have on the McPherson banking market warrant a detailed review because the concentration level on consummation would exceed the threshold levels in the DOJ Guidelines. The Citizens State Bank is the second largest insured depository institution in the McPherson banking market, controlling deposits of approximately $113.2 million, which represent approximately 16.2 percent of the market deposits. Home State Bank is the third largest insured depository institution in the McPherson banking market, controlling deposits of approximately $105.4 million, which represent approximately 15.1 percent of the market deposits. On consummation, the HHI in this market would increase by 489 points, from 1577 to 2066, and The Citizens State Bank would become the largest banking firm in the market with a pro forma share of market deposits of approximately 31.3 percent.

The Board has considered carefully whether other factors either mitigate the competitive effects of the proposal or indicate that the proposal would have a significantly adverse effect on competition in the McPherson banking market.[8] Several factors indicate that the increase in concentration in the McPherson banking market, as measured by the HHI and share of market deposits, overstates the potential competitive effects of the proposal in the market. After consummation of the proposal, 12 other commercial bank competitors would remain, some with a significant presence in the market. The second largest bank competitor in the market would closely approximate the size of Bon on consummation, controlling about 29.5 percent of market deposits. Another bank competitor would control more than 10 percent of market deposits. In addition, the market deposits of six other bank competitors in the market have recently increased at a rate well above the growth rate of market deposits for Bon or Home State.[9]

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

Based on these and other facts of record, the Board has concluded that consummation of the proposal would not have a significantly adverse effect on competition or on the concentration of resources in any relevant banking market. Accordingly, based on all the facts of record, the Board has determined that competitive considerations are consistent with approval.

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[7] Under the DOJ 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 recently issued revised Horizontal Merger Guidelines, the DOJ has confirmed that its guidelines for bank mergers or acquisitions, which were issued in 1995, were not changed. Press Release, Department of Justice (August 19, 2010), available at www.justice.gov/opa/pr/2010/August/10-at-938.html.

[8] 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).

[9] From 2005 to 2010, the market deposits of six banks with market shares smaller than Bon and Home State increased at rates ranging from 28 percent to 113 percent. During the same time period, the market deposits of Bon and Home State increased by 15 percent and 19 percent, respectively.

Financial, Managerial, and Other Supervisory Considerations

Section 3 of the BHC Act requires the Board to consider the financial and managerial resources and future prospects of the companies and banks involved in the proposal and certain other supervisory factors.[10] The Board has carefully considered these factors in light of all the facts of record, including supervisory and examination information received from the relevant federal and state supervisors of the organizations involved in the proposal, and other available financial information, including information provided by Bon.

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

The Board has considered the proposal carefully under the financial factors. Bon, Home State, and their subsidiary depository institutions are well capitalized and would remain so on consummation of the proposal. The proposed transaction is structured as a cash purchase of shares. Bon will use existing cash resources and the proceeds of a new debt issuance to fund the purchase. Based on its review of the record, the Board finds that Bon has sufficient financial resources to effect the proposal.

The Board also has considered the managerial resources of the organizations involved and of the proposed combined organization. The Board has reviewed the examination records of Bon, Home State, and their subsidiary depository institutions, including assessments of their management, risk-management systems, and operations. In addition, the Board has considered its supervisory experiences and those of the other relevant bank supervisory agencies with the organizations and their records of compliance with applicable banking law, including anti-money-laundering laws. Bon and its subsidiary depository institution are considered to be well managed. The Board also has considered Bon's plans for implementing the proposal, including the proposed management after consummation of the proposal. In addition, the Board has considered the future prospects of the organizations involved in the proposal in light of the financial and managerial resources and the proposed business plan.

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

Convenience and Needs Considerations and Financial Stability

In acting on a proposal under section 3 of the BHC Act, the Board must consider the effects of the proposal on the convenience and needs of the communities to be served and take into account the records of the relevant depository institutions under the Community Reinvestment Act ("CRA").[11] The CRA requires the federal financial supervisory agencies

[10] 12 U.S.C. § 1842(c)(2) and (3).

[11] 12 U.S.C. § 2901 *et seq*.; 12 U.S.C. § 1842(c)(2).

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 neighborhoods, in evaluating bank acquisition proposals. Accordingly, the Board has carefully considered the convenience and needs factor and the CRA performance records of The Citizens State Bank and Home State Bank 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 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.[12] The Citizens State Bank and Home State Bank received "satisfactory" ratings at their most recent examinations for CRA performance by the Federal Deposit Insurance Corporation as of November 3, 2008, and January 11, 2010, respectively.

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

The Board has also carefully considered information relevant to risks to the stability of the United States banking or financial system. The Board concludes that financial stability considerations in this proposal are consistent with approval.

Conclusion

Based on the foregoing and all the facts of record, the Board has determined that the application under section 3 of the BHC Act should be, and hereby is, approved. In reaching its conclusion, the Board has considered all the facts of record in light of the factors that it is required to consider under the BHC Act. The Board's approval is specifically conditioned on compliance by Bon with all the conditions imposed in this order and all the commitments made to the Board in connection with the application and on receipt of all other required regulatory approvals for the proposal. These conditions and commitments are deemed to be conditions imposed in writing by the Board in connection with its findings and decision 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 Kansas City, acting pursuant to delegated authority.

By order of the Board of Governors, effective November 28, 2011.

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

Robert deV. Frierson
Deputy Secretary of the Board

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

The PNC Financial Services Group, Inc.
Pittsburgh, Pennsylvania

PNC Bancorp, Inc.
Wilmington, Delaware

Order Approving Acquisition of a State Member Bank

The PNC Financial Services Group, Inc., a financial holding company within the meaning of the Bank Holding Company Act ("BHC Act"), and its wholly owned subsidiary, PNC Bancorp, Inc., a bank holding company within the meaning of the BHC Act (jointly, "PNC"), have requested the Board's approval under section 3 of the BHC Act[1] to acquire RBC Bank (USA), Raleigh, North Carolina ("RBC Bank"), a state member bank, from RBC USA Holdco Corporation, a wholly owned subsidiary of the Royal Bank of Canada.[2]

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published (76 *Federal Register* 50480 (2011)). The time for filing comments has expired, and the Board has considered the proposal and all comments received in light of the factors set forth in section 3 of the BHC Act.

PNC, with total consolidated assets of approximately $263 billion as of June 30, 2011, is the seventh largest depository organization in the United States, controlling deposits of approximately $180 billion, which represent approximately 2 percent of the total amount of deposits of insured depository institutions in the United States. PNC Bank operates in sixteen states and the District of Columbia[3] and engages in numerous nonbanking activities that are permissible under the BHC Act.[4] PNC Bank is the largest insured depository organization in Pennsylvania, controlling deposits of approximately $62 billion, which represent 21 percent of the total amount of deposits of insured depository institutions in the state. PNC Bank is the 14th largest insured depository organization in Florida, controlling deposits of approximately $5 billion, and the 82nd largest insured depository institution in Georgia, controlling deposits of $237 million, which represent 1.2 percent and less than 1 percent of the total amount of deposits of insured depository institutions in those states, respectively.

RBC Bank, with total consolidated assets of approximately $27 billion as of June 30, 2011, operates in Alabama, Florida, Georgia, North Carolina, South Carolina, and Virginia. In North Carolina, RBC Bank is the fifth largest depository institution, controlling deposits in the state of approximately $10 billion. RBC Bank is the 20th largest insured depository institution in Florida and the eighth largest insured depository institution in Georgia, controlling deposits of approximately $3 billion in each of those states.

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1 12 U.S.C. § 1842.

2 After the acquisition, PNC plans to merge RBC Bank with and into its only subsidiary depository institution, PNC Bank, National Association, Pittsburgh ("PNC Bank").

3 PNC Bank currently operates branches in Delaware, Florida, Georgia, Illinois, Indiana, Kentucky, Maryland, Michigan, Missouri, New Jersey, New York, Ohio, Pennsylvania, Virginia, West Virginia, Wisconsin, and the District of Columbia. PNC Bank also has limited-purpose branches in Toronto, Canada, and Nassau, The Bahamas.

4 PNC has a 21 percent financial interest in Blackrock, Inc. ("Blackrock"), New York, New York, and holds almost 24 percent of the voting shares of Blackrock. In addition, PNC selects two members of Blackrock's seventeen-member board of directors, and PNC and Blackrock have a number of business relationships. For BHC Act purposes, PNC is considered to control Blackrock. For accounting and financial reporting purposes, PNC treats its interest in Blackrock as an equity investment. Blackrock is a publicly traded company and one of the largest asset managers in the world, with approximately $3.4 trillion in assets under management.

On consummation of the proposal, PNC Bank would become the fifth largest depository organization in the United States, with consolidated deposits of $201 billion, representing approximately 2.2 percent of the total amount of deposits of insured depository institutions in the United States. In Pennsylvania, PNC Bank would remain the largest depository organization, controlling deposits of approximately $62 billion (approximately 21 percent of deposits of insured depository institutions in the state). In Florida, PNC Bank would become the ninth largest depository organization, controlling deposits of approximately $8 billion (approximately 2 percent of deposits of insured depository institutions in the state), and in Georgia, PNC Bank would become the eighth largest depository organization, controlling deposits of approximately $3.1 billion (approximately 1.7 percent of deposits of insured depository institutions in the state).

Interstate and Deposit Cap Analyses

Section 3 of the BHC Act imposes certain requirements on interstate transactions. Section 3(d) generally provides that the Board may approve an application by a bank holding company ("BHC") that is well capitalized and well managed[5] to acquire a bank located in a state other than the home state of the BHC without regard to whether the transaction is prohibited under state law. However, this section further provides that the Board may not approve an application that would permit an out-of-state BHC to acquire a bank in a host state that has not been in existence for the lesser of the state statutory minimum period of time or five years.[6] In addition, the Board may not approve an application by a BHC to acquire an insured depository institution if the home state of such insured depository institution is a state other than the home state of the BHC, 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 ("nationwide deposit cap").[7]

For purposes of the BHC Act, the home state of PNC is Pennsylvania and RBC Bank's home state is North Carolina.[8] PNC is well capitalized and well managed under applicable law. North Carolina law has no minimum age requirement,[9] and RBC Bank has been in existence for more than five years.

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 $8.9 trillion. On consummation of the proposed transaction, PNC would control approximately 2.2 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 proposal under section 3(d) of the BHC Act.

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[5] The standard was changed from adequately capitalized and adequately managed to well capitalized and well managed by section 607(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"), Pub. L. No. 111–203, 124 Stat. 1376, codified at 12 U.S.C. § 1842(d)(1)(A).

[6] 12 U.S.C. § 1842(d)(i)(B).

[7] 12 U.S.C. § 1842(d)(2)(A). For a detailed discussion of the nationwide deposit cap, *see Bank of America Corporation/LaSalle*, 93 *Federal Reserve Bulletin* 109, 109–110 (2007); *Bank of America Corporation/Fleet*, 90 *Federal Reserve Bulletin* 217, 219–220 (2004).

[8] A bank holding company's home state is the state in which the total deposits of all subsidiary banks of the 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 purposes of section 3(d) of the BHC Act, the Board considers a bank to be located in the states in which the bank is chartered or headquartered or operates a branch. 12 U.S.C. §§ 1841(o)(4)–(7), 1842(d)(1)(A), and 1842(d)(2)(B).

[9] *See* N.C.G.S. § 53-224.19 (permitting interstate merger acquisitions but not imposing an age requirement).

Competitive Considerations

Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or would be in furtherance of any attempt to monopolize the business of banking in any relevant banking market. The BHC Act also prohibits the Board from approving a proposal that would substantially lessen competition in any relevant banking market, unless the anticompetitive effects of the proposal are clearly outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the community to be served.[10]

The Board has considered the competitive effects of the proposal in light of all the facts of record. PNC Bank and RBC Bank compete directly in ten local markets: Brevard, Daytona Beach, Fort Pierce, Indian River, Miami-Fort Lauderdale, Naples, Orlando, Tampa Bay, and West Palm Beach, all in Florida; and Atlanta, Georgia. The Board has considered the number of competitors that would remain in the markets, the relative shares of total deposits in depository institutions in the markets controlled by PNC Bank and RBC Bank, the concentration levels of market deposits and the increases in those levels as measured by the Herfindahl-Hirschman Index ("HHI") under the Department of Justice Bank Merger Competitive Review guidelines ("DOJ Guidelines"),[11] and other characteristics of the markets.

Consummation of the proposal would be consistent with Board precedent and within the thresholds in the DOJ Guidelines in each of the ten banking markets. On consummation of the proposal, eight markets would remain moderately concentrated and two markets would remain unconcentrated, as measured by the HHI. Numerous competitors would remain in all ten markets. The change in the HHI's measure of concentration would be less than 100 points in nine of the ten markets. In Indian River, the change in the HHI's measure of concentration would be 184 points, and the post-merger HHI would be 1477, which is within the limits of the DOJ Guidelines.

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

Based on all the facts of record, the Board has concluded that consummation of the proposal would not have a significantly adverse effect on competition or on the concentration of resources in any relevant banking market and that competitive considerations are consistent with approval.

[10] 12 U.S.C. § 1842(c)(1).

[11] Under the DOJ 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 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 DOJ has stated that the higher-than-normal HHI thresholds for screening bank mergers and acquisitions for anticompetitive effects implicitly recognize the competitive effects of limited-purpose and other nondepository financial entities. Although the DOJ and the Federal Trade Commission issued revised Horizontal Merger Guidelines in 2010, the DOJ has confirmed that its guidelines for bank mergers or acquisitions, which were issued in 1995, were not changed. Press Release, Department of Justice (August 19, 2010), available at www.justice.gov/opa/pr/2010/August/10-at-938.html.

Other Section 3(c) Considerations

Section 3(c) of the BHC Act requires the Board to take into consideration a number of other factors in acting on bank acquisition applications. These are: the financial and managerial resources (including consideration of the competence, experience, and integrity of officers, directors, and principal shareholders) and future prospects of the company and banks concerned; effectiveness of the company in combatting money laundering; the convenience and needs of the community to be served; and the extent to which the proposal would result in greater or more concentrated risks to the stability of the United States banking or financial system. The Board has considered all these factors and, as described below, has determined that all considerations are consistent with approval of the application.[12] The review was conducted in light of all the facts of record, including supervisory and examination information from various U.S. banking supervisors of the institutions involved, publicly reported and other financial information, and information provided by PNC.

A. Financial, Managerial, and Other Supervisory Considerations

In evaluating financial factors in expansionary proposals by banking organizations, the Board reviews the financial condition of the organizations involved on both a parent-only and consolidated basis, as well as the financial condition of the subsidiary banks and significant nonbanking operations. In this evaluation, the Board considers a variety of information, including capital adequacy, asset quality, and earnings performance. The Board evaluates the financial condition of the pro forma organization, including its capital position, asset quality, and earnings prospects, and the impact of the proposed funding on the transaction. The Board also considers the ability of the organization to absorb the costs of the proposal and the proposed integration of the operations of the institutions. In assessing financial factors, the Board consistently has considered capital adequacy to be especially important.

The Board has considered the financial factors of the proposal. PNC and PNC Bank are well capitalized and would remain so on consummation of the proposed acquisition. The proposed transaction is structured as a stock purchase of all the shares of RBC Bank (and the related credit card portfolio of RBC's Georgia bank affiliate), for a total payment of $3.6 billion. The purchase would be financed with the proceeds from $1.0 billion of noncumulative preferred stock, $1.25 billion of five-year subordinated debt that was issued in the third quarter of 2011, and other available cash resources. Although capital ratios would decline upon consummation, PNC and PNC Bank would have capital ratios well above the established regulatory minimums. In addition, PNC has been performing capital stress testing since the second quarter of 2009. Under its most recent testing, PNC Bank projected that it would be able to maintain a baseline tier 1 common equity ratio at a level acceptable to the Board. Asset quality and earnings prospects are consistent with approval, and PNC appears to have adequate resources to absorb the costs of the proposal and the proposed integration of the institutions' operations. Based on its review of the record, the Board finds that PNC has sufficient financial resources to effect the proposal.

The Board also has considered the managerial resources of the organizations involved. The Board has reviewed the examination records of PNC, PNC Bank, and RBC Bank, including assessments of their management, risk-management systems, and operations. In addi-

[12] Because each factor under section 3(c) was independently consistent with approval in this case, there was no need for the Board to consider weighing one factor against others. The Board notes that section 4, which deals with acquisitions of nonbanks including insured depository institutions that are not banks, specifically requires a weighing of public benefits against adverse effects.

tion, the Board has considered its supervisory experiences and those of other relevant banking supervisory agencies with the organizations and their records of compliance with applicable banking law, including anti-money-laundering laws.

PNC and PNC Bank are each considered to be well managed. PNC has a demonstrated record of successfully integrating large organizations into its operations and risk-management systems following acquisitions, including its integrations of Riggs National Corporation in 2005, Mercantile Bancshares Corporation in 2007, Sterling Financial Corporation in 2008, and National City Corporation, an institution of roughly equal size to PNC at the time of its acquisition, in 2009. PNC is devoting significant financial and other resources to address all aspects of the post-acquisition integration process for this proposal. PNC would implement its risk-management policies, procedures, and controls at the combined organization that are acceptable from a supervisory perspective. In addition, PNC's management has the experience and resources to ensure that the combined organization operates in a safe and sound manner, and PNC is proposing to integrate RBC Bank's existing management and personnel in a manner that augments PNC's management.

PNC's integration record, managerial and operational resources, and plans for operating the combined institutions after consummation provide a reasonable basis to conclude that managerial factors are consistent with approval. Based on all the facts of record, the Board has concluded that considerations relating to the financial and managerial resources and future prospects of the organizations involved are consistent with approval.

B. Convenience and Needs Considerations

Under section 3, the Board must consider the effects of the proposal on the convenience and needs of the communities to be served and take into account the records of the relevant depository institutions under the Community Reinvestment Act ("CRA").[13] 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,[14] 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.[15]

The Board has considered the convenience and needs factor and the CRA performance records of the relevant insured depository institutions. As provided in the CRA, the Board evaluates the record of performance of an institution in light of examinations by the appropriate federal supervisors of the CRA performance records of the relevant institutions.[16] 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. PNC Bank received an "outstanding" rating at its most recent CRA performance evaluation by the Office of the Comptroller of the Currency, as of September 30, 2009, and RBC Bank received a "satisfactory" rating at its most recent CRA performance evaluation by the Federal Reserve, as of June 21, 2010. Moreover, the facts of record do not reflect a subsequent decline in the CRA performance of the two institutions since those

[13] 12 U.S.C. § 1842(c)(2); 12 U.S.C. § 2901 *et seq*.

[14] 12 U.S.C. § 2901(b).

[15] 12 U.S.C. § 2903.

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

examinations. The Board has also received 121 comments on the proposal, all in support of the transaction, including 104 comments from community groups.

The Board has considered all the facts of record, including reports of examination of the CRA records of the institutions involved, information provided by PNC, and confidential supervisory information. PNC represents that the proposal will benefit the convenience and needs of the communities currently served by RBC Bank in several ways. PNC intends to offer its treasury management, capital markets, and other corporate services to RBC Bank's corporate clients and to enhance RBC Bank's consumer products with PNC home mortgage loans, including loans designed for the credit needs of LMI borrowers. Consummation of the proposal would provide access to a larger ATM network to current customers of PNC Bank and RBC Bank. PNC also plans to extend its community development activities to the communities currently served by RBC Bank, offering deposit and lending products designed to address the banking needs of LMI families and communities, community-based organizations, and small businesses. PNC intends to deploy teams from its community development banking group into areas currently served by RBC Bank to ensure the promotion of community development lending, investment, and outreach. These efforts would include monetary grants and volunteer services supporting school readiness and Head Start programs in communities served by PNC Bank; a dedicated team focusing on small business lending in certain LMI areas; and strategic investments through a community development subsidiary and specialized New Market Tax Credit and Low-Income-Housing Tax Credit programs designed to foster small business job growth and affordable-housing development. The proposal would result in increased geographic diversification that could reduce the combined company's exposure to regional economic downturns and that could increase administrative efficiency, thereby providing indirect benefits to customers. Based on all the facts of record, the Board has concluded that considerations relating to the convenience and needs of the communities to be served and the CRA performance records of the relevant depository institutions are consistent with approval.

C. Financial Stability

The Dodd-Frank Act amended section 3 of the BHC Act to require the Board also to consider "the extent to which a proposed acquisition, merger, or consolidation would result in greater or more concentrated risks to the stability of the United States banking or financial system."[17] In analyzing this factor, the Board has considered whether the proposal would result in a material increase in risks to financial stability due to the increase in size of the combining firms, a reduction in the availability of substitute providers for the services offered by the combining firms, the extent of interconnectedness among the combining firms and the rest of the financial system, the extent to which the combining firms contribute to the complexity of the financial system, and the extent of cross-border activities of the combining firms.[18] The Board has also considered the relative degree of difficulty of

[17] Section 604(d) of the Dodd-Frank Act, Pub. L. No. 111–203, 124 Stat. 1376, codified at 12 U.S.C. § 1842(c)(7). 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 expansionary proposal by a financial institution. *See* sections 163, 173, and 604(e) and (f) of the Dodd-Frank Act. A special process was established by the Dodd-Frank Act for requiring the divestiture of a business by a financial firm. Section 121 of the act provides that the Board shall require a financial firm to divest or terminate a business only if the Board determines that the company "poses a grave threat to the financial stability of the United States," the Financial Stability Oversight Council ("FSOC") by a vote of two-thirds of its members approves the requirement to divest or terminate the business, and the Board has determined that actions other than divestiture or termination of the business are inadequate to mitigate the grave threat. 12 U.S.C. § 5331.

[18] These categories correspond to those used by the Basel Committee to assess the systemic importance of globally active banking organizations. *See* Basel Committee of Banking Supervision, "Global systemically important banks: assessment methodology and the additional loss absorbency requirement. Rules text." November 2011. These categories are not exhaustive, and additional categories could inform the Board's decision. The

resolving the combined firm.[19] The Board has assessed these factors individually and in combination and has based its assessment on quantitative analysis,[20] using publicly available data, data compiled through the supervisory process, and data obtained through information requests to the institutions involved in the proposal, as well as on qualitative judgments.[21]

Size. An organization's size is one important indicator of the risk the organization poses to the financial system. Congress has imposed a specific 10 percent nationwide deposit limit and a 10 percent nationwide liabilities limit on potential combinations by banking organizations.[22] Other provisions of the Dodd-Frank Act impose special or enhanced supervisory requirements on large banking organizations.[23]

The Board has considered measures of PNC's size relative to the USFS, including PNC's consolidated assets, its total leverage ratio exposures,[24] and its U.S. deposits. As a result of the proposed acquisition, PNC would become the 19th largest USFI based on assets, with $291 billion or 1.1 percent of USFS assets. PNC would become the 16th largest USFI based on leverage exposures, with $420 billion or 1.2 percent of USFS leverage exposures. PNC also would become the fifth largest USFI based on U.S. deposits, with $201 billion or 2.2 percent of total U.S. deposits.

Board expects to issue a notice of proposed rulemaking implementing the provisions of the Dodd-Frank Act that require the Board to take into account a proposal's impact on the risks to the stability of the U.S. financial or banking system. The public would have an opportunity through the rulemaking process to provide the Board with views on how it should take the financial stability factor into account when reviewing applications and notices.

[19] Blackrock is considered to be a subsidiary of PNC for purposes of the BHC Act. However, PNC owns only a minority of the shares of Blackrock, and neither GAAP nor public reporting rules require Blackrock to be consolidated into PNC's balance sheet. PNC's financial operations are not integrated with those of Blackrock, and other operational ties between the two are relatively limited. Based on these and other facts of record, the Board has treated Blackrock as an equity investment of PNC for purposes of the financial stability analysis. This analysis might change if facts regarding their relationship change; for example, if PNC were to increase its stake in Blackrock or establish more significant operational linkages with Blackrock. PNC would require Board approval under section 163(b) of the Dodd-Frank Act to increase its investment in Blackrock, which would require a review of whether the transaction would result in "greater or more concentrated risks to the stability of the United States banking or financial system." Section 163(b) of the Dodd-Frank Act, Pub. L. No. 111–203, 124 Stat. 1376, codified at 12 U.S.C. § 5363.

[20] Much of the data considered by the Board represent measures of an institution's activities relative to the U.S. financial system ("USFS"). For this purpose, the USFS comprises all U.S. financial institutions ("USFIs") used in computing total liabilities for purposes of calculating the limitation on liabilities of a financial company required under section 622 of the Dodd-Frank Act and includes U.S.-based bank and nonbank affiliates of foreign banking organizations. In connection with its supervision of nonbank financial institutions that the FSOC determines could pose a threat to the financial stability of the United States, the Board may require financial and other reporting by these institutions, which would increase the pool of available data for financial stability analyses. *See* sections 113 and 151 of the Dodd-Frank Act, codified at 12 U.S.C. §§ 5323 and 5341, respectively.

[21] In developing the financial stability analysis used in this proposal, the Board has taken into consideration related Board initiatives on financial stability to the extent appropriate, such as proposals to set capital surcharges for global systemically important financial institutions and to identify nonbank systemically important financial institutions. The Board recognizes that a merger analysis is unique in financial stability reviews because it focuses on preventing the formation of an institution that poses significant risks to financial stability rather than regulating an existing institution that poses similar risks. Accordingly, the stability framework for a merger analysis may overlap with, but not be identical to, the framework associated with the other stability initiatives.

[22] 12 U.S.C. §§ 1842(d) and 1852. *See also* section 623 of the Dodd-Frank Act, codified at 12 U.S.C. § 1852.

[23] Section 165 of the Dodd-Frank Act, codified at 12 U.S.C. § 5365, requires the Board to subject all bank holding companies with total consolidated assets of $50 billion or more and any nonbank financial company designated by the FSOC for supervision by the Board to enhanced prudential standards, in order to prevent or mitigate risks to the financial stability of the United States that could arise from the material distress or failure of these firms.

[24] Total leverage exposure is calculated in a manner roughly equivalent to the methodology set out in "Basel III: A global regulatory framework for more resilient banks and banking systems" and takes into account both on- and off-balance-sheet assets.

These measures suggest that, although the combined organization would be large on an absolute basis, PNC would have only a modest share of USFS assets, leverage exposures, and U.S. deposits. PNC also is significantly smaller than the largest USFIs. Three USFIs each would have between six and eight times the assets of PNC, and seven other institutions would have at least twice the assets of PNC. PNC's share of and rank in U.S. deposits, 2.2 percent and fifth, respectively, are higher than the other measures of its size because PNC is primarily engaged in commercial banking activities, which is not the case with many of the largest USFIs. PNC's deposit share would nonetheless be relatively modest. There are three USFIs that would each have between 3.5 and 5 times the U.S. deposits of PNC and three institutions that would each have between 0.9 and 1.5 times the U.S. deposits of PNC. PNC's overall national market share for deposits of approximately 2.2 percent and its market share of national liabilities of approximately 1.4 percent are both well below the 10 percent limits set by Congress.[25]

Both PNC and RBC Bank engage in a relatively traditional set of commercial banking activities, and the increased size of the combined organization would not increase the difficulty of resolving the organization's activities. Accordingly, although the proposed transactions would increase PNC's overall size, and its ranking to the fifth largest bank in the United States based on U.S. deposits, its larger size alone would not result in materially greater or more concentrated risks to the stability of the United States banking or financial system.

Measures of a financial institution's size on a pro forma basis could either understate or overstate risks to financial stability posed by the financial institution. For instance, a relatively small institution that operates in a critical market for which there is no substitute provider or that could transmit its financial distress to other financial organizations through multiple channels, could present material risks to the stability of the USFS. Conversely, an institution that is relatively large could engage in activities that are not complex for which there are several substitute providers in the event of failure or severe financial distress and, accordingly, may present only limited risks to U.S. financial stability.

PNC's size does not rise to the level when the Board would be inclined, solely on that basis, to restrict its ability to make a $27 billion acquisition. Accordingly, the Board has considered other factors, both individually and in combination with size, to evaluate the likely impact of this transaction on financial stability.

Substitutability. The Board has examined whether PNC or RBC Bank engages in any activities that are critical to the functioning of the USFS and whether substitute providers would remain that could quickly step in to perform such activities should the combined entity suddenly be unable to do so as a result of severe financial distress.

PNC and RBC Bank both provide business and consumer credit. RBC Bank has a de minimis market share (less than 1 percent) in a variety of business- and consumer credit-related activities that the Board has considered. Although PNC has a larger share in some of these markets, numerous other USFIs provide business and consumer credit, and the transaction does not create, solidify, or maintain the position of a single entity that is likely to pose an unacceptable risk to U.S. financial stability. The Board also considered a number of critical activities that are performed either by PNC or RBC Bank (but not by both) and in no case would the combined entity provide a service for which many substitute providers could not be readily identified.

[25] In this context, liabilities have been computed under the limitations on consolidated liabilities of section 622 of the Dodd-Frank Act, codified at 12 U.S.C. § 1852.

Interconnectedness. The Board has examined data to determine whether financial distress experienced by the merged entity could create financial instability by being transmitted to other institutions or markets within the U.S. financial or banking system. In particular, the Board has considered whether the combined entity's relationships to other market participants and the similarity of product offerings could transmit material financial distress experienced by the combined entity to its counterparties directly, transmit such distress indirectly through a fire sale of assets or erosion of asset prices, or trigger contagion resulting in the withdrawal of liquidity from other financial institutions.[26]

PNC does not currently engage, and as a result of this transaction would not engage in the future, in business activities or participate in markets to a degree that in the event of financial distress of the combined entity, would pose material risk to other institutions. The pro forma merged entity's expected use of wholesale funding is lower relative to all USFIs than is its corresponding share of consolidated assets. On a pro forma basis, the transaction also would not concentrate exposure to any single counterparty that was among the top three counterparties of either PNC or RBC Bank before the merger. The record does not show other evidence that the pro forma combined entity would be so interconnected with markets and institutions in the U.S. financial or banking system as to make it likely that the combined entity would transmit financial distress to other market participants or to the market generally in a manner or to a degree that would cause material risks to the U.S. financial or banking system. Although distress in a large institution such as PNC could clearly have an effect on other market participants, that effect would not appear to be so adverse as to have a material impact on market stability.

Complexity. The Board has considered the extent to which the pro forma entity contributes to the overall complexity of the USFS. The pro forma entity's share of complex assets in the aggregate USFS appears to be largely consistent with its corresponding share of consolidated assets. The Board also has considered whether the complexity of the pro forma entity's assets and liabilities would hinder its timely and efficient resolution in the event it were to experience financial distress. PNC and RBC Bank do not engage in complex activities, such as serving as a core clearing and settlement organization for critical financial markets, that might complicate the resolution process by increasing the complexity, costs, or timeframes involved in a resolution. Under these circumstances, resolving the pro forma organization would not appear to involve a level of cost, time, or difficulty such that it would cause a material increase in risks to the stability of the USFS.[27]

Cross-border activity. The Board has examined the cross-border activities of PNC and RBC Bank to determine whether the cross-border presence of the combined organization would create difficulties in coordinating a resolution, thereby materially increasing the risks to U.S. financial stability. PNC has several indirect subsidiaries outside the United States, and PNC Bank operates branches in Toronto, Canada, and Nassau, The Bahamas. RBC Bank's cross-border activities are limited to a branch in Georgetown, Cayman Islands.[28] The combined organization is not expected to engage in any additional activities outside the United States as a result of the proposed transaction. In addition, the combined organization would not engage in critical services whose disruption would impact the macroeco-

[26] The source of the contagion could include a belief on the part of market participants that a particular institution is related to the merged entity because it has a similar business model or risk profile, or because the institution is thought to have counterparty exposures to the merged entity.

[27] As noted previously, the Dodd-Frank Act requires bank holding companies like PNC that hold more than $50 billion in total consolidated assets to submit resolution plans, which are intended to assist an institution in managing its risks and plan for a rapid and orderly resolution in the event of material distress or failure and to enable the regulators to understand an institution's complexity. *See* 12 U.S.C. § 5365.

[28] On consummation of the merger of PNC Bank and RBC Bank, PNC intends to transfer all assets and liabilities of the Cayman Branch to PNC Bank's branch in Nassau, The Bahamas, and to close the Cayman Branch.

nomic condition of the United States by disrupting trade or resulting in increased difficulties for the resolution process. Based on this review, the Board considers that the cross-border presence of the consolidated organization would not result in a material increase in risks to the stability of the U.S. financial or banking system.

Financial stability factors in combination. The Board has assessed the foregoing factors in combination to determine whether interactions among them might mitigate or exacerbate risks suggested by looking at them individually. The Board also has considered whether the proposed transaction would provide any stability benefits and whether enhanced prudential standards applicable to the combined organization would tend to offset any potential risks.[29]

For instance, concerns regarding PNC's size would be greater if PNC were also highly interconnected to many different segments of the USFS through its counterparty relationships, participation in short-term funding and capital markets, or other channels. The Board's level of concern about its size would also be greater if the structure and activities of PNC were sufficiently complex that, if PNC were to fail, it would be difficult to resolve its failure quickly without causing significant disruptions to other financial institutions or markets.

As discussed above, the combined entity would not be highly interconnected. Furthermore, the organizational structure and operational regime of the combined organization would be centered on a commercial banking business, and the resolution process would be handled in a predictable manner by the Federal Deposit Insurance Corporation. The Board has also considered other measures that are suggestive of the degree of difficulty with which PNC could be resolved in the event of a failure. These measures suggest that PNC would be significantly more straightforward to resolve than large universal banks or large investment banks.

Based on these and all the other facts of record, the Board has concluded that the proposal would not materially increase risks to the stability of the U.S. financial or banking system. Accordingly, the Board has determined that considerations relating to financial stability are consistent with approval.

D. Conclusion on Section 3(c) Factors

As described above, the Board has considered the financial and managerial resources and future prospects of the companies and banks concerned; effectiveness of the companies in combatting money laundering; the convenience and needs of the community to be served; and the extent to which the proposal would result in greater or more concentrated risks to the stability of the United States banking or financial system. Based on all the facts of record, including those described above, the Board has determined that all of the factors are consistent with approval.

Conclusion

Based on the foregoing and all the facts of record, the Board approved the proposal effective December 19, 2011. In reaching its conclusion, the Board has considered all the facts of record in light of the factors that it is required to consider under the BHC Act and other applicable statutes. The Board's approval is specifically conditioned on compliance by PNC, PNC Bancorp, and PNC Bank with all the commitments made to and relied on by

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[29] Section 165 of the Dodd-Frank Act, Pub. L. No. 111–203, 124 Stat. 1376, codified at 12 U.S.C. § 5365.

the Board in connection with the application and on receipt of all other regulatory approvals. For purposes of this action, the conditions and commitments are deemed to be conditions imposed in writing by the Board in connection with its findings and decision herein and, as such, may be enforced in proceedings under applicable law.

The proposal may not be consummated before the fifteenth calendar day after December 19, 2011, or later than three months thereafter, unless such period is extended for good cause by the Board or the Federal Reserve Bank of Cleveland, acting pursuant to delegated authority.

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

December 23, 2011

Robert deV. Frierson
Deputy Secretary of the Board

Order Issued Under Section 4 of the Bank Holding Company Act

Westpac Banking Corporation
Sydney, Australia

Order Approving Notice to Engage in Nonbanking Activities

Westpac Banking Corporation (“Westpac”), Sydney, Australia, a foreign banking organization subject to the provisions 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 Act and section 225.24 of the Board’s Regulation Y[1] to engage in certain nonbanking activities through the acquisition of all the voting shares of JOHCM (USA) General Partner Inc. (“JOHCM USA”), Wilmington, Delaware, and its foreign parent company, J O Hambro Capital Management Limited (“JOHCM”), London, England. JOHCM and JOHCM USA would be acquired through Westpac’s subsidiary, BT Investment Management Limited (“BTIM”), Sydney, and BTIM’s wholly owned subsidiary, BTIM UK Limited, London. As a result of the acquisition, Westpac and its subsidiaries would engage in the United States in the following activities:

1. providing financial and investment advisory services, in accordance with section 225.28(b)(6) of Regulation Y;[2]
2. providing private placement services, in accordance with section 225.28(b)(7) of Regulation Y;[3] and
3. acting as the general partner for private investment limited partnerships that invest in assets in which a bank holding company is permitted to invest.

Notice of the proposal, affording interested persons an opportunity to comment, has been published in the *Federal Register* (76 *Federal Register* 46,808 (2011)). The time for filing comments has expired, and the Board has considered the proposal and all comments received in light of the factors set forth in section 4 of the BHC Act.

Westpac, with total assets of approximately $644 billion, is the third largest bank in Australia by asset size and engages in a broad range of banking and financial services throughout

[1] 12 U.S.C. §§ 1843(c)(8) and (j); 12 CFR 225.24.
[2] 12 CFR 225.28(b)(6).
[3] 12 CFR 225.28(b)(7).

Australia, New Zealand, and the South Pacific region.[4] Westpac operates a federal branch, with total consolidated assets of $25.5 billion, in New York, New York, and engages in investment advisory activities in the United States through its subsidiary, Hastings Funds Management (USA), San Antonio, Texas.

JOHCM, with approximately $11 billion in assets under management, is an equity investment management firm registered with the Securities and Exchange Commission ("SEC") under the Investment Advisors Act of 1940. JOHCM USA serves as the general partner to a private fund, the JOHCM International Select Fund ("the Fund"), Wilmington, Delaware, a limited partnership that invests in a portfolio of publicly traded international equity securities.[5] JOHCM USA privately places limited partnership interests in the Fund with accredited investors, as defined under SEC rules.[6] In addition, JOHCM USA has retained JOHCM to provide investment advice to the Fund.[7]

The Board previously has determined by regulation that financial and investment advisory activities and private placement activities are closely related to banking for purposes of section 4(c)(8) of the BHC Act.[8] In addition, the Board previously has determined by order that private investment limited partnership activities are permissible for bank holding companies when conducted within certain limits.[9] Westpac has committed that it will conduct the activities of JOHCM and JOHCM USA in accordance with the limitations set forth in Regulation Y and the Board's orders and interpretations relating to each of the proposed activities.

Section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"), which prohibits a banking entity from "acquir[ing] or retain[ing] any equity, partnership, or other ownership interest in or sponsor[ing] a hedge fund or private equity fund,"[10] may restrict the activities in which Westpac proposes to engage. The Board and other federal regulatory agencies recently requested public comment on a proposed regulation to implement section 619 of the Dodd-Frank Act.[11] The regulation has not been finalized and, accordingly, the Board expresses no view on whether the proposed activities would be permissible for Westpac to conduct after the effective date of any final rule the Board may adopt. Westpac has committed that it will conform its activities to comply with the final rule within the deadline established for compliance with section 619 of the Dodd-Frank Act.

To approve the proposal, the Board is required by section 4(j)(2)(A) of the BHC Act to determine that the proposed acquisition of JOHCM USA and the conduct of activities in the United States by JOHCM "can reasonably be expected to produce benefits to the public 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] As part of its evalua-

[4] Asset and ranking data are as of March 31, 2011.

[5] The Fund is exempt from registration with the SEC under section 3(c)(1) of the Investment Company Act of 1940. 15 U.S.C. § 80a-3(c)(1).

[6] SEC Regulation D, 17 CFR 230.501.

[7] Currently, the Fund is the only U.S. limited partnership for which JOHCM USA serves as the general partner and places limited partnership interests. Westpac proposes to conduct these activities for similar limited partnerships that might be established in the future.

[8] 12 CFR 225.28(b)(6), (7).

[9] *See Dresdner Bank AG*, 84 *Federal Reserve Bulletin* 361 (1998); *Meridian Bancorp, Inc.*, 80 *Federal Reserve Bulletin* 736 (1994).

[10] Pub. L. No. 111–203, 124 Stat. 1376, 1620 (2010).

[11] *See* www.federalreserve.gov/newsevents/press/bcreg/20111011a.htm.

[12] 12 U.S.C. § 1843(j)(2)(A)

tion of a proposal under these public interest factors, the Board reviews the financial and managerial resources of the companies involved, the effect of the proposal on competition in the relevant markets, and the public benefits of the proposal.[13]

Financial and Managerial Resources

In reviewing the proposal under section 4 of the BHC Act, the Board has considered the financial and managerial resources of the companies involved and the effect of the proposal on those resources. The Board has considered, among other things, confidential reports of examination, information provided by Westpac, and publicly reported and other financial information in assessing the financial and managerial strength of Westpac.

In evaluating the financial factors of this proposal, the Board has considered a number of factors, including capital adequacy and earnings performance. Westpac's capital ratios exceed the minimum levels that would be required by the Basel Capital Accord and are considered equivalent to the capital that would be required of a U.S. banking organization. Moreover, consummation of this proposal would not have a significant impact on the financial condition of Westpac. Based on its review, the Board finds that Westpac has sufficient financial resources to effect the proposal.

In addition, the Board has carefully considered the managerial resources of Westpac, the supervisory experiences of other banking supervisory agencies with Westpac, and Westpac's record of compliance with applicable U.S. banking laws. The Board has also reviewed reports of examination from the appropriate federal supervisors of the U.S. operations of Westpac that assessed its managerial resources. Based on all the facts of record, the Board has concluded that the financial and managerial resources of the organizations involved in the proposal are consistent with approval.

Competitive Considerations and Financial Stability

The Board has carefully considered the competitive effects of the proposal. There are numerous existing and potential competitors in the industries for the relevant nonbanking activities. In addition, the markets for the proposed services are regional or national in scope. Based on all the facts of record, the Board concludes that consummation of the proposal would have no significantly adverse competitive effects in any relevant market.

The Board has also carefully considered information relevant to risks to the stability of the United States banking and financial systems. Specifically, the Board has considered whether the proposal would result in a material increase in risks to financial stability due to an increase in the size of the acquirer, a reduction in the availability of substitute providers of critical financial products or services, or an increase in the extent of the interconnectedness of the financial system. Consummation of this proposal would not result in a significant decrease in the availability of substitute providers of critical financial services or a significant increase in the size of Westpac and would not result in a significant increase in the interconnectedness of the financial system. Based on these and other factors, the Board concludes that financial stability considerations in this proposal are consistent with approval.

[13] *See* 12 CFR 225.26; *see, e.g.*, *BancOne Corporation*, 83 *Federal Reserve Bulletin* 602 (1997).

Public Benefits

As part of its evaluation of the public interest factors under section 4 of the BHC Act, the Board has reviewed carefully the public benefits and possible adverse effects of the proposal. The record indicates that consummation of the proposal would result in benefits to the public by enhancing Westpac's ability to serve its customers.

For the reasons discussed above and based on all the facts of record, the Board has determined that the conduct of the proposed nonbanking activities within the framework of Regulation Y and Board precedent is not likely to result in significantly 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. Based on all the facts of record, the Board has concluded that consummation of the proposal can reasonably be expected to produce public benefits that would outweigh any likely adverse effects. 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.

Conclusion

Based on the foregoing and all the facts of record, the Board has determined that the notice should be, and hereby is, approved. In reaching its conclusion, the Board has considered all the facts of record in light of the factors that it is required to consider under the BHC Act. The Board's approval is specifically conditioned on compliance by Westpac with the conditions imposed in this order and the commitments made to the Board in connection with the notice. The Board's approval is also subject to the conditions set forth in Regulation Y, including those in sections 225.7 and 225.25(c),[14] and to the Board's authority to require such modification or termination of the activities of Westpac or any of its subsidiaries as the Board finds necessary to ensure compliance with, and to prevent evasion of, the provisions of the BHC Act and the Board's regulations and orders issued thereunder. For purposes of this action, these conditions and commitments are deemed to be conditions imposed in writing by the Board in connection with its findings and decision herein and, as such, may be enforced in proceedings under applicable law.

By order of the Board of Governors, effective October 24, 2011.

Voting for this action: Chairman Bernanke, Vice Chair Yellen, and Governors Duke and Tarullo. Absent and not voting: Governor Raskin.

Robert deV. Frierson
Deputy Secretary of the Board

Order Issued Under Sections 3 and 4 of the Bank Holding Company Act

Green Dot Corporation
Monrovia, California

Order Approving the Formation of a Bank Holding Company

Green Dot Corporation ("Green Dot"), Monrovia, California, has requested the Board's approval under section 3 of the Bank Holding Company Act of 1956, as amended ("BHC

[14] 12 CFR 225.7 and 225.25(c)

Act"),[1] to acquire Bonneville Bancorp ("Bonneville") and thereby indirectly acquire Bonneville's wholly owned subsidiary bank, Bonneville Bank ("Bank"), both of Provo, Utah.[2] Green Dot and Bonneville also have filed with the Board elections to become financial holding companies on consummation of the proposal pursuant to sections 4(k) and (*l*) of the BHC Act and section 225.82 of the Board's Regulation Y.[3]

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published (75 *Federal Register* 7598 (February 22, 2010)). The time for filing comments has expired, and the Board has considered the proposal in light of the factors set forth in section 3 of the BHC Act.

Green Dot, with total consolidated assets of approximately $322 million, provides bank-issued, general-purpose reloadable prepaid debit cards ("GPR cards")[4] and provides settlement services for prepaid debit cards. Green Dot's GPR cards are network branded and are linked to pooled accounts that are held at depository institutions and insured by the Federal Deposit Insurance Corporation ("FDIC"). Green Dot sells its GPR cards through national retail chains and on the Internet.[5] Green Dot's GPR cards currently are issued by third-party banks that maintain accounts on behalf of Green Dot's customers.

Green Dot proposes that Green Dot Bank issue Green Dot GPR cards linked to FDIC-insured accounts and provide settlement services.[6] Green Dot Bank's settlement services would include collecting funds generated from sales of Green Dot GPR cards and related products, distributing funds to issuing banks for cards serviced by Green Dot, and distributing funds to other banks for Green Dot Network[7] acceptance partners. Green Dot would provide administrative services to Green Dot Bank, such as human resources, accounting and tax, marketing, and information technology, and infrastructure services under an intercompany service agreement.[8] Green Dot does not propose to engage in other activities to any significant extent.

Bank, with total assets of approximately $35.7 million, is the 60th largest insured depository institution in Utah, controlling deposits of approximately $29.6 million, which represent less than 1 percent of the total amount of deposits of insured depository institutions in the state.[9] On consummation of the proposal, no company would own 10 percent or more of Green Dot's shares.

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1 12 U.S.C. § 1842.

2 Bonneville and Bank would be renamed Green Dot Bancorp and Green Dot Bank on consummation of the proposal.

3 12 U.S.C. §§ 1843(k) and (*l*); 12 CFR 225.82.

4 Green Dot also offers private-label programs to retailers.

5 A large majority of Green Dot's GPR cards are sold through a single retail chain. The structure of the current agreement between the retail chain and Green Dot appears designed to encourage the parties to continue their business relationship and more closely align the financial interests of the two companies.

6 Green Dot expects to complete the transfer of its GPR card operations within twelve to eighteen months after consummation of the proposed transaction. Bank would retain its existing assets and liabilities and would continue to engage in current lending activities as well as prepaid card activities.

7 Green Dot Network is a scalable technology platform and payments network that supports card sales, purchases, and reloading services to cardholders, retailers, and issuing banks.

8 The provision of such services must comply with the restrictions of sections 23A and 23B of the Federal Reserve Act and the Board's Regulation W on affiliate transactions. 12 U.S.C. §§ 371c, 371c-1; 12 CFR part 223.

9 Asset data are as of June 30, 2011. Deposit and ranking data are as of June 30, 2011, and reflect merger activity through that date. In this context, insured depository institutions include commercial banks, savings banks, and savings associations.

Competitive Considerations

The Board has considered carefully the competitive effects of the proposal in light of all the facts of the record. Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or would be in furtherance of any attempt to monopolize the business of banking in any relevant banking market. The BHC Act also prohibits the Board from approving a proposed bank acquisition that would substantially lessen competition in any relevant banking market, unless the anticompetitive effects of the proposal are clearly outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the community to be served.[10]

Green Dot does not currently control a depository institution. Based on all the facts of record, the Board has concluded that consummation of the proposal would not have a significantly adverse effect on competition or on the concentration of banking resources in any relevant banking market and that competitive considerations are consistent with approval.

Financial, Managerial, and Supervisory Considerations and Future Prospects

Section 3 of the BHC Act requires the Board to consider the financial and managerial resources and future prospects of the companies and depository institutions involved in the proposal and certain other supervisory factors.[11] The Board has considered those factors in light of all the facts of record, including supervisory and examination information received from the relevant federal and state supervisors of the organizations involved, and publicly reported and other available financial information, including information provided by Green Dot. In addition, the Board has consulted with the state and primary federal supervisors of Bank. The Utah Department of Financial Institutions ("Utah DFI") and FDIC have not objected to Green Dot's proposal. The Board has considered the BHC Act factors and related information in light of Green Dot's proposal that Green Dot Bank's operations would be substantially focused on the prepaid card business.

In evaluating financial factors, the Board consistently has considered capital adequacy to be an especially important aspect. Green Dot, Bonneville, and Bank are well capitalized. In addition, Green Dot would make an initial cash injection of $13.6 million in Bank from cash on hand and would maintain a tier 1 leverage ratio of at least 15 percent at Green Dot Bank for five years after consummation. Green Dot has no long-term debt. The Board has consulted with the FDIC and Utah DFI regarding these required capital levels. Green Dot would remain well capitalized on consummation of the proposal. In connection with the proposal to issue its GPR cards through and settle its GPR card transactions at Green Dot Bank, Green Dot has committed to maintain, at Green Dot and/or Green Dot Bank, cash and/or cash equivalents equal to the amount of insured deposits at Green Dot Bank generated through its GPR card operations. The Board also has taken into account Green Dot's record of offering GPR cards to the public, the company's financial strength, and the company's ability to serve as a source of strength to Green Dot Bank. The Board has reviewed Green Dot's operating plan for Green Dot Bank and Green Dot's projections that Green Dot and Green Dot Bank would be able to remain well-capitalized and profitable even under certain stress scenarios that could negatively affect the prepaid card operations that would be conducted at Green Dot and Green Dot Bank.

[10] 12 U.S.C. § 1842(c)(1).

[11] 12 U.S.C. § 1842(c)(2) and (3).

The Board also has considered the managerial resources of the organizations involved and of the proposed combined organization. The Board has reviewed the examination records of Bonneville and Bank and has conducted inspections of Green Dot,[12] including assessments of its current management, risk-management systems, and operations. The Board also has considered the supervisory experience of the other relevant banking agencies with the organizations, including their records of compliance with applicable banking and anti-money-laundering laws.[13] In addition, the Board has considered Green Dot's plans for implementing the proposal and for the proposed management of the organizations involved after consummation. Moreover, the Board has considered information regarding Green Dot's enterprise-wide risk-management program collected by examiners with the Federal Reserve, FDIC, and Utah DFI. The Board has also considered that Green Dot has retained management with significant experience in the prepaid card industry as well as management experienced in commercial and community banking.

In addition, the Board has considered the future prospects of Green Dot, Bonneville, and Bank in light of the financial and managerial resources and the proposed business plan. As noted, Green Dot Bank's business activity would be focused narrowly on the issuance of GPR cards. A business plan that focuses on a narrow business activity[14] and depends on a limited number of key business partners carries significantly greater risks than a business plan that employs broad diversification of activities and counterparties. The Board expects banking organizations with a narrow focus to address these increased risks with financial resources, managerial systems, and expertise commensurate with that additional level of risk. In this case, the Board has relied on the significant level of capital that Green Dot and its bank will have on consummation and Green Dot's commitment to maintain Green Dot Bank as well capitalized with a tier 1 leverage ratio of at least 15 percent for five years after consummation. This capital level is well in excess of the tier 1 leverage ratio needed to be considered well capitalized but is appropriate in light of the single focus of Green Dot and Green Dot Bank's activity. Green Dot has committed that Green Dot Bank will not pay dividends for three years after consummation of the proposal. The Board has also considered that Green Dot Bank's primary source of deposits would be the funds associated with GPR cards purchased by individuals, which Green Dot has committed to balance with equal levels of cash or cash equivalents. In addition, the Board has considered Green Dot's enterprise-wide risk-management program and Green Dot's retention of management with significant experience in the prepaid card industry as well as management experienced in commercial and community banking.

On this basis, including the commitments made by Green Dot to the Board, the Board has concluded that considerations relating to the financial and managerial resources and future prospects involved in the proposal are consistent with approval, as are the other supervisory factors.

Convenience and Needs Considerations

In acting on a proposal under section 3 of the BHC Act, the Board also must consider the effects of the proposal on the convenience and needs of the communities to be served and

[12] The Federal Reserve Bank of San Francisco, FDIC, and Utah DFI conducted on-site reviews of Green Dot's operations in connection with the proposal.

[13] Green Dot is currently registered with the United States Treasury Department's Financial Crimes Enforcement Network as a Money Service Business and files Suspicious Activity Reports and Currency Transaction Reports.

[14] Green Dot has committed to balance Green Dot Bank's GPR card deposits with equal levels of cash or cash equivalents at Green Dot or Green Dot Bank. Accordingly, the proposal does not appear to present increased credit risk associated with narrowly focused business plans that are dependent on one asset category, such as a particular type of lending. As discussed below, the Board has considered the risks posed by Green Dot's business plan in light of its proposal to mitigate such risks, including its commitments.

take into account the records of the relevant insured depository institutions under the Community Reinvestment Act (“CRA”).[15] 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, 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 neighborhoods, in evaluating banking proposals.[16]

The Board has considered carefully all the facts of record, including evaluations of the CRA performance record of Bank, information provided by Green Dot, and confidential supervisory information. Bank has received a “satisfactory” rating at its most recent CRA performance evaluation by the FDIC, as of May 21, 2007. To ensure that Bank will continue to meet its CRA obligation in the Provo community, Green Dot has committed to submit a proposed strategic plan for Green Dot Bank to its primary federal regulator within six months of consummation of the proposal.[17] Green Dot also has stated that Bank would maintain its current level of lending to its local community.

On May 19, 2011, the Office of the Attorney General of Florida (“Florida AG’s Office”) announced that it is investigating five prepaid debit card companies, including Green Dot, for possible deceptive and unfair practices. The Board has consulted with the Florida AG’s Office regarding this matter and has been advised by that office that Green Dot is fully cooperating with the investigation.[18] Green Dot has also represented that it is developing and will issue GPR cards with improved disclosures that are designed to address the matters raised by the Florida AG’s Office and to comply with Florida law.

Based on a review of the entire record, the Board has concluded that convenience and needs considerations and the CRA performance record of Bank are consistent with approval of the proposal.

Financial Holding Company Elections

As noted, Green Dot and Bonneville have filed elections to become financial holding companies pursuant to sections 4(k) and (*l*) of the BHC Act and section 225.82 of the Board’s Regulation Y. Green Dot and Bonneville have certified that Bank is well capitalized and well managed and have provided all the information required under Regulation Y. Green Dot and Bonneville have also certified that they are well capitalized and well managed, pursuant to section 4(*l*) of the BHC Act, as amended by section 606 of the Dodd-Frank Wall Street Reform and Consumer Protection Act.[19] Based on all the facts of record, the Board has determined that the elections of Green Dot and Bonneville to become financial holding companies will become effective on consummation of the proposal, if on that date Green Dot, Bonneville, and Bank remain well capitalized and well managed and if Bank has received a rating of at least “satisfactory” at its most recent performance evaluation under the CRA.

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[15] 12 U.S.C. §§ 2901–2908; 12 U.S.C. § 1842(c)(2).

[16] 12 U.S.C. § 2903.

[17] Under the strategic plan alternative, a bank is required to develop a plan, using input from members of the public in the bank’s assessment area(s), that provides measurable goals for meeting the credit needs of the bank’s assessment area(s). *See, e.g.*, 12 CFR 228.27. The bank’s primary federal regulator is responsible for evaluating the plan and, if approved, the bank’s success in achieving the goals of the approved plan.

[18] The Board’s action on this application does not limit in any manner the authority of the State of Florida to take any action that it considers appropriate with respect to Green Dot.

[19] Pub. L. No. 111–203, 124 Stat. 1376, codified at 12 U.S.C. § 1843(*l*)(1).

Financial Stability

As required by section 3 of the BHC Act, the Board has considered the effects of the proposal on the stability of the United States banking or financial system.[20] Based on a review of the entire record, the Board has concluded that the proposal would not result in greater or more concentrated risks to the stability of the United States banking or financial system.

Conclusion

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

The proposed transaction 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 San Francisco, acting pursuant to delegated authority.

By order of the Board of Governors, effective November 23, 2011.

Voting for this action: Chairman Bernanke, Vice Chair Yellen, and Governors Tarullo and Raskin. Voting against this action: Governor Duke.

Robert deV. Frierson
Deputy Secretary of the Board

Dissenting Statement of Governor Duke

I am not in favor of approving this application. As a general matter, I have concerns about business plans that focus narrowly on one or a few products. Companies with narrow business plans face risks that are different than those faced by more diversified companies and are more vulnerable to unexpected shocks. In this case, I have specific concerns about the risks presented by Green Dot's proposal to implement a business plan at Green Dot Bank focused on the issuance of general-purpose, reloadable prepaid debit cards ("GPR cards").

Green Dot's proposal to implement a business plan at Green Dot Bank predominantly focused on issuing GPR cards would directly tie the future prospects of Green Dot to success in the specialized market for prepaid debit cards. The prepaid debit card industry is subject to various risks, including the possibility that the technology currently employed by industry participants could become obsolete, that consumers' demand for prepaid debit cards as an alternative to more traditional banking products and services could decline, that potential legislative or regulatory changes could reduce or eliminate the profitability of issuing prepaid debit cards, and that competition in the prepaid debit card industry may increase as a result of full-service banking organizations entering the market. In addition, the business model employed by prepaid debit card providers, including the model

[20] Section 604 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111–203, 124 Stat. 1376, codified at 12 U.S.C. § 1842(c)(7).

employed by Green Dot, involves significant exposure to operational, concentration, consumer, counterparty, settlement, and compliance risks. Moreover, in addition to the increased risks presented by a business plan focused on a narrow business activity, Green Dot currently relies on a single retail partner for a large majority of its revenues, and a loss of the relationship would have a materially adverse impact on Green Dot's revenues.

Furthermore, I do not believe that the steps Green Dot proposed to mitigate risk, including its commitments that Bank would maintain increased capital levels for five years and refrain from paying dividends for three years and its commitment to maintain certain levels of cash and cash equivalents, adequately address the risks posed by Green Dot's proposal to operate Green Dot Bank primarily as a GPR card issuer. These commitments may increase the ability of Green Dot to absorb losses, but they do not address the fundamental source of the risk posed by Green Dot's narrow business plan and, consequently, do not actually reduce the risks associated with that business plan.

For these reasons, in my view the considerations related to the future prospects of Green Dot and Green Dot Bank are not consistent with approval.

Accordingly, I would deny this proposal.

November 23, 2011

Order Issued Under Bank Merger Act

The Croghan Colonial Bank

Fremont, Ohio

Order Approving the Acquisition of Branches

The Croghan Colonial Bank ("Bank"), a state member bank and a subsidiary of Croghan Bancshares, Inc., both of Fremont, Ohio, has applied under section 18(c) of the Federal Deposit Insurance Act[1] ("Bank Merger Act") to acquire four branches from The Home Savings and Loan Company of Youngstown, Ohio ("Home Savings"), Youngstown, in Tiffin, Fremont, and Clyde, all in Ohio.[2] Bank has also applied under section 9 of the Federal Reserve Act[3] ("FRA") to establish branches at three of those locations.

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.[4] 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 Federal Deposit Insurance Corporation ("FDIC"). The time for filing comments has expired, and the Board has considered the application and all comments received in light of the factors set forth in the Bank Merger Act and section 9 of the FRA.

1 12 U.S.C. § 1828(c).

2 The four branches to be acquired are listed in the appendix.

3 12 U.S.C. § 321.

4 12 CFR 262.3(b).

Bank is the 44th largest insured depository institution in Ohio, with less than 1 percent of all deposits in Ohio banks and thrift institutions.[5] Home Savings is the 16th largest insured depository institution in Ohio, with less than 1 percent of deposits in the state.

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.[6] 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 the communities to be served.[7]

The proposal would affect competition in the Fremont, Ohio banking market, where Bank and Home Savings directly compete.[8] The Board has reviewed carefully the competitive effects of the proposal on the banking market in light of all the facts of record, including the number of competitors that would remain in the market, the relative share of the total deposits in insured depository institutions in the market ("market deposits") that Bank would control,[9] the concentration level of market deposits and the increase in this level as measured by the Herfindahl-Hirschman Index ("HHI") under the Department of Justice Bank Merger Competitive Review guidelines ("DOJ Bank Merger Guidelines"),[10] and other characteristics of the markets.

Bank has the largest share of market deposits in the Fremont banking market with 37.6 percent, and Home Savings has the ninth largest share of market deposits with 2.7 percent. On consummation of the proposal, Bank's share of market deposits would increase to 41.9 percent, and the HHI would increase 302 points, from 1971 to 2273.

In addition to banks and thrift institutions, there are two credit unions that operate in the Fremont banking market: Fremont Federal Credit Union and Clyde-Fremont Area Credit Union. Both credit unions have broad membership criteria that include all the residents in the banking market. In addition, both credit unions compete actively with area banks for retail customers and offer services such as street-level offices, drive-up lanes, and ATMs.

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[5] Data are as of June 30, 2011. In this context, insured depository institutions include insured commercial banks, savings banks, and savings associations.

[6] 12 U.S.C. § 1828(c)(5)(A).

[7] 12 U.S.C. § 1828(c)(5)(B).

[8] The Fremont banking market is defined as Sandusky County, excluding the city of Bellevue, all in Ohio.

[9] Data are based on calculations in which the pre-acquisition deposits of Home Savings 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). The post-acquisition deposits of Home Savings are weighted at 100 percent because the deposits will be owned by a commercial banking organization. *See*, *e.g.*, *Norwest Corporation*, 78 *Federal Reserve Bulletin* 452 (1992).

[10] 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 anti-competitive 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 recently 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.

The Board finds that these circumstances warrant including the deposits of these credit unions on a 50 percent weighted basis.[11]

If both credit unions are included on a weighted basis, Bank's pro forma share of market deposits would be 36 percent, and the HHI would increase by 231 points, from 1554 to 1785. The Board has concluded that the activities of these credit unions exert a competitive influence that mitigates, in part, the potential effects of the proposal in the Fremont banking market. In addition, numerous competitors would remain in the banking market. Four banks would each have shares of market deposits ranging from 8 percent and 11 percent.

The DOJ has reviewed the anticipated competitive effects of the proposal and has advised the Board that consummation of the proposal would not likely have a significantly adverse effect on competition in the relevant banking market. The FDIC has been afforded an opportunity to comment and has not objected to the proposal.

The Board has reviewed carefully all the facts of record and, for the reasons discussed in this order, has concluded that consummation of the proposal is not likely to affect competition or the concentration of resources in a significantly adverse manner in the relevant banking market. Accordingly, based on all the facts of record, the Board has determined that competitive factors are consistent with approval of the proposal.

Financial, Managerial, and Other Supervisory Factors

In reviewing this proposal under the Bank Merger Act and section 9 of the FRA, the Board has considered the financial and managerial resources and future prospects of the institutions involved. The Board has reviewed these factors in light of all the facts of record, including supervisory reports of examination assessing the financial and managerial resources of Bank and information provided by the bank. The Board notes that Bank would remain well capitalized on consummation of 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 and other supervisory factors are consistent with approval of the proposal.

Convenience and Needs Considerations and Financial Stability

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").[12] 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 neighborhoods, in evaluating bank acquisition proposals. Accordingly, the Board has carefully considered the convenience and needs factor and the CRA performance records of Bank and Home Savings 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 performance records

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[11] The Board previously has considered the competitiveness of certain active credit unions as a mitigating factor. *See*, *e.g.*, *The PNC Financial Services Group, Inc.*, 93 *Federal Reserve Bulletin* C65 (2007); *Regions Financial Corporation*, 93 *Federal Reserve Bulletin* C16 (2007); *Wachovia Corporation*, 92 *Federal Reserve Bulletin* C183 (2006); and *F.N.B. Corporation*, 90 *Federal Reserve Bulletin* 481 (2004).

[12] 12 U.S.C. § 2901 *et seq*.

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.[13]

Bank received an overall rating of "satisfactory" at its most recent CRA performance examination by the Federal Reserve Bank of Cleveland, as of June 2011. Home Savings received an overall rating of "satisfactory" from the FDIC at its most recent evaluation for CRA performance, as of July 2008.

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

The Board has also carefully considered information relevant to risks to the stability of the United States banking or financial system. The Board concludes that financial stability considerations in this proposal are consistent with approval.

Establishment of Branches

As noted above, Bank has also applied under section 9 of the FRA to establish branches at three of the acquired offices of Home Savings. Bank has indicated that it intends to close the branch in Clyde, Ohio, that it would acquire from Home Savings and to consolidate its operations into a branch that Bank currently operates that is less than one-tenth of a mile away.[14] The Board has considered the factors it is required to consider when reviewing an application for establishing branches pursuant to section 9 of the FRA[15] and for the reasons discussed in this order, finds those factors are 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 applications is specifically conditioned on compliance by Bank 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.

The acquisition 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 Cleveland, acting pursuant to delegated authority.

By order of the Board of Governors, effective November 28, 2011.

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

[14] Both branches are in the Fremont banking market. The proposed branch closure qualifies as a "short distance" consolidation. *See Joint Policy Statement Regarding Branch Closings*, 64 *Federal Register* 34844 at 34846. Accordingly, the closure is not subject to the notice requirements of section 42 of the Federal Deposit Insurance Act. 12 U.S.C. § 1831r-1(e); 64 *Federal Register* 34844 at 34846.

[15] *See* 12 U.S.C. § 322.

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

Robert deV. Frierson
Deputy Secretary of the Board

Appendix

Branches in Ohio to be Acquired from Home Savings
1. 48 E. Market Street, Tiffin 44883
2. 796 W. Market Street, Tiffin 44883
3. 910 Sean Drive, Fremont 43420
4. 225 N. Main Street, Clyde 43410 (to be closed)

Orders Issued Under International Banking Act

Banco do Estado do Rio Grande do Sul S.A.
Port Alegre, Brazil

Order Approving Establishment of a Branch

Banco do Estado do Rio Grande do Sul S.A. ("Bank"), Port Alegre, Brazil, a foreign bank within the meaning of the International Banking Act ("IBA"), has applied under section 7(d) of the IBA[1] to establish a limited federal branch in Miami, Florida. The Foreign Bank Supervision Enhancement Act of 1991, which amended the IBA, provides that a foreign bank must obtain the approval of the Board to establish a branch in the United States.

Notice of the application, affording interested persons an opportunity to comment, has been published in a newspaper of general circulation in Miami (*Miami Daily Business Review*, March 12, 2010). The time for filing comments has expired, and the Board has considered all comments received.

Bank, with total assets of approximately $19.0 billion,[2] is the eleventh largest bank in Brazil. The State of Rio Grande do Sul owns approximately 99.6 percent of Bank's voting stock. Bank provides a range of banking services and financial products to retail customers, small- and medium-sized companies, and public-sector entities. Bank currently operates a branch in New York, New York, and this branch will be closed soon after the proposed limited federal branch in Miami is established. Bank also operates a branch in the Cayman Islands. Bank meets the requirements for a qualifying foreign banking organization under Regulation K.[3]

Bank proposes to relocate the operations of its existing branch in New York to Miami in order to better serve the needs of its customers in the United States. Consistent with the restrictions on a limited branch, the proposed branch would not take any deposits other than those permitted for a corporation organized under section 25A of the Federal Reserve Act.[4]

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1 12 U.S.C. § 3105(d).

2 Asset and ranking data are as of June 30, 2011.

3 12 CFR 211.23(a).

4 To convert the limited branch into a branch, Bank must apply pursuant to section 7 of the IBA. 12 U.S.C. § 3105(d). Under section 25A of the Federal Reserve Act, an Edge corporation may receive deposits outside the United States and only such deposits within the United States that are incidental to or for the purpose of carry-

Under the IBA and Regulation K, in acting on an application by a foreign bank to establish a branch, the Board must consider whether the foreign bank (1) engages directly in the business of banking outside the United States; (2) has furnished the Board with the information it needs to assess the application adequately; and (3) is subject to comprehensive supervision on a consolidated basis by its home country supervisors.[5] The Board also considers additional standards as set forth in the IBA and Regulation K.[6]

As noted above, Bank engages directly in the business of banking outside the United States. Bank also has provided the Board with information necessary to assess the application through submissions that address the relevant issues.

With respect to supervision by home country authorities, the Board previously has determined that other banks in Brazil are subject to home country supervision on a consolidated basis by the Central Bank of Brazil ("Central Bank"), which has primary responsibility for the regulation of financial institutions in Brazil.[7] Bank is supervised by the Central Bank on substantially the same terms and conditions as these other banks. Based on all the facts of record, it has been determined that Bank is subject to comprehensive supervision on a consolidated basis by its home country supervisor.

The additional standards set forth in section 7 of the IBA and Regulation K have also been taken into account.[8] The Central Bank has no objection to the establishment of the proposed branch.

With respect to the financial and managerial resources of Bank, taking into consideration the bank's record of operations in its home country, its overall financial resources, and its standing with its home country supervisors, financial and managerial factors are consistent with approval of the proposed limited branch. Brazil has adopted risk-based capital stan-

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ing out transactions in foreign countries. 12 U.S.C. § 615(a). Regulation K defines the extent of permissible deposit-taking activities of Edge corporations. 12 CFR 211.6(a)(1). Under section 5 of the IBA, a foreign bank may establish a branch outside its home state if the branch limits its deposit-taking to that of an Edge corporation operating under section 25A of the Federal Reserve Act. 12 U.S.C. § 3103(a)(7)(A). Currently, Bank's home state is New York. Regulations implementing the IBA allow foreign banks to change their home state one time with prior notice to the Federal Reserve. 12 CFR 211.22(b). With the closure of the New York branch, Bank will change its IBA home state from New York to Florida.

5 12 U.S.C. § 3105(d)(2); 12 CFR 211.24. In assessing this standard, the Board considers, among other indicia of comprehensive, consolidated supervision, the extent to which the home country supervisors: (i) ensure that the bank has adequate procedures for monitoring and controlling its activities worldwide; (ii) obtain information on the condition of the bank and its subsidiaries and offices through regular examination reports, audit reports, or otherwise; (iii) obtain information on the dealings with and relationship between the bank and its affiliates, both foreign and domestic; (iv) receive from the bank financial reports that are consolidated on a worldwide basis or comparable information that permits analysis of the bank's financial condition on a worldwide consolidated basis; (v) evaluate prudential standards, such as capital adequacy and risk asset exposure, on a worldwide basis. No single factor is essential, and other elements may inform the Board's determination.

6 12 U.S.C. § 3105(d)(3)–(4); 12 CFR 211.24(c)(2)–(3). The additional standards set forth in section 7 of the IBA and Regulation K include the following: whether the bank's home country supervisor has consented to the establishment of the office; the financial and managerial resources of the bank; whether the bank has procedures to combat money laundering, whether there is a legal regime in place in the home country to address money laundering, and whether the home country is participating in multilateral efforts to combat money laundering; whether the appropriate supervisors in the home country may share information on the bank's operations with the Board; whether the bank and its U.S. affiliates are in compliance with U.S. law; the needs of the community; the bank's record of operation. The Board may also take into account, in the case of a foreign bank that presents a risk to the stability of the United States, whether the home country of the foreign bank has adopted, or is making demonstrable progress toward adopting, an appropriate system of financial regulation for the financial system of such home country to mitigate such risk. 12 U.S.C. § 3105(d)(3)(E).

7 The Board has determined that three Brazilian banks, Banco Itaú S.A., Banco Bradesco S.A., and Banco do Brasil S.A., were subject to comprehensive consolidated supervision by the Central Bank in connection with each bank's election to be treated as a financial holding company (effective in February 2002 for Banco Itaú, in January 2004 for Banco Bradesco S.A., and in April 2010 for Banco do Brasil).

8 *See*, *supra*, note 6.

dards that are consistent with those established by the Basel Capital Accord ("Accord"). Bank's capital is in excess of the minimum levels that would be required by the Accord and is considered equivalent to capital that would be required of a U.S. banking organization. Managerial and other financial resources of Bank also are consistent with approval, and Bank appears to have the experience and capacity to support the proposed branch. In addition, Bank has established controls and procedures for the proposed branch to ensure compliance with U.S. law and for its operations in general.

Brazil is a member of the Financial Action Task Force and subscribes to its recommendations on measures to combat money laundering. In accordance with these recommendations, Brazil has enacted laws and created legislative and regulatory standards to deter money laundering, terrorist financing, and other illicit activities. Money laundering is a criminal offense in Brazil, and financial institutions are required to establish internal policies, procedures, and systems for the detection and prevention of money laundering throughout their worldwide operations. Bank has policies and procedures to comply with these laws and regulations, and Bank's compliance with applicable laws and regulations is monitored by governmental entities responsible for anti-money-laundering compliance.

With respect to access to information about Bank's operations, the Board has reviewed the restrictions on disclosure in relevant jurisdictions in which Bank operates and has communicated with relevant government authorities regarding access to information. Bank has committed to make available to the Board such information on the operations of Bank and any of its affiliates that the Board deems necessary to determine and enforce compliance with the IBA, the Bank Holding Company Act, and other applicable federal law. To the extent that the provision of such information to the Board may be prohibited by law or otherwise, Bank has committed to cooperate with the Board to obtain any necessary consents or waivers that might be required from third parties for disclosure of such information. In light of these commitments and other facts of record, and subject to the condition described below, the Board has determined that Bank has provided adequate assurances of access to any necessary information that the Board may request.

Information relevant to the standard regarding risk to the stability of the United States financial system has also been reviewed. In particular, consideration has been given to the absolute and relative size of Bank in its home country, the scope of Bank's activities, including the type of activities it proposes to conduct in the United States and the potential for those activities to increase or transmit financial instability, and the framework in place for supervising Bank in its home country. Based on these and other factors, financial stability considerations in this proposal are consistent with approval.

On the basis of all the facts of record, and subject to the commitments made by Bank, as well as the terms and conditions set forth in this order, Bank's application to establish a limited federal branch is hereby approved by the Director of the Division of Banking Supervision and Regulation, with the concurrence of the General Counsel, pursuant to authority delegated by the Board.[9] Should any restrictions on access to information on the operations or activities of Bank and its affiliates subsequently interfere with the Board's ability to obtain information to determine and enforce compliance by Bank or its affiliates with applicable federal statutes, the Board may require termination of any of Bank's direct or indirect activities in the United States, or in the case of any such operation licensed by the Office of the Comptroller of the Currency ("OCC"), recommend termination of such operation. Approval of this application also is specifically conditioned on compliance by Bank with the commitments made in connection with this application and with the condi-

[9] 12 CFR 265.7(d)(12).

tions in this order.[10] The commitments and conditions referred to above are conditions imposed in writing by the Board in connection with this decision and may be enforced in proceedings under 12 U.S.C. § 1818 against Bank and its affiliates.

By order, approved pursuant to authority delegated by the Board, effective October 6, 2011.

Robert deV. Frierson
Deputy Secretary of the Board

Bankia, S.A.
Valencia, Spain

Order Approving Establishment of a Branch

Bankia, S.A. ("Bankia"), a foreign bank within the meaning of the International Banking Act ("IBA"), has applied under section 7(d) of the IBA[1] to establish a branch in Miami, Florida. The Foreign Bank Supervision Enhancement Act of 1991, which amended the IBA, provides that a foreign bank must obtain the approval of the Board to establish a branch in the United States.[2]

Notice of the application, affording interested persons an opportunity to comment, has been published in a newspaper of general circulation (*Miami Herald*, June 14, 2011). The time for filing comments has expired, and the Board has considered all comments received.

Bankia, with total assets of approximately $406.3 billion,[3] is the fourth largest bank in Spain. Banco Financiero y de Ahorros, S.A. ("BFA"), Madrid, Spain, owns 52.4 percent of Bankia.[4] No other shareholder owns more than 5 percent of the shares of Bankia. Bankia is a commercial bank that offers services and products in retail banking, corporate banking and finance, capital markets, asset management, and personal banking. Bankia intends to take over the international operations previously conducted by the savings banks that own BFA. Bankia's indirect parents, Caja Madrid and Bancaja, maintain an agency and branch, respectively, in Miami, Florida. Bankia meets the requirements for a qualifying foreign banking organization under Regulation K.[5]

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[10] The Board's authority to approve the establishment of the proposed branch parallels the continuing authority of the OCC to license offices of a foreign bank. The Board's approval of this application does not supplant the authority of the OCC to license the proposed office of Bank in accordance with any terms or conditions that it may impose.

[1] 12 U.S.C. § 3105(d).

[2] *Id.*

[3] Asset and ranking data are as of September 30, 2011.

[4] BFA was created through a Sistema Institucional de Protección (Integration Agreement), an integration transaction supported by the Bank of Spain to address the effects of the global financial crisis on Spanish financial institutions by consolidating a number of Spanish savings banks, or cajas de ahorros, operating in Spain. BFA was established by seven Spanish savings banks, including Caja de Ahorros y Monte de Piedad de Madrid, Caja Madrid ("Caja Madrid"), which owns 52.1 percent of BFA, and Caja de Ahorros de Valencia, Castellón y Alicante, Bancaja ("Bancaja"), which owns 37.7 percent. Each of the remaining five savings banks owns less than 3 percent of the issued shares of BFA. The Board approved BFA's application to become a bank holding company on December 16, 2010. *See Caja de Ahorros de Valencia, Castellón y Alicante, Bancaja*, 97 *Federal Reserve Bulletin* 4 (2011). BFA received €4.465 billion from the Fondo de Reestructuración Ordenada Bancaria ("FROB") in exchange for perpetual convertible preference shares of BFA. FROB was created by the Spanish government to support and facilitate integrations transactions among Spanish financial institutions. FROB is a bank holding company by virtue of its ownership interest in BFA. *See Caja de Ahorros de Valencia, Castellón y Alicante, Bancaja*, *supra*. FROB's investment in BFA represents approximately 17 percent of the total equity and, if converted to voting shares, would represent 17 percent of BFA's voting shares. The current proposal would not increase FROB's indirect ownership of any bank in the United States.

[5] 12 CFR 211.23(a).

Bankia, as part of a corporate reorganization,[6] proposes to establish the branch to assume the operations of Caja Madrid's agency and Bancaja's branch, and those offices would be closed. The proposed branch would offer substantially the same products and services currently provided by the Caja Madrid and Bancaja offices.

Under the IBA and Regulation K, in acting on an application by a foreign bank to establish a branch, the Board must consider whether the foreign bank (1) engages directly in the business of banking outside the United States; (2) has furnished the Board the information it needs to assess the application adequately; and (3) is subject to comprehensive supervision on a consolidated basis by its home country supervisors.[7] The Board also considers additional standards as set forth in the IBA and Regulation K.[8]

As noted above, Bankia engages directly in the business of banking outside the United States. Bankia also has provided the Board with information necessary to assess the application through its submissions that address the relevant issues.

With respect to supervision by home country authorities, the Board previously has determined that BFA, Caja Madrid, and Bancaja are subject to comprehensive supervision on a consolidated basis by their home country supervisor.[9] The Board also has determined that other banks in Spain that are supervised under the same regime as Bankia were subject to home country supervision on a consolidated basis.[10] Bankia is supervised by the Bank of Spain on substantially the same terms and conditions as BFA, Caja Madrid, Bancaja, and those other banks. Based on all the facts of record, the Board has determined that Bankia is subject to comprehensive supervision on a consolidated basis by its home country supervisor.

The additional standards set forth in section 7 of the IBA and Regulation K have also been taken into account.[11] The Bank of Spain has no objection to the establishment of the proposed branch.

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6 Subsequent to BFA's creation, BFA and the savings banks agreed to transfer certain BFA assets and liabilities, including the group's banking business, to Bankia.

7 12 U.S.C. § 3105(d)(2); 12 CFR 211.24. In assessing this standard, the Board considers, among other indicia of comprehensive, consolidated supervision, the extent to which the home country supervisors (i) ensure that the bank has adequate procedures for monitoring and controlling its activities worldwide; (ii) obtain information on the condition of the bank and its subsidiaries and offices through regular examination reports, audit reports, or otherwise; (iii) obtain information on the dealings with and relationship between the bank and its affiliates, both foreign and domestic; (iv) receive from the bank financial reports that are consolidated on a worldwide basis or comparable information that permits analysis of the bank's financial condition on a worldwide consolidated basis; (v) evaluate prudential standards such as capital adequacy and risk asset exposure, on a worldwide basis. No single factor is essential, and other elements may inform the Board's determination.

8 12 U.S.C. § 3105(d)(3)–(4); 12 CFR 211.24(c)(2)–(3). The additional standards set forth in section 7 of the IBA and Regulation K include the following considerations: whether the bank's home country supervisor has consented to the establishment of the office; the financial and managerial resources of the bank; whether the bank has procedures to combat money laundering, whether there is a legal regime in place in the home country to address money laundering, and whether the home country is participating in multilateral efforts to combat money laundering; whether the appropriate supervisors in the home country may share information on the bank's operations with the Board; whether the bank and its U.S. affiliates are in compliance with U.S. law; the needs of the community; the bank's record of operation; in the case of a foreign bank that presents a risk to the stability of the United States, whether the home country of the foreign bank has adopted, or is making demonstrable progress toward adopting, an appropriate system of financial regulation for the financial system of such home country to mitigate such risk.

9 *See Caja de Ahorros de Valencia, Castellón y Alicante, Bancaja*, *supra*; *Caja de Ahorros y Monte de Piedad de Madrid*, 95 *Federal Reserve Bulletin* B23 (2009); *Caja de Ahorros de Valencia, Castellón y Alicante, Bancaja*, 84 *Federal Reserve Bulletin* 231 (1998).

10 *See, e.g., Banco Popular Español S.A.*, 92 *Federal Reserve Bulletin* C130 (2006); *Banco Bilbao Vizcaya Argentaria, S.A.*, 91 *Federal Reserve Bulletin* 258 (2005); *Banco Pastor, S.A.*, 87 *Federal Reserve Bulletin* 555 (2001).

11 *See, supra*, note 8.

With respect to the financial and managerial resources of Bankia, taking into consideration the bank's record of operations in its home country, its overall financial resources, and its standing with home country supervisors, financial and managerial factors are consistent with approval of the proposed branch. Spain has adopted risk-based capital standards that are consistent with those established by the Basel Capital Accord ("Accord"). Bankia's capital is in excess of the minimum levels that would be required by the Accord and is considered equivalent to capital that would be required of a U.S. banking organization for a similar proposal. Managerial and other financial resources of Bankia are also consistent with approval, and Bankia appears to have the experience and capacity to support the proposed branch. In addition, Bankia has established controls and procedures for the proposed branch to ensure compliance with U.S. law.

Spain has enacted laws and regulations to deter money laundering that are consistent with the Financial Action Task Force recommendations. Money laundering is a criminal offense in Spain, and financial institutions are required to establish internal policies, procedures, and systems for the detection and prevention of money laundering throughout their worldwide operations. Bankia has policies and procedures to comply with these laws and regulations, and its compliance with applicable laws and regulations is monitored by governmental entities responsible for anti-money-laundering compliance.

With respect to access to information about Bankia's operations, the restrictions on disclosure in relevant jurisdictions in which Bankia operates have been reviewed and relevant government authorities have been contacted regarding access to information. Bankia has committed to make available to the Board such information on the operations of Bankia and any of its affiliates that the Board deems necessary to determine and enforce compliance with the IBA, the Bank Holding Company Act, and other applicable federal law. To the extent that the provision of such information to the Board may be prohibited by law or otherwise, Bankia has committed to cooperate with the Board to obtain any necessary consents or waivers that might be required from third parties for disclosure of such information. In light of these commitments and other facts of record, and subject to the condition described below, it has been determined that Bankia has provided adequate assurances of access to any necessary information that the Board may request.

Section 173 of the Dodd-Frank Act amended the IBA to provide that the Board may consider, for a foreign bank that presents a risk to the stability of the United States financial system, whether the home country of the foreign bank has adopted, or is making demonstrable progress toward adopting, an appropriate system of financial regulation for the financial system of such home country to mitigate such risk.[12] Spain has made progress toward adopting a system of financial regulation for its financial system to mitigate the risk to financial stability from its banks. The Bank of Spain and the Spanish government have taken a number of measures to strengthen the overall financial supervisory regime. These measures include supporting the integration of Spanish savings banks into financial groups, adopting legislative measures that increase minimum capital requirements for Spanish financial institutions, and requiring financial institutions to implement their recapitalization plans. The Bank of Spain also established a Financial Stability Department to monitor and analyze financial stability risks and issues in the Spanish and global financial systems and produces an annual Financial Stability Report that includes an assessment of the key macroeconomic and financial market risks in Spain. In addition, Spanish authorities have been actively involved in advancing international financial stability discussions in various fora, including the Organisation for Economic Co-operation and Development, the International Monetary Fund, the Basel Committee on Banking Supervision,

[12] 12 U.S.C. § 3105(d)(3)(E).

and the Financial Stability Board. More recently, Spain actively participated in the G-20 meeting of finance ministers and central bank governors where agreement was reached on a set of guidelines that measure potentially destabilizing imbalances in the global economy as a first step toward making the world less prone to financial crisis.

On the basis of all the facts of record, and subject to the commitments made by Bankia and its parent companies, as well as the terms and conditions set forth in this order, Bankia's application to establish a branch in Miami is hereby approved by the Director of the Division of Banking Supervision and Regulation, with the concurrence of the General Counsel, pursuant to authority delegated by the Board.[13] Should any restrictions on access to information on the operations or activities of Bankia and its affiliates subsequently interfere with the Board's ability to obtain information to determine and enforce compliance by Bankia's or its affiliates with applicable federal statutes, the Board may require termination of any of Bankia or its affiliates' direct or indirect activities in the United States. Approval of this application also is specifically conditioned on compliance by Bankia with the commitments made in connection with this application and with the conditions in this order.[14] The commitments and conditions referred to above are conditions imposed in writing by the Board in connection with this decision and may be enforced in proceedings under 12 U.S.C. § 1818 against Bankia and its affiliates.

By order, approved pursuant to authority delegated by the Board, effective December 16, 2011.

Robert deV. Frierson
Deputy Secretary of the Board

[13] 12 CFR 265.7(d)(12).

[14] The Board's authority to approve the establishment of the proposed branch parallels the continuing authority of the State of Florida to license branches of a foreign bank. The Board's approval of this application does not supplant the authority of the State of Florida or its agent, the Office of Financial Regulation ("OFR"), to license the proposed branch of Bankia in accordance with any terms or conditions that the OFR may impose.

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Legal Developments: First Quarter, 2012

Orders Issued Under Bank Holding Company Act

Order Issued Under Section 3 of the Bank Holding Company Act

Adam Bank Group, Inc.
Tampa, Florida

Order Approving the Acquisition of a Bank
FRB Order No. 2012-3 (March 21, 2012)

Adam Bank Group, Inc. ("ABG"), Tampa, Florida, has requested the Board's approval under section 3 of the Bank Holding Company Act ("BHC Act")[1] to acquire Brazos Valley Bank, National Association ("Bank"), College Station, Texas.

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published (76 *Federal Register* 60837 (2011)). The time for filing comments has expired, and the Board has considered the application and all comments received in light of the factors set forth in section 3 of the BHC Act.

ABG, with total consolidated assets of approximately $935 million, is the 729th largest insured depository organization in the United States, controlling approximately $728 million in deposits.[2] ABG's only subsidiary insured depository institution, American Momentum Bank ("AMB"), Tampa, operates in Florida and Texas.[3] AMB is the 85th largest depository organization in Florida, controlling deposits of approximately $380 million, which represent less than 1 percent of the total amount of deposits of insured depository institutions in the state. AMB is the 305th largest depository organization in Texas, controlling deposits of approximately $118 million, which represent less than 1 percent of the total amount of deposits of insured depository institutions in that state.[4]

Bank, with total assets of approximately $113 million, is the 344th largest insured depository institution in Texas, controlling deposits of approximately $106 million. On consummation of this proposal, ABG would become the 201st largest depository organization in Texas, controlling deposits of approximately $224 million, which represent less than 1 percent of the total amount of deposits of insured depository institutions in the state.

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1 12 U.S.C. § 1842.

2 National deposit, asset, and ranking data are as of December 31, 2011, and are updated to reflect mergers through that date. In this context, insured depository institutions include commercial banks, savings associations, and savings banks.

3 ABG owns 91.6 percent of the voting shares of AMB.

4 State deposit, asset, and ranking data are as of June 30, 2011. The state deposit, asset, and ranking data do not include two acquisitions after June 30 that are reflected in the national deposit, asset and ranking data noted above. *See* note 2. Those acquisitions did not affect competition in Texas and in particular, the Bryan-College Station, Texas banking market.

Interstate Analysis

Section 3(d) of the BHC Act imposes certain requirements on interstate transactions. Section 3(d) generally provides that the Board may approve an application by a bank holding company ("BHC") that is well capitalized and well managed to acquire control of a bank in a state other than the BHC's home state without regard to whether the transaction is prohibited under state law.[5] However, this section further provides that the Board may not approve an application that would permit an out-of-state BHC to acquire a host state's bank that has not been in existence for the lesser of the state statutory minimum period of time or five years.[6] In addition, the Board may not approve an application by a BHC to acquire an insured depository institution if the home state of such insured depository institution is a state other than the home state of the BHC 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.[7]

For purposes of the BHC Act, the home state of ABG is Florida,[8] and Bank is located in Texas.[9] ABG is well capitalized and well managed under applicable law. Texas law imposes a five-year age requirement,[10] and Bank has been in existence for more than five years.

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 $9.6 trillion. On consummation of the proposed transaction, ABG would control less than 1 percent of the total amount of deposits in insured depository institutions in the United States. Accordingly, and in light of all the facts of record, the Board is not required to deny the proposal under section 3(d) of the BHC Act.

Competitive Considerations

Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or would be in furtherance of any attempt to monopolize the business of banking in any relevant banking market. The BHC Act also prohibits the Board from approving a proposed bank acquisition that would substantially lessen competition in any relevant banking market unless the anticompetitive effects of the proposal are clearly outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the community to be served.[11]

AMB and Bank compete directly in the Bryan-College Station, Texas banking market.[12] AMB operates a branch in College Station, which is in Brazos County. Bank's head office is also in College Station. The Board has reviewed the competitive effects of the proposal in this banking market in light of all the facts of record. In particular, the Board has consid-

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5 The standard was changed from adequately capitalized and adequately managed to well capitalized and well managed by section 607(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376, codified at 12 U.S.C § 1842(d)(1)(A).

6 12 U.S.C. § 1842(d)(1)(B).

7 12 U.S.C. § 1842(d)(2)(A).

8 *See* 12 U.S.C. § 1842(d). 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.

9 For purposes of section 3(d) of the BHC Act, the Board considers a bank to be located in the states in which the bank is chartered or headquartered or operates a branch. *See* 12 U.S.C. §§ 1841(o)(4)–(7) and 1842(d)(1)(A) and 1842(d)(2)(B).

10 Tex Fi. Code Ann. § 202.003.

11 12 U.S.C. § 1842(c)(1).

12 The Bryan-College Station, Texas banking market is defined as Brazos County, Texas.

ered the number of competitors that would remain in the banking market; the relative shares of total deposits in insured depository institutions in the market ("market deposits") controlled by AMB and Bank;[13] the concentration level of market deposits and the increase in those levels, as measured by the Herfindahl-Hirschman Index ("HHI") under the Department of Justice Merger Competitive Review Guidelines ("DOJ Bank Merger Guidelines");[14] and other characteristics of the market.

Consummation of the proposal would be consistent with Board precedent and within the thresholds in the DOJ Bank Merger Guidelines in the Bryan-College Station banking market. On consummation, the HHI measure of concentration would increase by 26 points to 1041. The appropriate banking agencies have been afforded an opportunity to comment and have not objected to the proposal.[15]

Based on all the facts of record, the Board has concluded that consummation of the proposal would not have a significantly adverse effect on competition or on the concentration of resources in the banking market where the subsidiary depository institutions of AMB and Bank compete directly or in any other relevant banking market. Accordingly, the Board has determined that competitive considerations are consistent with approval.

Other Section 3(c) Considerations

Section 3(c) of the BHC Act requires the Board to take into consideration the following factors in acting on bank acquisition applications: the financial and managerial resources (including consideration of the competence, experience, and integrity of the officers, directors, and principal shareholders) and future prospects of the company and banks concerned; the effectiveness of the company in combatting money laundering; the convenience and needs of the community to be served; and the extent to which the proposal would result in greater or more concentrated risks to the stability of the United States banking or financial system. The Board has considered all of these factors and, as described below, has determined that they are consistent with approval of the application. The review was conducted in light of all the facts of record, including supervisory and examination information from various U.S. banking supervisors of the institutions involved, publicly reported and other financial information, and information provided by ABG.

[13] Deposit and market share data are as of June 30, 2011, adjusted to reflect mergers and acquisitions through June 30 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).

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

[15] In the Bryan-College Station banking market, AMB controls $118 million in deposits, representing 4.2 percent of total deposits in the market, and Bank controls $105.6 million in deposits, representing 3.7 percent of total deposits in the market. On consummation, ABG would control $223.6 million in deposits, representing 7.9 percent of total market deposits.

A. Financial, Managerial, and Other Supervisory Considerations

In evaluating financial factors in expansionary proposals by banking organizations, the Board reviews the financial condition of the organizations involved on both a parent-only and consolidated basis, as well as the financial condition of the subsidiary depository institutions and the organizations' significant nonbanking operations. In this evaluation, the Board considers a variety of information, including capital adequacy, asset quality, and earnings performance. The Board evaluates the financial condition of the 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 costs 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.

ABG and AMB are well capitalized and will remain so on consummation of the proposed acquisition. ABG is a shell entity, and AMB comprises 99.8 percent of its consolidated assets. The proposed transaction is a bank merger, structured as a cash purchase of shares. AMB will fund the purchase from existing liquidity. AMB has been in operation since October 2006, and achieved profitable operations for fiscal years ending 2010 and 2011. AMB successfully integrated two failed bank acquisitions during July 2011, acquiring assets and deposit liabilities of approximately $297 million. On a pro forma basis, the acquisition of Bank would not have a significant impact on AMB's operations. Based on its review of the record, the Board finds that the organization has sufficient financial resources to effect the proposal.

The Board also has considered the managerial resources of the organizations involved and of the proposed combined organization. The Board has reviewed the examination records of ABG, AMB, and Bank, including assessments of their management, risk-management systems, and operations. In addition, the Board has considered its supervisory experiences and those of other relevant bank supervisory agencies with the organizations and their records of compliance with applicable banking and anti-money-laundering laws. The Board also has considered ABG's plans for implementing the proposal.

ABG and AMB are considered to be well managed. The boards and senior management of ABG and AMB[16] have significant community banking experience. In addition, the chairman of AMB has a successful record of acquiring and integrating the operations of troubled depository institutions into a larger profitable institution in a safe and sound matter. As noted above, AMB purchased two failed banks in July 2011 that are now part of the ABG organization.

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

B. Convenience and Needs Considerations

Under section 3, the Board must consider the effects of the proposal on the convenience and needs of the communities to be served and take into account the records of the relevant depository institutions under the Community Reinvestment Act ("CRA").[17] The CRA requires federal financial supervisory agencies to encourage insured depository insti-

[16] The pro forma management of the organization will be the same as the current management of ABG and AMB.

[17] 12 U.S.C. § 1842(c)(2); 12 U.S.C. § 2901 *et seq.*

tutions to help meet the credit needs of the local communities in which they operate, consistent with their safe and sound operation,[18] 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.[19]

The Board has considered all the facts of record, including evaluations of the CRA performance of AMB and Bank, data reported by AMB under the Home Mortgage Disclosure Act ("HMDA"),[20] other information provided by ABG, confidential supervisory information, and public comment received on the proposal. A commenter criticized the performance of AMB in meeting the credit needs of LMI and minority borrowers and of residents in predominately minority areas. The commenter asserted that from 2007 to 2009, no mortgage loans were made to low-income borrowers and that only one was made to a moderate-income borrower. The commenter further stated that AMB did not receive any mortgage applications from minority borrowers and originated only one mortgage loan in a predominately minority census tract for that period. The commenter also criticized the bank's branch distribution in low-income and minority areas.

In evaluating this proposal, the Board also consulted with the Federal Deposit Insurance Corporation ("FDIC") on its supervisory experience with AMB, including AMB's lending performance, and the FDIC's review of a substantially similar comment that it received in connection with a merger application from AMB. In addition, the Board has considered the convenience and needs factor as provided in the CRA in light of examinations by the appropriate federal supervisors of the CRA performance records of the relevant institutions.[21] 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. AMB received a "satisfactory" rating at its most recent CRA performance evaluation by the FDIC, as of October 24, 2008, and Bank received a "satisfactory" rating at its most recent CRA performance evaluation by the Office of the Comptroller of the Currency, as of January 22, 2007.

In addition, the Board has considered the HMDA data for 2009 and 2010 reported by AMB in Brazos County, Texas,[22] and has considered the fair lending record of AMB. The Board also has reviewed supervisory information and consulted with the FDIC. The HMDA data show that AMB's mortgage lending is limited.[23] According to the data, AMB made no loans to minorities during this period. ABG stated that during the severe economic downturn in Florida, AMB sought other financing opportunities, such as community development loans to meet the lending needs of the market. ABG stated that AMB has taken a cautious approach to expanding its branch network to maintain a strong focus on safety and soundness. ABG also noted that the bank's most recently established branch is in a moderate-income tract in Clearwater.

[18] 12 U.S.C. § 2901(b).

[19] 12 U.S.C. § 2903.

[20] 12 U.S.C. § 2801 et seq.

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

[22] The Board considered the HMDA data reported by AMB for Brazos County because all the bank's HMDA originations during this period were in Texas and that is the location of its Texas branch.

[23] AMB indicated that, in addition to AMB's HMDA-reportable lending, the bank received 23 requests for mortgage loans that were referred to and closed by its correspondent lenders. ABG reported that approximately $508,000 of these loans were for properties in moderate-income areas.

Because of the limitations of HMDA data, the Board has considered other kinds of lending efforts by AMB.[24] For example, AMB has provided more than $58 million in financing to developers who build and operate affordable housing. The bank supported one project that included 53 affordable 1-4 family homes in a low to moderate income, predominantly minority neighborhood. AMB has sought out additional community development lending opportunities and has provided financing for the acquisition/development/rehabilitation of multifamily affordable housing projects totaling $160.8 million, including $66.1 million in loans for properties in low-to-moderate income areas. AMB has provided $68.3 million in loans in the communities of Bryan and College Station for the construction of single family homes. Of this total, $4.8 million was in low-to-moderate income census tracts and 59 percent were affordable homes qualifying for low down payments or the First Time Homebuyer's Program.

Although AMB is currently not a significant HMDA lender, it is beginning efforts to increase its home mortgage lending in Florida and Texas. ABG recently hired a senior mortgage production expert who has begun development of a comprehensive real estate lending initiative for Florida and Texas.

AMB has in place a formal fair lending program that includes its home mortgage and small business lending operations. AMB also provides internal compliance training, and the bank's staffs in bank management, line-of-business, and compliance attend outside conferences and seminars and other fair lending and consumer protection training sessions.

The Board also considered the location of AMB's branches. Two of the bank's twenty-one branches are in moderate-income tracts, and one of these is in a minority tract. ABG asserts that the bank placed its branches in downtown areas with large workforce populations, in shopping areas that attract people from throughout the market, and on major thoroughfares.

The credit needs of Bank's communities will benefit from AMB's financial strength, and the proposed acquisition will provide Bank's customers with a more viable source of banking services. ABG plans to continue to offer Bank's products and to replace any discontinued products and services with similar offerings by AMB.

The Board has considered all the facts of record, including reports of examination of the CRA records of AMB and Bank, information provided by ABG, public comments received on the proposal, and confidential supervisory information, including current records of compliance with consumer laws and regulations.

Based on a review of the entire record, and for the reasons discussed above, the Board has concluded that considerations relating to the convenience and needs factor and the CRA performance records of the relevant insured depository institutions are consistent with approval.

[24] Although the HMDA data may reflect disparities in the rates of loan applications, originations, and denials among members of different racial or ethnic groups in certain local areas, they provide an insufficient basis by themselves on which to conclude whether or not AMB is excluding any group on a prohibited basis. The Board recognizes that HMDA data alone, even with the recent addition of pricing information, provide only limited information about the covered loans. HMDA data, therefore, have limitations that make them an inadequate basis, absent other information, for concluding that an institution has engaged in illegal lending discrimination.

The Board is nevertheless concerned when HMDA data for an institution indicate disparities in lending and believes that all lending institutions are obligated to ensure that their lending practices are based on criteria that ensure not only safe and sound lending but also equal access to credit by creditworthy applicants regardless of their race or ethnicity. Moreover, the Board believes that all bank holding companies and their affiliates must conduct their mortgage lending operations without any abusive lending practices and in compliance with all consumer protection laws.

C. Financial Stability

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

Based on all the facts of record, including those described above, the Board has determined that all of the factors it must consider under section 3(c) of the BHC Act 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 BHC Act and other applicable statutes. The Board's approval is specifically conditioned on compliance by ABG with all the conditions imposed in this order and the commitments made to the Board in connection with the application, including receipt of all required regulatory approvals. For purposes of this action, the conditions and commitments are deemed to be conditions imposed in writing by the Board in connection with its findings and decision herein and, as such, may be enforced in proceedings under applicable law.

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

By order of the Board of Governors, effective March 21, 2012.

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

Jennifer J. Johnson
Secretary of the Board

Orders Issued Under Section 4 of the Bank Holding Company Act

Capital One Financial Corporation
McLean, Virginia

Order Approving the Acquisition of a Savings Association and Nonbanking Subsidiaries
FRB Order No. 2012-2 (February 14, 2012)

Capital One Financial Corporation ("Capital One"), 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 Act and section 225.24 of the Board's Regulation Y[1] to acquire ING Bank, fsb ("FSB"), Wilmington, Delaware, and thereby

[1] 12 U.S.C. §§ 1843(c)(8) and (j); 12 CFR 225.24.

indirectly acquire ShareBuilder Advisors, LLC (“ShareBuilder”) and ING Direct Investing, Inc. (“IDII”), both of Seattle, Washington.[2]

Capital One, with total consolidated assets of approximately $200 billion, is the 24th largest depository organization in the United States measured by asset size. Capital One is the eighth largest depository organization in the United States measured by deposits, controlling deposits of approximately $127 billion, which represents approximately 1.4 percent of the total amount of deposits of insured depository institutions in the United States.[3] Capital One controls two insured depository institutions, Capital One, National Association (“CONA”), McLean, Virginia, and Capital One Bank (USA), National Association (“COBNA”), Glen Allen, Virginia, that operate in eight states and the District of Columbia.[4]

FSB, with total consolidated assets of approximately $92 billion, is the 17th largest depository organization in the United States measured by deposits, controlling deposits of approximately $82 billion, which represents less than 1 percent of the total amount of deposits of insured depository institutions in the United States. FSB’s only banking office is in Delaware, but FSB solicits business and operates nationwide primarily through the Internet.[5]

On consummation of the proposal, Capital One would become the fifth largest depository organization in the United States by deposit size, with consolidated deposits of approximately $210 billion, representing approximately 2.3 percent of the total amount of deposits of insured depository institutions in the United States. Capital One would become the 20th largest depository organization in the United States by asset size, with total consolidated assets of approximately $292 billion.

Public Comment on the Proposal

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published in the *Federal Register* (76 *Federal Register* 44,008 (July 22, 2011) and 76 *Federal Register* 54,770 (September 2, 2011)), and the time for filing comments has expired. The Board extended the initial period for public comment to accommodate the broad public interest in this proposal, providing interested persons more than 85 days to submit written comments.

Because of the extensive public interest in the proposal, the Board held public meetings in Washington, D.C., Chicago, Illinois, and San Francisco, California, to provide interested persons an opportunity to present oral testimony on the factors that the Board must review under the BHC Act.[6] Approximately 235 people testified at the public meetings, and many of the commenters who testified also submitted written comments.

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[2] FSB is owned by ING Groep N.V. (“ING Groep”), Amsterdam, The Netherlands. In 2008 and 2009, the government of The Netherlands provided ING Groep a guarantee of some of ING Groep’s assets, including certain U.S. assets of FSB. Under this proposal, Capital One would not acquire any FSB assets that are subject to the guarantee of the Dutch government.

[3] Asset and nationwide deposit ranking data are as of September 30, 2011. In this context, insured depository institutions include commercial banks, savings banks, and savings associations.

[4] CONA is Capital One’s largest subsidiary depository institution as measured by both assets and deposits. COBNA primarily offers credit and debit card products in addition to deposit products.

[5] FSB operates eight cafés in the United States that are marketing offices of FSB and do not meet the definition of “branch” under the regulations of the Office of Thrift Supervision (“OTS”) and Office of the Comptroller of the Currency (“OCC”). *See* 76 *Federal Register* 48,999 (August 9, 2011), to be codified at 12 CFR 145.92.

[6] The Board held the Washington public meeting on September 20, 2011, the Chicago public meeting on September 27, 2011, and the San Francisco public meeting on October 5, 2011. Several commenters requested that the Board further extend the comment period and hold additional public meetings in New York City, Los Angeles,

In total, approximately 915 individuals and organizations submitted comments on the proposal through oral testimony, written comments, or both. Commenters included members of Congress, state legislators, community groups, nonprofit organizations, customers of Capital One or FSB, and other interested organizations and individuals.

A large number of commenters supported the proposal. Many of the commenters in support of the proposal commended Capital One for its commitment to local communities and described favorable experiences with the small business, community development, and affordable mortgage programs of the organization. Commenters also praised the willingness of Capital One to provide products and services under the Community Reinvestment Act ("CRA"),[7] such as affordable mortgage products, educational seminars, and funds to support community development activities. In addition, commenters praised Capital One's charitable contributions and noted that Capital One officers and employees frequently provide valuable services to community organizations as board members and volunteers.

A significant number of commenters opposed the proposal, requested that the Board only approve the proposal subject to certain conditions, or expressed concerns about the proposal.[8] Many commenters expressed concern about the impact of the proposal on the financial stability of the U.S. banking or financial system. Commenters also expressed their belief that, if approved by the Board, Capital One's acquisition of FSB would result in adverse effects that would outweigh the public benefits provided by the proposal.

A significant number of commenters criticized the performance of Capital One and FSB under the CRA. Some of the commenters criticized the compliance records of the mortgage lending operations of Capital One and FSB and expressed concern about their records of lending to minorities. Commenters also criticized Capital One's performance record of lending to small businesses and the record of its credit card lending operations. In addition, commenters expressed concern about the impact of the acquisition on Capital One's commitment to CRA-related initiatives and its future performance under the CRA. Commenters also noted concern about Capital One's proposed acquisition of credit card assets from subsidiaries of HSBC Holdings plc ("HSBC"), London, United Kingdom, and requested that the Board review the two proposals together or require an application from Capital One to acquire those assets, to ensure that the HSBC proposal is taken into consideration in connection with the review of the CRA, financial stability, and other factors related to the FSB proposal.[9]

In evaluating the statutory factors under the BHC Act, the Board considered the information and views presented by all commenters, including the testimony at the public meetings and in the written submissions.[10] The Board also considered all the information presented

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Atlanta, New Orleans, and other communities. The Board believes that holding public meetings in Washington, Chicago, and San Francisco, as well as providing all commenters an extended period to submit written comments, provided sufficient opportunity for interested persons to provide relevant information to the Board. The three public meetings were distributed across the United States, and as noted above, the written comment period exceeded 85 days.

7 12 U.S.C. § 2901 *et seq.*

8 Approximately 425 comments were submitted in the form of substantially identical letters.

9 Capital One has applied to the OCC for approval under the Bank Merger Act to acquire various assets from HSBC. The OCC is required to take into consideration the same factors that are reviewed by the Board under the BHC Act, including the effects of the acquisition on financial stability and on the convenience and needs of the community to be served. 12 U.S.C. § 1828(c)(5). Although Capital One is not required by law to apply for approval by the Federal Reserve to acquire the HSBC assets, Capital One has provided information to the Board regarding the proposed acquisition of HSBC's assets. The Board has taken this information into account for purposes of its review of the factors it must consider with respect to Capital One's notice to acquire FSB.

10 One commenter expressed concern about ex parte communications and the opportunity for the public to rebut all information that was provided by Capital One. On review, the Board found that the public had a full opportunity to provide the Board with any information related to the factors that the Board must consider in acting

in the notice and supplemental filings by Capital One; various reports filed by the relevant companies; publicly available information; and other information and reports. In addition, the Board reviewed confidential supervisory information, including examination reports on the depository institution holding companies and the depository institutions involved and information provided by other federal financial supervisory agencies, the Department of Housing and Urban Development ("HUD"), and the Department of Justice ("DOJ"). After a review of all the facts of record, and for the reasons discussed in this order, the Board has concluded that the statutory factors it is required to consider under the BHC Act are consistent with approval of the proposal.

Factors Governing Board Review of the Transaction

The Board previously has determined by regulation that the operation of a savings association by a bank holding company and the other nonbanking activities for which Capital One has requested approval are closely related to banking for purposes of section 4(c)(8) of the BHC Act.[11] The Board requires that savings associations acquired by bank holding companies or financial holding companies conform their direct and indirect activities to those permissible for bank holding companies under section 4(c)(8) of the act.[12] Capital One has committed that all the activities of FSB and the other nonbanking subsidiaries of FSB that it proposes to acquire will conform to those activities that are permissible under section 4 of the BHC Act and Regulation Y.

Section 4(j)(2)(A) of the BHC Act requires the Board to consider whether the proposed acquisition of FSB and its nonbanking subsidiaries "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."[13] 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, and the public benefits of the proposal.[14] In acting on a notice to acquire a savings association, the Board reviews the records of performance of the relevant insured depository institutions under the CRA. In cases involving the interstate acquisition of an insured depository institution under section 4(c)(8) of the BHC Act, the Board must also consider the concentration of deposits on a nationwide basis.[15]

Interstate and Deposit Cap Analyses

The Dodd-Frank Act amended section 4 of the BHC Act to provide that, in general, the Board may not approve an application by a bank holding company to acquire an insured

on the notice. The information submitted by Capital One, and the release of that information to the public, was in accordance with the Board's regulations and policies. The Board confirmed that all contacts between Capital One and staff were in accordance with the Board's rules on ex parte communications.

[11] 12 CFR 225.28(b)(4), (6), and (7).

[12] A savings association operated by a bank holding company may engage only in activities that are permissible for bank holding companies under section 4(c)(8) of the BHC Act. 12 CFR 225.28(b)(4).

[13] 12 U.S.C. § 1843(j)(2)(A). Section 604(e) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Pub. L. No. 111–203, 124 Stat. 1601 (2010), ("Dodd-Frank Act") added the "risk to the stability of the United States banking or financial system" to the list of possible adverse effects.

[14] *See* 12 CFR 225.26; *see, e.g.*, *Bank of America Corporation/Countrywide*, 94 *Federal Reserve Bulletin* C81 (2008) ("Bank of America Order"); *Wachovia Corporation*, 92 *Federal Reserve Bulletin* C138 (2006); *BancOne Corporation*, 83 *Federal Reserve Bulletin* 602 (1997).

[15] 12 U.S.C. § 1843(i)(8).

depository institution if the home state of the insured depository institution is a state other than the home state of the bank holding company, 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 ("nationwide deposit cap").[16] The intended purpose of the nationwide deposit cap was to help guard against undue concentrations of economic power.[17] For purposes of the BHC Act, the home state of Capital One is Virginia, and the home state of FSB is Delaware.[18]

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 $8.9 trillion.[19] On consummation of the proposed transaction, Capital One would control approximately 2.3 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 proposal under section 4(i) of the BHC Act.

Competitive Considerations

As part of the Board's consideration of the factors under section 4 of the BHC Act, the Board has considered the competitive effects of Capital One's acquisition of FSB and its nonbanking subsidiaries, in light of all the facts of record. Capital One's subsidiary banks and FSB's deposit-taking and lending operations are located in different banking markets. Based on all the facts of record, including the differences in business models, products, and methods for providing services to consumers, the Board has concluded that the acquisition by Capital One of FSB's deposit-taking and lending operations would not result in any significant adverse effect on competition in any relevant banking market.

The Board also has considered the competitive effects of Capital One's proposed acquisition of FSB's other nonbanking subsidiaries and activities in light of all the facts of record.[20] Capital One and FSB both engage in investment advisory and securities broker-

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

[17] Fleet Order at 219.

[18] 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 federal savings association, the home state is the state in which the home office of the savings association is located. 12 U.S.C. § 1841(o)(4)(E).

[19] *See* Fleet Order at 219. Deposit data are calculated based on reports filed by insured depository institutions and are as of September 30, 2011. Each bank 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(*l*), on the institution's Consolidated Report of Condition and Income. Each insured savings association similarly must report its total deposits on the institution's Thrift Financial Report. 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.

[20] Under the 2010 Horizontal Merger Guidelines ("Guidelines") issued by the DOJ and the Federal Trade Commission, the post merger level of market concentration and the change in concentration resulting from a merger are important factors in evaluating the effect of the merger on competition. Market shares alone may not fully reflect the competitive significance of firms in the market or the impact of a merger and are used in conjunction with other evidence of competitive effects.

The Guidelines use the Herfindahl-Hirschman Index ("HHI") as a measure of concentration. For mergers that do not involve banks, the Guidelines state that mergers resulting in unconcentrated markets are unlikely to have adverse competitive effects and ordinarily require no further analysis. The Guidelines also state that mergers involving an increase in the HHI of less than 100 points are unlikely to have adverse competitive effects and ordinarily require no further analysis. Press Release, Department of Justice, August 19, 2010, www.justice.gov/opa/pr/2010/August/10-at-938.html.

age services through subsidiaries that are registered broker-dealers.[21] The Board previously has determined that these activities are permissible for bank holding companies.[22]

Capital One and FSB compete in the securities brokerage business.[23] The Board previously has determined that the geographic market for securities brokerage is either regional or national in scope.[24] On consummation of the proposal, the securities brokerage market would remain unconcentrated, and numerous competitors would continue to engage in the securities brokerage business.

Capital One and FSB also compete in the investment advisory business.[25] The Board previously has determined that the geographic market for investment advisory services is either regional or national in scope.[26] The record in this case indicates that there are numerous competitors that would continue to engage in the investment advisory business on consummation of the proposal and that Capital One's and FSB's levels of participation are relatively small.

Based on all the facts of record, the Board concludes that consummation of the proposed transaction would not have a significantly adverse effect on competition or on the concentration of resources in any relevant banking or nonbanking activities market and is consistent with approval.

Financial and Managerial Resources

The Board considered the financial and managerial resources of Capital One, FSB, and their subsidiaries and the effect of the transaction on those resources, in light of confidential reports of examination, other supervisory information from the primary federal supervisor of the organizations involved in the proposal, publicly reported and other financial information, information provided by Capital One and FSB, and other relevant information. The Board also consulted with the OCC as the primary federal supervisor of Capital One's subsidiary depository institutions and FSB.

In addition, the Board considered the public comments that relate to these factors. As noted above, the Board received a number of comments requesting that it consider the current proposal in light of Capital One's proposed acquisition of assets from subsidiaries of HSBC. Commenters asserted that these proposals represent unsound banking practices

[21] Although both Capital One and FSB currently own insurance subsidiaries, FSB's insurance subsidiary, ING Direct Insurance Agency, LLC, is inactive and did not engage in any sales activity in 2010 or 2011. Accordingly, there is no overlap in competition between Capital One and FSB in providing insurance services.

[22] *See* 12 CFR 225.28(b)(7).

[23] Capital One has two registered broker-dealers: Capital One Southcoast, Inc., which is a full-service investment banking firm that provides corporate finance, equity research, and institutional equity sales and trading services; and Capital One Investment Services LLC, which offers services to retail investors. FSB owns IDII, which is an Internet-based broker-dealer that provides brokerage services to retail investors and employer-sponsored 401(k) plans.

[24] *See* Bank of America Order at C86; *Allied Irish Banks, p.l.c.*, 94 *Federal Reserve Bulletin* C11 (2007); *Wachovia Corporation*, 92 *Federal Reserve Bulletin* C183 (2006); *Marshall & Ilsley Corporation*, 92 *Federal Reserve Bulletin* C121 (2006); *Wells Fargo & Company*, 88 *Federal Reserve Bulletin* 103 (2002); and *NationsBank Corporation*, 84 *Federal Reserve Bulletin* 858 (1998).

[25] Capital One has two registered investment advisors: Capital One Financial Advisors, which distributes third-party investment management products through Capital One's branch network; and Capital One Asset Management, which provides investment advisory services to certain clients of CONA. FSB indirectly owns ShareBuilder, a registered investment advisor that creates exchange-traded funds for consideration by retail brokerage customers of IDII. ShareBuilder does not offer personalized investment advice.

[26] *See Marshall & Ilsley Corporation*, 92 *Federal Reserve Bulletin* C121 (2006); *SunTrust Banks, Inc.*, 90 *Federal Reserve Bulletin* 533 (2004); and *Fifth Third Bancorp*, 87 *Federal Reserve Bulletin* 330 (2001).

that would allow Capital One to acquire high-cost deposits from FSB to fund the origination and acquisition of subprime credit card assets.

In evaluating financial resources in expansionary proposals by banking organizations, the Board reviews the financial condition of the organizations involved on both a parent-only and consolidated basis, as well as the financial condition of the subsidiary insured depository institutions and the organizations' significant nonbanking operations. In this evaluation, the Board considers a variety of information, including capital adequacy, asset quality, and earnings performance. In assessing financial factors, the Board consistently has considered capital adequacy to be especially important. The Board evaluates the financial condition of the combined organization at consummation, 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 costs of the proposal and the proposed integration of the operations of the institutions.

The Board has considered the financial factors of the proposal. Capital One's regulatory capital ratios are well above the minimums required of well-capitalized bank holding companies and would remain so on consummation of the proposal. Capital One's subsidiary depository institutions and FSB also are well capitalized and would remain so after consummation. The proposed transaction is structured as a cash and share exchange. Capital One would acquire FSB from ING Groep in exchange for approximately $6.2 billion in cash and 55.9 million Capital One common shares, valued at approximately $2.8 billion.[27] Capital One represented that the cash portion of the purchase price of FSB would be funded with the proceeds from the sale of $2 billion of additional shares and the issuance of $3 billion of senior unsecured debt,[28] with the remaining $1.2 billion to be funded from available cash resources. This transaction would not materially increase the debt service requirements of the combined company.[29] Asset quality and earnings prospects also are consistent with approval.[30]

The Board also has considered the managerial resources of the organizations involved and the proposed combined organization. The Board has reviewed the examination records of Capital One, its subsidiary depository institutions, and FSB, including assessments of their management expertise, internal controls, risk management systems, and operations. In

[27] The Capital One common shares to be acquired by ING Groep represent approximately 9.6 percent of Capital One's voting shares. One commenter asserted that ING Groep must file an application for control of more than 4.9 percent of Capital One's voting stock. The commenter also argued that ING Groep would control Capital One by virtue of its ownership of up to 9.9 percent of Capital One's voting shares. These assertions are not legally correct in this case. As a result of the proposal, ING Groep would no longer control a savings association and, consequently, would no longer be a regulated savings and loan holding company or bank holding company. As such, ING Groep would not require the Board's approval to acquire up to 9.9 percent of the voting stock of Capital One. In addition, the Board has determined in a separate action that ING Groep would not control Capital One as a result of this proposal. *See* Board letter to Mark Menting, Esq. (February 14, 2012).

[28] In July 2011, Capital One entered into forward sale agreements totaling $2 billion in connection with a public offering of 40 million common shares. Also in July 2011, Capital One closed a public offering of $3 billion of senior unsecured notes. Capital One represented that it expects to use the proceeds of the forward sale agreements and the debt offering to fund the proposed acquisition of FSB.

[29] In reviewing the financial factors in this case, the Board has taken account of Capital One's plan to acquire certain assets from HSBC and to fund the acquisition of HSBC assets primarily with cash and the proceeds from the repositioning of FSB's balance sheet. In addition, Capital One expects to issue additional equity, including up to $750 million in equity that Capital One has the option to issue to HSBC.

[30] Several commenters expressed concern that Capital One's asset portfolio is highly concentrated in credit cards, including a substantial amount of subprime credit card assets. The Board believes that Capital One has the financial and managerial resources to manage its asset portfolio. Capital One lends across a full spectrum of borrowers, and its overall business is diversified. Capital One has substantially decreased its reliance on credit card revenue since 2005. Currently, credit card loans represent approximately 48 percent of Capital One's loan portfolio and approximately 28 percent of the company's total assets.

addition, the Board has considered its supervisory experiences and those of other relevant financial supervisory agencies with the organizations and the organizations' records of compliance with applicable banking laws and with anti-money-laundering ("AML") laws.[31]

Capital One and its subsidiary depository institutions are considered to be well managed. Capital One has a demonstrated record of successfully integrating large organizations into its operations and risk-management systems following acquisitions, including its integrations of Hibernia Corporation in 2005, North Fork Bancorporation in 2006, and Chevy Chase Bank in 2009. Capital One is devoting significant financial and other resources to address all aspects of the post-acquisition integration process for this proposal. Capital One would implement its risk-management policies, procedures, and controls at the combined organization. In addition, Capital One's management has the experience and resources to ensure that the combined organization operates in a safe and sound manner.

The Board also has considered comments that allege weaknesses in Capital One's compliance management as it relates to consumer protection practices. Commenters criticized Capital One for attempting to collect credit card debts from customers whose debts previously had been discharged in bankruptcy,[32] not complying with laws governing repossession of automobiles,[33] not following state and federal laws that protect exempt income from debt collection,[34] and failing to comply with fair lending laws, among other matters.[35]

The Board believes that it is appropriate in connection with the acquisition of FSB for Capital One to enhance its risk-management systems and policies to account for the size, complexity, and diversification of the business lines that would result from the acquisition of FSB. To ensure minimal disruption to FSB's customers and maintain focus on risk management during the integration, Capital One has committed that it will ensure the adequate completion of the integration of FSB as well as the HSBC portfolio, referenced above, in a timely manner consistent with supervisory expectations.

In addition, the Board expects that Capital One will ensure that its risk management framework and methodologies, including its compliance functions, are commensurate with its new size and complexity. The various consumer complaints and legal actions against Capital One referenced in this order suggest that Capital One's processes and procedures for

[31] One commenter contended that ING Groep and FSB are being reviewed by U.S. authorities, including the DOJ, for possible violations of AML and economic sanctions laws. ING Groep has represented that these reviews focus on ING Bank N.V., Amsterdam. Capital One represented that it plans to integrate its corporate compliance program at FSB and each of its subsidiaries, that it has begun to engage in full assessments of FSB's AML and economic sanctions programs in order to immediately manage compliance by Capital One and FSB at consummation, and that it plans to integrate the organizations' different compliance processes over time.

[32] In early 2007, Capital One determined that it had inadvertently filed proofs of claim on discharged debts. Capital One cooperated with a U.S. bankruptcy trustee's investigation and, pursuant to a November 2008 consent order, retained an independent auditor to oversee a review of its proofs of claim to determine whether Capital One had filed claims on previously discharged debts. Capital One addressed this issue by retaining an outside vendor to perform an additional review in advance of any filing of a claim by Capital One. Capital One represented that the court-mandated auditor has revealed that the error rate in filing proofs of claim dropped significantly after the outside vendor was retained. Capital One paid $2.35 million in restitution to affected customers. The Federal Reserve will use the supervisory and examination process to ensure the effectiveness of the debt collection practices and programs adopted by Capital One.

[33] Capital One has settled several class action lawsuits regarding its automobile repossession practices prior to 2008. Capital One corrected errors in its automobile finance processing systems in 2008 by fully integrating systems from its acquisitions of Hibernia Corporation and North Fork Bancorporation.

[34] Capital One represented that in mid-2011, a small number of depositors had been improperly subjected to garnishment orders requested by Capital One. Capital One subsequently took corrective steps to provide remediation to the depositors and to implement new processes and controls to prevent improper garnishment requests.

[35] Comments relating to fair lending compliance are discussed in *Other Considerations, infra*.

enterprise-wide compliance transaction testing could be improved. Accordingly, the Board conditions its decision on Capital One augmenting these processes and procedures by adopting a plan within 90 days acceptable to the Federal Reserve Bank of Richmond that specifies the areas in which transaction testing will be conducted, the type of testing appropriate for each area, and an appropriate sampling methodology; addresses the frequency and scope of compliance transaction testing; provides for periodic reporting to management and the Audit and Risk Committee of the board of directors; provides for improved employee training; and includes requirements for at least an annual review by internal audit of the testing implementation for at least the next three years. Compliance with this condition will be monitored as part of the supervisory process.

Based on all the facts of record, including a review of the comments received, and in reliance on the commitments and conditions discussed above, the Board has concluded that considerations relating to the financial and managerial resources of the organizations involved in the proposal are consistent with approval under section 4 of the BHC Act.

Records of Performance Under the CRA

As noted previously, the Board reviews the records of performance under the CRA of the relevant insured depository institutions when acting on a notice to acquire any insured depository institution, including a savings association.[36] 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,[37] 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.[38]

The Board has considered all the facts of record, including reports of examination of the CRA performance records of Capital One's subsidiary banks and of FSB, data reported by Capital One and FSB under the CRA and the Home Mortgage Disclosure Act ("HMDA"),[39] other information provided by Capital One, confidential supervisory information, and public comments received on the proposal. As noted above, the Board held three public meetings to allow interested members of the public an opportunity to provide oral testimony regarding the proposal in addition to having the opportunity to submit written information and views. As a result of the meetings and through the course of the public comment period, the Board received approximately 915 comments.

Approximately 340 individuals, organizations, and businesses submitted comments or testified in support of the proposal. These commenters generally commended Capital One's record of performance under the CRA, particularly its support for community development and small business programs, through loans, investments and grants, donated space, and corporate volunteers; its business education programs to small business owners, including in LMI communities; its development of affordable home purchase loans for borrowers in LMI communities; and its other programs.

Approximately 575 other individuals and groups expressed concern in their comments and testimony about the mortgage, small business, and consumer lending records of Capital

[36] 12 U.S.C. § 2901 *et seq.*
[37] 12 U.S.C. § 2901(b).
[38] 12 U.S.C. § 2903.
[39] 12 U.S.C. § 2801 *et seq.*

One and FSB; Capital One's ability to satisfy its CRA obligations after consummation of the proposal; or related matters.[40] Among the criticisms made by commenters were that:

- Capital One has not engaged in an adequate amount of home mortgage lending to LMI and minority borrowers.
- Capital One has failed to meet the community development and small business needs in communities served by banks that Capital One previously acquired. Some of these commenters asserted that Capital One had reduced its small business loans in various communities and replaced affordable loans to small businesses with higher-cost credit cards.
- Capital One's lending in California, especially to minority- and women owned businesses, has been inadequate.
- Capital One and FSB have been inconsistent in making branches and services available to LMI communities.
- FSB's record of lending to LMI and minority borrowers and FSB's café locations have disproportionately excluded LMI consumers.[41]

A. CRA Performance Evaluations

As provided in the CRA, the Board has evaluated the proposal in light of the examinations by the appropriate federal supervisors of the CRA 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.[42]

Capital One's lead bank, CONA, received an "outstanding" rating at its most recent CRA performance evaluation by the OCC, as of April 4, 2011 ("CONA Evaluation). COBNA received a "satisfactory" rating at its most recent CRA performance evaluation by the OCC, as of April 4, 2011 ("COBNA Evaluation").[43]

FSB received an "outstanding" rating at its most recent CRA performance evaluation by the OTS, as of August 6, 2008 ("FSB Evaluation").[44] Capital One has represented that it will institute elements of the community development and community investment policies of CONA and COBNA at FSB to strengthen FSB's ability to meet the banking needs of the communities it serves.[45]

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[40] Many commenters urged the Board to require Capital One to provide specific pledges or plans, or to take certain future actions, or asked the Board to condition its approval on a commitment by Capital One to provide loans or investments to specific communities. The Board focuses on the existing CRA performance record of an applicant and the programs that an applicant has in place to serve the credit needs of its assessment areas at the time the Board reviews a proposal. *See* Bank of America Order at C87.

[41] Two commenters also asserted that FSB personnel cash checks and otherwise perform activities that qualify those cafés as branches of FSB. Capital One has represented that café personnel currently do not cash checks or accept deposits, and, consequently, that these cafés are not branches of FSB under the Home Owners' Loan Act ("HOLA"), 12 U.S.C. § 1461 *et seq.*, and were not included in the OTS analysis of FSB's record under the CRA. Four of the cafés are in LMI census tracts, one is in a middle income tract, and three are in upper-income tracts. Capital One has represented that it intends to add deposit-taking ATMs at FSB's cafés and expand its CRA assessment areas to include the relevant communities served by these cafés.

[42] *See Interagency Questions and Answers Regarding Community Reinvestment*, 66 *Federal Register* 11,642 at 11,665 (2010).

[43] The period for the CONA Evaluation was January 1, 2007, through December 31, 2010. COBNA is a limited-purpose bank for purposes of the CRA, and it is evaluated under the community development test. The period for the COBNA Evaluation was March 1, 2008, through December 31, 2010.

[44] The period for the FSB Evaluation was January 1, 2005, through December 31, 2007.

[45] Several commenters asserted that Capital One should meet the credit needs of LMI customers in California. The CRA requires a bank or savings association to meet the credit needs of the communities in which it oper-

CRA Performance of CONA. CONA is the largest insured depository institution controlled by Capital One, representing approximately 65 percent of Capital One's insured depository institution assets. In the CONA Evaluation, the bank received "outstanding" ratings for the lending and investment tests and a "high satisfactory" rating for the service test. CONA's performance in the New York-Northern New Jersey-Long Island Multi-State Metropolitan Area ("NY Metro AA"), the Washington, D.C. Multi-State Metropolitan Area ("D.C. Metro AA"), and the State of Louisiana ("Louisiana AA") was given considerably more weight than its performance in the other states that are part of CONA's assessment area[46] to reflect the fact that 90 percent of the bank's deposits are booked in branches in those areas.

Examiners stated that CONA had good lending activity and characterized its distribution of loans among geographies of different income levels as excellent.[47] Examiners reported that CONA's distribution of HMDA-reportable mortgage loans among borrowers of different income levels was good.[48] Examiners commended CONA's community development lending, which they described as serving significant community development needs. Examiners also stated that CONA exhibited an adequate distribution of loans among borrowers of different income levels. Examiners noted that CONA's branches were accessible to geographies and individuals of different income levels and stated that product innovation and flexibility had a positive impact on the lending test. In addition, examiners noted an excellent level of community development investments that were responsive to the needs of the bank's assessment areas and community development services that were responsive to the areas' needs as well. Examiners also reported that CONA's level of community development lending significantly enhanced its lending test performance.[49]

ates, which include geographies of the institution's main office, its branches, and its deposit-taking ATMs. 12 CFR part 228; 12 CFR part 195. As noted above, Capital One expects to add services to FSB's cafés that will cause the cafés to be branches for purposes of HOLA, beginning with the cafés in San Francisco and Los Angeles. After the cafés become branches, Capital One will be required under the CRA to provide banking products and services to LMI customers in San Francisco and Los Angeles. 12 U.S.C. § 2901 *et seq.*; 12 CFR part 195.

Several commenters also suggested that the Board delay action on the proposal to allow the federal banking agencies to promulgate updated CRA regulations that would impose broader CRA requirements on companies like Capital One and FSB that conduct business outside their branch footprints. The Board has analyzed the proposal under the existing CRA regulations and procedures.

[46] The other states are Delaware, Maryland, New Jersey, Texas, and Virginia.

[47] Some commenters alleged that Capital One's depository institution subsidiaries decreased their home mortgage lending between 2007 and 2009. The Board reviewed HMDA data for 2008 and 2009, which indicate that Capital One's home mortgage application volume decreased nationwide by more than 61 percent. This decline was attributable to general economic conditions and Capital One's decisions to concentrate on direct lending and to close the legacy mortgage businesses of recently acquired North Fork Bank and Chevy Chase Bank, which focused on broker-originated alternative mortgage products.

[48] In CONA's NY Metro AA, examiners generally found that the bank's lending levels were excellent. The examiners concluded that the distribution of home purchase, home improvement, and home refinance loans was excellent and that the distribution of multifamily loans was good. In the D.C. Metro AA, examiners found that CONA's lending activity was good, that the distribution of home purchase loans in LMI geographies was consistent with the number of owner-occupied housing units, and that the distribution of home improvement loans was adequate. In the Louisiana AA, examiners reported that CONA's lending activity and geographic distribution of home mortgage loans and home refinance loans was good and that the geographic distribution of home purchase loans was excellent. The geographic distribution for home improvement loans was adequate in this assessment area.

[49] Examiners commended CONA's community development lending performance in Louisiana for being complex, innovative, and responsive to the needs of the area. In the NY Metro AA, CONA originated 300 community development loans totaling $1.1 billion during the assessment period. Examiners also praised CONA's community development lending in the D.C. Metro AA as demonstrating a high level of responsiveness. CONA made over $71 million in loans to rehabilitate affordable housing units in the D.C. Metro AA.

In addition, examiners reported that CONA's distribution of small business loans was good.[50] As noted above, many commenters expressed concern that Capital One had reduced its small business lending and, in particular, alleged that Capital One had replaced affordable loans to small businesses with higher-cost credit cards. Although Capital One's CRA-reportable small business loan volume declined by more than 81 percent between 2008 and 2009 (compared with a decrease of 56 percent for lenders in the aggregate), Capital One increased its CRA-reportable small business loan volume by more than 18 percent in 2010 (compared with an additional decrease of more than 9 percent for lenders in the aggregate). In addition, the percentage of Capital One's CRA-reportable small business loans that were made in minority or LMI census tracts in 2010 exceeded that of lenders in the aggregate. The Board also has reviewed data provided by Capital One and determined that credit cards account for a small portion of its small business lending.[51]

In the CONA Evaluation, examiners commended the bank's performance under the investment test. During the evaluation period, CONA made more than 1,350 investments, including grants and contributions, that totaled more than $1 billion. Examiners also commended CONA's demonstrated leadership and responsiveness to community development needs.[52] In addition, examiners found that CONA exhibited leadership and used innovative and complex methods to continue investing in Low Income Housing Tax Credits ("LIHTC").[53]

CONA received an overall "high satisfactory" rating under the service test in the CONA Evaluation. Examiners found that CONA's distribution of branches was accessible to geographies and individuals of different income levels.[54] Examiners reported that the bank provided a good level of community development services and praised the amount of time bank employees volunteered with different organizations.[55]

CRA Performance of COBNA.[56] COBNA's overall CRA rating was lowered from "outstanding" to "satisfactory" as a result of a review of the bank's credit card program that

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[50] In this context, "small business loans" are loans with original amounts of $1 million or less that either are secured by nonfarm, nonresidential properties or are classified as commercial and industrial loans. In both the NY Metro AA and the Louisiana AA, examiners noted that the percentage of loans to small businesses in LMI areas exceeded the percentage of such businesses in these geographies.

[51] Capital One represented that it does not market small business credit cards to applicants who are denied traditional small business loans.

[52] Examiners stated that CONA demonstrated exceptional levels of commitment and leadership in supporting the Louisiana AA's recovery from the devastation of Hurricanes Katrina and Rita. In the Louisiana AA, CONA originated or renewed 38 community development loans and lines of credit totaling $338 million.

[53] CONA provided more than $70 million in LIHTC investments in affordable housing in the NY Metro AA. In 2010, CONA made $20.4 million in LIHTC investments in the D.C. Metro AA. In the Louisiana AA, CONA made more than $50 million in LIHTC investments that included providing critical financing for a low-income-housing project in Jefferson, Louisiana, when another lender was unable to fulfill its commitment.

[54] Some commenters noted that in CONA's CRA evaluation in 2007, the bank received a "low satisfactory" rating on the service test. At that time, examiners reported that CONA lacked an appropriate distribution of branches and ATMs in LMI communities in Louisiana and Texas. Capital One represented that this rating was attributable to Capital One's acquisition of Hibernia Bank in 2005, which had not invested sufficiently in building branches in LMI communities in Louisiana and Texas. Capital One represented that, of the 33 new branches CONA opened in LMI areas since 2007, 19 are in Louisiana and Texas.

[55] In the NY Metro AA, examiners found that CONA provided an excellent level of community development services and stated that bank employees were involved with 188 different organizations. Examiners reported that in the D.C. Metro AA, CONA provided a good level of community development services, with a majority of those services being geared toward community services, such as providing financial education to students. In the Louisiana AA, examiners found that the level of community development services was good and that bank employees were involved with more than 200 different organizations.

[56] COBNA's assessment area includes all of Henrico County and the City of Richmond, both in Virginia. COBNA's community development strategy targeted opportunities first within its assessment area; then within the Commonwealth of Virginia, the surrounding states, and the Northeast region; and finally opportunities nation-

reflected certain disclosure issues identified by COBNA.[57] During the evaluation period, COBNA made more than $527 million in qualified investments. Examiners stated that COBNA demonstrated a high level of qualified investments and community development services. Examiners found that COBNA made extensive use of complex or innovative qualified investments, community development services, and community development loans. Examiners also found that COBNA demonstrated excellent responsiveness to community development needs in its assessment area.[58] In addition, examiners praised bank personnel for providing approximately 5,000 hours of participation as members of boards of directors and for providing financial and technical expertise.

CRA Performance of FSB. As noted above, FSB received an overall "outstanding" rating in its 2008 CRA evaluation, with a "high satisfactory" rating on the lending test and "outstanding" ratings on both the investment and service tests. Examiners noted that FSB's distribution of home mortgage loans reflected good penetration of LMI geographies in its assessment area and in the supplemental areas used to evaluate performance.[59] In addition, examiners found that FSB's lending performance to borrowers of different income levels in its assessment areas and in the supplemental areas was satisfactory, considering the bank's nationwide lending strategy and unique branchless platform. Examiners noted a significant level of qualified investments and grants to community development organizations, which showed a good responsiveness to credit and community economic development needs, particularly the needs of small businesses. In addition, examiners found that FSB was a leader in providing access to community development services in its assessment area through alternative delivery systems, such as the Internet, call centers, and a network of ATMs. Examiners also commended FSB on the record of its employees in providing community development services.

B. Conclusion on CRA Performance

The Board has considered all the facts of record, including the CRA performance records of the institutions involved, information provided by Capital One, comments received on the proposal and responses to those comments, and confidential supervisory information. Based on a review of the entire record, and for the reasons discussed above, the Board concludes that the CRA performance records of the relevant insured depository institutions are consistent with approval of the proposal.

Other Considerations

In its evaluation, the Board has considered the records of Capital One and FSB in complying with fair lending and other consumer protection laws.

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wide. Because there was a great need for qualified community development investments and lending in the Gulf Coast region following Hurricanes Katrina and Rita, COBNA focused its community development opportunities in that region.

[57] The violations related to credit card disclosures for a specific add-on product offered between January 2004 and April 2010. COBNA identified the violation in early 2010 and had provided restitution to affected consumers by June 2010.

[58] COBNA invested $25.5 million in 5 LIHTC developments, creating 654 units of affordable housing for LMI individuals.

[59] FSB's assessment area consists of the Philadelphia-Camden-Wilmington Metropolitan Statistical Area (or "MSA"). FSB's Supplemental MSAs include MSAs that encompass many large and midsize cities across the United States, including Washington, D.C., San Francisco, Chicago, Los Angeles, Phoenix, and Denver.

A. HMDA Analysis

The Board has reviewed HMDA data from 2008, 2009, and 2010 reported by CONA and FSB and their lending affiliates.[60] Several commenters alleged that Capital One and FSB denied the home mortgage loan applications of minority borrowers more frequently than those of nonminority applicants in certain MSAs.[61] The HMDA data indicate that, with the exception of certain areas outside CONA's branch footprint, the percentage of CONA's applications from and originations to minority borrowers, LMI borrowers, and borrowers in predominantly LMI areas generally exceeded the percentage for lenders in the aggregate. In addition, the data indicate that CONA did not exhibit a higher denial rate for minority applicants relative to its denial rate for nonminority applicants ("denial disparity ratio"), as compared with the denial disparity ratio for minority and nonminority applicants of lenders in the aggregate. The HMDA data do not suggest that Capital One excluded any racial, ethnic, economic, or geographic segment of the population within its branch footprint.[62]

In a small number of markets outside Capital One's branch footprint, including California and the Chicago MSA, the data indicate that CONA's percentage of HMDA applications from and originations to minority borrowers was lower than for lenders in the aggregate in 2008 and 2009.[63] The Board is concerned when HMDA data for an institution indicate disparities in lending and believes that all lending institutions are obligated to ensure that their lending practices are based on criteria that ensure not only safe and sound lending but also equal access to credit by creditworthy applicants regardless of their race or ethnicity. Moreover, the Board believes that all bank holding companies and their affiliates must conduct their mortgage lending operations without any abusive lending practices and in compliance with all consumer protection laws.

Although the HMDA data might reflect certain disparities in the rates of loan applications, originations, and denials among members of different racial or ethnic groups in certain local areas, they provide an insufficient basis by themselves on which to conclude whether Capital One or FSB has excluded or imposed higher costs on any group on a prohibited basis. The Board recognizes that HMDA data alone, even with the recent addition of pric-

[60] The Board reviewed HMDA data for CONA in its combined assessment areas, in each of its states, in its multistate assessment areas (Texarkana MSA, D.C. Metro AA, and NY Metro AA), and in two out-of-market areas of interest to the commenters (the State of California and the Chicago MSA). The HMDA data for CONA include Chevy Chase Bank, which Capital One acquired in 2009, in order to ensure consistent results. The Board reviewed HMDA data for FSB nationwide, in its assessment area, in its Supplemental MSAs, and in MSAs of interest to the commenters.

[61] Some commenters also questioned Capital One's efforts in awarding contracts to minority- and women-owned businesses. Although the Board fully supports programs designed to promote equal opportunity and economic opportunities for all members of society, the comments about supplier diversity practices are beyond the factors the Board is authorized to consider under the BHC Act. *See, e.g.*, Bank of America Order at C90.

In addition, one commenter asserted that the Board should ensure that Capital One's supplier diversity practices are consistent with section 342 of the Dodd-Frank Act, codified at 12 U.S.C. § 5452, which instructs the Board, including the Federal Reserve Banks, and certain other federal agencies each to establish an Office of Minority and Women Inclusion that is authorized to develop standards for "assessing the diversity policies and practices of entities regulated by the agency." The Board and the other federal agencies are developing standards for assessing the diversity policies and practices of regulated firms in accordance with section 342. Section 342 specifically provides, however, that those standards may not mandate any particular diversity practice or require any specific action based on the agency's assessment. 12 U.S.C. § 5452(b)(4).

[62] The HMDA data also indicate that although FSB generally received a lower proportion of its applications from minorities relative to lenders in the aggregate, FSB's denial disparity ratio for minority borrowers generally approximated or was more favorable than lenders in the aggregate.

[63] California and the Chicago MSA accounted for a relatively small proportion of CONA's application volume in 2008 and 2009, consistent with Capital One's strategy to make mortgage loans primarily within its branch footprint. In 2009, CONA received 3,329 applications in California and 1,304 applications in the Chicago MSA, representing 4.6 percent and 1.8 percent of its HMDA-related application volume, respectively. In 2010, Capital One's HMDA-related application volume dropped to 110 in California and 20 in the Chicago MSA.

ing information, provide only limited information about the covered loans.[64] HMDA data, therefore, have limitations that make them an inadequate basis, absent other information, for concluding that an institution has engaged in illegal lending discrimination.

Because of the limitations of HMDA data, the Board has considered these data and taken into account other information, including examination reports that provide on-site evaluations of compliance with fair lending and other consumer protection laws and regulations by CONA and its lending affiliates.[65] The Board also has consulted with the OCC, the primary federal supervisor of Capital One's subsidiary banks and FSB. In addition, the Board has considered information provided by Capital One about its compliance risk-management systems.

As discussed further below, Capital One's compliance program includes fair lending policy and product guides, testing of the integrity of its HMDA data, and fair lending training for lending-related employees. In addition, Capital One has adopted a process for evaluating new laws and regulations for applicability to its mortgage lending operations. Moreover, the CRA examinations of CONA and COBNA found that both banks demonstrated good lending activity with a good dispersion of loans across income levels in the areas within the banks' CRA assessment areas. The Board notes that lending in the areas referenced by commenters outside the banks' assessment areas was not significant. Overall, despite the disparities indicated by the HMDA data for Capital One, the Board's analysis of the HMDA data, consultations with the OCC, and review of Capital One's compliance programs suggest that Capital One's mortgage lending operations and compliance programs are adequate to ensure compliance with fair lending and other consumer protection laws.

B. Other Commenter Concerns

Commenters expressed a number of specific concerns regarding Capital One's compliance with fair lending and consumer protection laws. For instance, commenters alleged that Capital One's policies on originating home mortgage loans insured by the Federal Housing Administration ("FHA") have had an illegal discriminatory impact on minorities. Specifically, commenters alleged that Capital One refused to lower its minimum FICO credit score required for FHA loans from 620 to 580, the minimum threshold established by FHA for such loans, and that Capital One's policy had a discriminatory impact.[66] To address these concerns, Capital One is preparing to offer FHA loans to borrowers with FICO scores of between 580 and 620, with appropriate protections to minimize the risk of the borrower's default, by developing the servicing and reporting platforms necessary to sell such loans directly to the Government National Mortgage Association.

Commenters also alleged that Capital One had failed to participate in the Department of the Treasury's Hardest Hit Fund ("HHF") Program under the Troubled Asset Relief Program and that the alleged inaction has had a discriminatory impact on minorities and LMI borrowers. Commenters further alleged that Capital One has not participated in other mortgage modification programs, such as the Home Affordable Mortgage Program

[64] 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 whether an applicant who was denied credit was, in fact, creditworthy. In addition, 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) are not available from HMDA data.

[65] Examiners reported that the CONA Evaluation was not impacted by fair lending issues at the former Chevy Chase Bank, which Capital One acquired in 2009. Capital One identified fair lending issues at Chevy Chase Bank shortly after the acquisition but before Capital One merged Chevy Chase Bank into CONA. Examiners reported that Capital One took appropriate actions to address the issues.

[66] One organization noted that it had filed a complaint with HUD regarding Capital One's policies.

("HAMP"), which commenters asserted also has had a discriminatory impact on minorities and LMI borrowers. Capital One enrolled in four state HHF programs, including those of Oregon and Washington, D.C., after receiving requests on behalf of borrowers. In addition, Capital One participates in HAMP and also offers a proprietary mortgage modification program similar to HAMP. More borrowers are eligible for mortgage modifications under Capital One's proprietary program than under HAMP because the proprietary program has broader eligibility requirements, including a higher balance limit.

Commenters also alleged that Capital One's overdraft protection practices are unfair. Capital One has adopted policies and procedures regarding the payment of overdrafts consistent with the requirements of Regulation E.[67] In addition, Capital One has a daily limit on overdraft fees charged to an individual customer and a threshold account balance below which overdraft fees are not assessed. Capital One also provides consumer financial education about avoiding overdrafts to its customers with repeat overdrafts and makes available a line of credit linked to the customers' checking accounts to prevent overdraft fees.

Several commenters expressed concern that Capital One has engaged in false, misleading, or deceptive credit card practices. Commenters referenced pending litigation against Capital One alleging misleading marketing practices.[68] Some commenters stated that Capital One had received a high number of complaints regarding its credit card practices and alleged that Capital One's statements about its credit cards and the interest rates and fees are unfair or deceptive. In addition, a commenter expressed concern that Capital One has engaged in abusive credit card practices by offering borrowers multiple high-fee cards with low credit limits rather than a single card with a higher credit limit.

The Board has consulted with the OCC about Capital One's compliance with regulatory requirements related to its credit card lending operations and the systems Capital One has adopted to prevent false, misleading, or deceptive practices. Capital One conducts ongoing reviews to ensure that the terms and marketing of its credit card and other products are appropriate and comply with applicable laws and regulations, including the Truth in Lending Act and Regulation Z. Capital One's compliance program includes fair lending policy and product guides, compliance file reviews, testing of the integrity of its HMDA data, and other quality-assurance measures to help ensure compliance with consumer protection laws. Capital One also provides computer-based fair lending training for lending-related employees and supplemental, in-person training for personnel with higher fair lending compliance risks in their jobs. Capital One has represented that it will implement its compliance management program at FSB. In addition, the Board has considered the commitments made by Capital One and the conditions imposed by the Board, discussed above, that are designed to further enhance the compliance programs at Capital One. Finally, Capital One does not issue "high fee" cards as defined by the Credit Card Accountability Responsibility and Disclosure Act of 2009. Capital One also has policies that limit an individual customer to a maximum of two unsecured, general-purpose credit cards.

[67] 12 CFR part 205.

[68] On January 7, 2012, Capital One entered into a settlement agreement with the West Virginia Attorney General to resolve a lawsuit alleging that Capital One violated the West Virginia Consumer Credit and Protection Act between 2001 and 2005 by, among other things, offering a payment protection product to customers who were ineligible for certain benefits at the time of enrollment and encouraging customers to enter into debt repayment plans through solicitations that purported to be offers of new credit. As part of the settlement, under which Capital One did not admit guilt, Capital One agreed to provide $13.5 million for debt forgiveness, debt relief, and consumer education for West Virginia consumers. Capital One has enhanced its compliance risk management practices since the period to which the complaint relates and discontinued one of the lines of business that was the focus of the lawsuit.

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.[69] A financial stability factor also was added by the Dodd-Frank Act to the list of considerations in reviewing proposals under section 3 of the BHC Act.[70]

Financial Stability Standard

In reviewing applications and notices under sections 3 and 4 of the BHC Act, the Board expects that it will generally find a significant adverse effect if the failure of the resulting firm, or its inability to conduct regular-course-of-business transactions, would likely impair financial intermediation or financial market functioning so as to inflict material damage on the broader economy. This kind of damage could occur in a number of ways, including seriously compromising the ability of other financial institutions to conduct regular-course-of-business transactions or seriously disrupting the provision of credit or other financial services.

To assess the likelihood that failure of the resulting firm may inflict material damage on the broader economy, the Board will consider a variety of metrics. These would include measures of the size of the resulting firm; availability of substitute providers for any critical products and services offered by the resulting firm; interconnectedness of the resulting firm with the banking or financial system; extent to which the resulting firm contributes to the complexity of the financial system; and extent of the cross-border activities of the resulting firm.[71] These categories are not exhaustive, and additional categories could inform the Board's decision.[72] These metrics are useful in evaluating the extent to which an institution's creditors, counterparties, investors, or other market participants may have financial exposure to the institution and thus may experience strain when the firm does not meet its financial obligations to them; the extent to which the institution holds assets that, if liquidated quickly, would significantly disrupt trading or funding in key markets or cause significant losses or funding problems for other firms with similar holdings due to falling asset prices; the extent to which financial distress in the resulting institution may cause other institutions that hold similar assets or are engaged in similar activities or are perceived to

[69] Dodd-Frank Act, § 604(e), codified at 12 U.S.C. § 1843(j)(2)(A). 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) and (f) of the Dodd-Frank Act. A special process was established by the Dodd-Frank Act for requiring the divestiture of a business by a financial firm. Section 121 of the Dodd-Frank Act provides that the Board shall require a financial firm to divest or terminate a business if the Board determines that the company "poses a grave threat to the financial stability of the United States;" the Financial Stability Oversight Council ("FSOC"), by a vote of two-thirds of its members, approves the action; and the Board has determined that actions other than divestiture or termination of the business are inadequate to mitigate the grave threat. 12 U.S.C. § 5331.

[70] Dodd-Frank Act, § 604(d), codified at 12 U.S.C. § 1842(c)(7).

[71] A large value of a metric for any one category may suggest that distress at the resulting firm is likely to result in material damage to the broader economy. Many of the metrics considered by the Board measure an institution's activities relative to the U.S. financial system ("USFS"). For example, pro forma asset size of the resulting firm is expressed in terms of the resulting firm's pro forma assets as a share of total assets of the USFS. For this purpose, the USFS comprises all U.S. financial institutions ("USFIs") used in computing total liabilities for the purposes of calculating the limitation on liabilities of a financial company required under section 622 of the Dodd-Frank Act and includes U.S.-based bank and nonbank affiliates of foreign banking organizations. In connection with its supervision of nonbank financial institutions that the FSOC determines could pose a threat to the financial stability of the United States, the Board may require financial and other reporting by these institutions, which would increase the pool of available data for financial stability analyses. *See* sections 113 and 151 of the Dodd-Frank Act, codified at 12 U.S.C. §§ 5323 and 5341, respectively.

[72] The metrics for the resulting entity are not, by themselves, determinative. The Board will take into account all factors that are relevant to a transaction, some of which may not be captured by the metrics.

be dependent in important ways upon the distressed institution to experience a loss of market confidence; and the extent to which an institution in financial distress may no longer be able to provide a service that market participants rely upon and for which there are limited readily available substitutes.

In addition to these quantitative measures, the Board will consider 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.

The Board's methodology is compatible with the Basel Committee's approach to identifying global systemically important banks ("GSIBs")[73] but differs from the Basel Committee's approach in three important ways. First, the Board will consider a broader and somewhat different set of metrics. Second, the Board will consider the systemic footprint of the resulting firm relative to the USFS. Third, under the Board's approach, it is possible that if even a single category of metrics indicates that a resulting firm would pose a significant risk to the stability of the U.S. banking or financial system, the Board may determine that there is an adverse effect of the proposal on the stability of the U.S. banking or financial system.[74] This methodology will help identify not only the more obvious risks associated with significant expansion proposals by GSIBs, but also transactions involving other firms that could pose a risk to the stability of the U.S. banking or financial system, even if the resulting firm is not a GSIB.

On the other hand, certain types of transactions likely would have only a de minimis impact on an institution's systemic footprint and, therefore, are not likely to raise concerns about financial stability. For example, a proposal that involves an acquisition of less than $2 billion in assets, results in a firm with less than $25 billion in total assets, or represents a corporate reorganization may be presumed not to raise financial stability concerns absent evidence that the transaction would result in a significant increase in interconnectedness, complexity, cross-border activities, or other risk factor.

Analysis of the Financial Stability Impact of this Proposal

In this case, the Board has undertaken its metrics-based analysis to determine whether this proposal presents a significant risk to the stability of the U.S. banking or financial system. The Board also has considered the relative degree of difficulty of resolving the resulting firm. The Board reviewed publicly available data, comments received from the public, data compiled through the supervisory process, and data obtained through information requests to the institutions involved in the proposal, as well as qualitative information.

Size. An organization's size is one important indicator of the risk that the organization poses to the financial system. Congress has imposed a specific 10 percent nationwide deposit limit and a 10 percent nationwide liabilities limit on potential combinations by banking organizations.[75] Other provisions of the Dodd Frank Act impose special or

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[73] *See* Basel Committee on Banking Supervision ("Basel Committee"). "Global systemically important banks: assessment methodology and the additional loss absorbency requirement. Rules text." November 2011.

[74] The Board will consider each metric both individually and in combination with others, rather than following the Basel Committee approach of focusing solely on a weighted average of all the metrics. For example, a merger of two firms that are dominant providers of critical products or services would likely present a significant risk to U.S. financial stability, even if the values of the resulting firm's metrics were low in all other categories.

[75] 12 U.S.C. §§ 1843(i)(8) and 1852.

enhanced supervisory requirements on large banking organizations.[76] These measures are helpful indicators of potential systemic risk; however, the fact that Congress also requires the Board to review the potential systemic impact of a transaction that does not reach these limits likely indicates they were not meant to substitute for an analysis of size as part of the systemic risk factor.

The Board has considered measures of Capital One's size relative to the USFS, including Capital One's consolidated assets, its consolidated liabilities,[77] its total leverage exposures,[78] and its U.S. deposits. As a result of the proposed acquisition of FSB and the HSBC assets,[79] Capital One would become between the 14th and 20th largest USFI based on assets, liabilities, and leverage exposures with between 1.1 percent and 1.6 percent of the USFS total. Based on deposits, Capital One would become the fifth largest USFI, with 2.3 percent of the total. These measures suggest that, although the combined organization would be large on an absolute basis, its shares of USFS assets, liabilities, leverage exposures, and deposits would remain modest, and its shares of national deposits and liabilities would fall well below the 10 percent limitations set by Congress.

Measures of a financial institution's size on a pro forma basis could either understate or overstate risks to financial stability posed by the financial institution. For instance, a relatively small institution that operates in a critical market for which there is no substitute provider, or that could transmit its financial distress to other financial organizations through multiple channels, could present significant risks to the stability of the USFS.

Although the proposed transaction would increase Capital One's overall size, and result in it becoming the fifth largest bank in the United States based on U.S. deposits, its larger size must be viewed in conjunction with the other metrics. Accordingly, the Board has considered other factors, both individually and in combination with size, to evaluate the likely impact of this transaction on financial stability.

Substitutability. The Board has examined whether Capital One or FSB engages in any activities that are critical to the functioning of the USFS and whether there would be adequate substitute providers that could quickly step in to perform such activities should the combined entity suddenly be unable to do so as a result of severe financial distress. Capital One accepts retail deposits and engages in mortgage lending, mortgage and credit card servicing, commercial real estate financing, small business lending, credit card and other consumer lending, and securities brokerage services. FSB offers savings accounts, certificates of deposit, residential mortgage loans, and retail securities brokerage services. In most of these activities, Capital One has, and as a result of the proposals, would continue

[76] Section 165 of the Dodd-Frank Act, codified at 12 U.S.C. § 5365, requires the Board to subject all bank holding companies with total consolidated assets of $50 billion or more, and any nonbank financial company designated by the FSOC for supervision by the Board, to enhanced prudential standards in order to prevent or mitigate risks to the financial stability of the United States that could arise from the severe distress or failure of these firms. Two commenters urged the Board not to approve the proposed transaction until the Board adopts rules to implement section 165 of the Dodd-Frank Act. The Board, jointly with the FDIC, has issued a notice of final rulemaking that implements the requirements of section 165(d). *See* 76 *Federal Register* 67,323 (November 1, 2011). The Board also has issued a notice of proposed rulemaking, implementing the other requirements within section 165 of the Dodd-Frank Act. 77 *Federal Register* 594 (January 5, 2012).

[77] The Board has considered both consolidated liabilities on Capital One's balance sheet and liabilities as computed under the limitations on consolidated liabilities in section 622 of the Dodd-Frank Act, codified at 12 U.S.C. § 1852.

[78] Total leverage exposure is calculated in a manner roughly equivalent to the methodology set out in "Basel III: A global regulatory framework for more resilient banks and banking systems" and takes into account both on- and off-balance-sheet assets.

[79] As noted above, Capital One has applied to the OCC for approval under the Bank Merger Act to acquire up to $29 billion in credit card assets from HSBC. The Board has assumed the acquisition of the entire $29 billion in assets.

to have a small share on a nationwide basis, and numerous competitors would remain for each of the activities in which Capital One and FSB engage.

Capital One is currently the fifth largest provider of credit cards in the United States. Assuming the acquisition of the HSBC credit card assets (a transaction subject to review by the OCC in a separate proceeding), Capital One would increase its share of outstanding credit card balances in the United States from 7.7 percent to 11.8 percent and thereby become the fourth largest provider of credit cards in the United States. In considering the potential effect on financial stability in this case, the Board also has considered that three competing credit card lenders would each have outstanding credit card balances that are between one-third and two-thirds larger than those of Capital One, and two other lenders would each have balances approximately half the size of the outstanding credit card balances of Capital One. In addition, there are numerous other credit card lenders that operate on a national or regional basis. Capital One's share of credit card loans does not appear to be substantial enough to cause significant disruptions in the supply of credit card loans if Capital One were to experience distress, due to the availability of substitute providers that could assume Capital One's business.

Interconnectedness. The Board has examined data to determine whether financial distress experienced by the combined entity could create financial instability by being transmitted to any other institutions or markets within the U.S. banking or financial system.[80]

Capital One does not engage currently and as a result of this transaction would not engage in business activities or participate in markets to a degree that would pose significant risk to other institutions, in the event of financial distress of the combined entity. The combined entity's use of wholesale funding, as a share of USFS wholesale funding usage, is less than 1 percent and is well below its corresponding share of USFS consolidated assets. The combined entity's shares of USFS intra-financial system assets and liabilities also are less than 1 percent. The transaction under review in this case also would not increase exposure to any single counterparty that is among the top three counterparties of either Capital One or FSB before the merger.

Complexity. The Board has considered the extent to which the combined entity would contribute to the overall complexity of the USFS. The combined entity's complex assets and trading book and available-for-sale securities represent a significantly lower share in the USFS than its corresponding share of consolidated assets. The Board also has considered whether the complexity of the combined entity's assets and liabilities would hinder its timely and efficient resolution in the event it were to experience financial distress. Capital

[80] Commenters argued that Capital One is materially interconnected with the USFS because it securitizes a portion of its credit card receivables into securities that are sold to pension funds, insurance companies, and other large, systemically important institutions. This factor is mitigated in several ways. Capital One's credit card securitizations represent a relatively small portion of the credit card securitization market. Taking into account the acquisition of HSBC's credit card business, Capital One's total share of credit card securitizations is less than 9 percent, consistent with its share of outstanding credit card loans. A number of factors align Capital One's interest in ensuring sound underwriting of the underlying credit card accounts with those of investors in the securitization. These include recent changes to accounting rules that require credit card securitizations to be consolidated on the balance sheet of the securitizer in many situations and capital rules that require a capital reserve. *See* Statements of Financial Accounting Standards Nos. 166 and 167, codified in Accounting Standards Codification Topics 860 and 810; *Final Rule for Regulatory Capital Standards Related to Statements of Financial Accounting Standards Nos. 166 and 167*, 75 *Federal Register* 4636 (January 28, 2010). In addition, Capital One retains a seller's interest that exposes the institution to losses from the underlying credit card receivables on a pari passu basis with investors in its credit card securitizations. The Dodd-Frank Act also enhanced the disclosure and reporting obligations of securitizers to provide better information to investors to analyze the credit risks and ongoing performance of the securitized assets and, ultimately, whether to purchase or sell the asset-backed securities. *See* §§ 942, 943, and 945 of the Dodd-Frank Act, as codified by 15 U.S.C. §§ 78o-7, 77d, and 77g, respectively.

One and FSB do not engage in complex activities, such as being a core clearing and settlement organization for critical financial markets, that might complicate the resolution process by increasing the complexity, costs, or timeframes involved in a resolution. Under the circumstances, resolving the combined organization would not appear to involve a level of cost, time, or difficulty such that it would cause a significant increase in risk to the stability of the USFS.[81]

Cross-Border Activity. The Board has examined the cross-border activities of Capital One and FSB to determine whether the cross-border presence of the combined organization would create difficulties in coordinating any resolution, thereby significantly increasing the risk to U.S. financial stability. Capital One has credit card operations in the United Kingdom and Canada that total approximately $8.7 billion. These businesses are similar to Capital One's operations in the United States and do not add any substantial complexity to its operations. Although FSB currently is owned by ING Groep, a Dutch financial institution, FSB operates only in the United States. The combined organization is not expected to engage in any additional activities outside the United States as a result of the proposed transaction. In addition, the combined organization would not engage in the provision of critical services whose disruption would impact the macroeconomic condition of the United States by disrupting trade or resulting in increased resolution difficulties.

Financial Stability Factors in Combination. The Board has assessed the foregoing factors individually and in combination to determine whether interactions among them might mitigate or exacerbate risks suggested by looking at them individually. The Board also has considered whether the proposed transaction would provide any stability benefits and whether enhanced prudential standards applicable to the combined organization would offset any potential risks.[82]

For instance, concerns regarding Capital One's size would be greater if Capital One were also highly interconnected to many different segments of the USFS through its counterparty relationships or other channels, or if Capital One participated to a larger extent than it does in short-term funding and capital markets. The Board's level of concern also would be greater if the structure and activities of Capital One were sufficiently complex that, if Capital One were to fail, it would be difficult to resolve quickly without causing significant disruptions to other financial institutions or markets.

As discussed above, the combined entity would not be highly interconnected. Furthermore, the organizational structure and operations of the combined organization would be centered on a commercial banking business, and in the event of distress, the resolution process would be handled in a predictable manner by relevant authorities. The Board also has considered other measures that are suggestive of the degree of difficulty with which Capital One could be resolved in the event of a failure, such as the organizational and legal complexity and cross-border activities of the resulting firm. These measures suggest that Capital One would be significantly less complicated to resolve than the largest U.S. universal banks and investment banks.

Based on these and all the other facts of record, the Board has determined that considerations relating to financial stability are consistent with approval.

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[81] As noted previously, the Dodd-Frank Act requires bank holding companies that hold more than $50 billion in total consolidated assets, such as Capital One, to submit resolution plans, which are intended to assist the institutions in managing their risks and to plan for a rapid and orderly resolution in the event of material distress or failure and to enable the regulators to understand an institution's complexity. *See* 12 U.S.C. § 5365.

[82] Section 165 of the Dodd-Frank Act, codified at 12 U.S.C. § 5365.

Public Benefits of the Proposal

As noted above, the Board is required to consider whether the proposed acquisition of FSB and its nonbanking subsidiaries "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."[83]

As part of this review, the Board considered that the European Commission required ING Groep to divest FSB by 2013 as a condition of its approval to allow the government of The Netherlands to provide aid to ING Groep in 2008 and 2009. The sale of FSB to Capital One provides depositor continuity to the U.S. operations of FSB and to FSB customers and enables all FSB customers to continue receiving their banking services by virtue of its acquisition by a single organization.

The record indicates that consummation of the proposal would result in additional benefits to consumers currently served by FSB. The proposal would allow Capital One to offer a wider array of mortgage loans and banking products and services to FSB's customers, including fixed-rate 30-year mortgage loans, full-access checking accounts, automobile loans, small business loans, commercial loans, and credit card and other consumer loans, none of which are provided by FSB. In addition, FSB customers would have access to Capital One's branch locations and ATM network, small business technical assistance programs, and corporate trust services.[84]

As noted above, Capital One plans to add deposit-taking facilities to FSB's eight cafés, which will enhance the services available to the customers and communities served by these cafés. The conversion of these locations to branches of FSB would also expand Capital One's CRA assessment areas to the relevant communities served by those cafés. Seven of the eight cafés are in areas that are not currently served by branches of FSB; four of these cafés are in LMI census tracts.

In addition, Capital One's customers would benefit from access to a more efficient and robust Internet banking service than is currently offered by Capital One. This provides Capital One customers a broader suite of products and services and more convenient ways to access their accounts than currently available.

The proposed acquisition of FSB would also increase Capital One's access to low-cost deposits, which will diversify Capital One's funding base. The proposal also would result in significant operational efficiencies for Capital One. Capital One would realize significant cost savings from consolidating systems, platforms, and corporate staff functions. In addition, Capital One would achieve substantial funding savings from optimizing management of the combined deposit portfolio. By improving efficiencies and strengthening its funding and liquidity profile, Capital One would be better placed to provide credit and other banking services to its entire customer base, including current customers of FSB.

The Board has determined that the conduct of the proposed nonbanking activities within the framework of Regulation Y and Board precedent is not likely to result in significant adverse effects, such as undue concentration of resources, decreased or unfair competition,

[83] 12 U.S.C. § 1843(j)(2)(A).

[84] Some commenters advocated that Capital One continue to offer the same terms and conditions applicable to FSB's savings accounts. Capital One has represented that it does not plan to change any of FSB's current product features.

conflicts of interests, unsound banking practices, or risk to the stability of the United States banking or financial system. Moreover, for the reasons discussed above, the Board believes that the factors related to competition, financial and managerial resources, convenience and needs, and financial stability are consistent with approval of this case.

Based on all the facts of record, including the commitments and conditions noted in this case, the Board has concluded that consummation of the proposal can reasonably be expected to produce public benefits that would outweigh any likely adverse effects. 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.

Conclusion

Based on the foregoing and all the facts of record, the Board has determined that the proposal should be, and hereby is, approved.[85] In reaching its conclusion, the Board has considered all the facts of record in light of the factors that it is required to consider under the BHC Act. The Board's approval is specifically conditioned on compliance by Capital One and FSB with the conditions imposed in this order and the commitments made to the Board in connection with the notice. The Board's approval also is subject to all the conditions set forth in Regulation Y, including those in sections 225.7 and 225.25(c),[86] and to the Board's authority to require such modification or termination of the activities of a bank holding company or any of its subsidiaries as the Board finds necessary to ensure compliance with, and to prevent evasion of, the provisions of the BHC Act and the Board's regulations and orders issued thereunder. For purposes of this action, these conditions and commitments are deemed to be conditions imposed in writing by the Board in connection with its findings and decision herein and, as such, may be enforced in proceedings under applicable law.

The acquisition shall not be consummated 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 Richmond, acting pursuant to delegated authority.

By order of the Board of Governors, effective February 14, 2012.

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

Robert deV. Frierson
Deputy Secretary of the Board

[85] Several commenters requested that the Board hold a public hearing on the proposal. 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 proposal and, in fact, submitted written comments that the Board has considered in acting on the proposal. 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 proposal are denied.

[86] 12 CFR 225.7 and 225.25(c).

Hana Financial Group Inc.
Seoul, Korea

Order Approving Notice to Engage in Nonbanking Activities
FRB Order No. 2012-1 (February 8, 2012)

Hana Financial Group Inc., Seoul, Korea ("HFG"), a foreign banking organization subject to the provisions of the Bank Holding Company Act ("BHC Act"),[1] has requested the Board's approval under section 4(c)(8) of the BHC Act[2] and section 225.24 of the Board's Regulation Y[3] to acquire indirect controlling interests in KEB NY Financial Corp., New York, New York ("KEB NY"), and KEB LA Financial Corp., Los Angeles, California ("KEB LA"). HFG would acquire KEB NY and KEB LA as part of the acquisition of a controlling interest in Korea Exchange Bank, Seoul, Korea ("KEB"). KEB NY and KEB LA are wholly owned subsidiaries of KEB.[4] As a result of the proposed acquisition, HFG would engage in the United States in the following nonbanking activities:

1. making, acquiring, brokering, or servicing loans or other extensions of credit (including factoring, issuing letters of credit, and accepting drafts) for the account of KEB NY and KEB LA, or for the account of others, in accordance with 12 CFR 225.28(b)(l); and
2. activities usual in connection with making, acquiring, brokering, or servicing loans or other extensions of credit, as determined by the Board and permitted under 12 CFR 225.28(b)(2).

Notice of the proposal, affording interested persons an opportunity to comment, has been published in the *Federal Register* (76 *Federal Register* 6136 (2011)). The time for filing comments has expired, and the Board has considered the notice and all comments received in light of the factors set forth in section 4 of the BHC Act.

HFG, with consolidated assets of approximately $157.1 billion, is the fourth largest banking organization in Korea. In the United States, HFG, indirectly through its subsidiary Hana Bank, Seoul, operates a New York state-licensed agency in New York City. KEB is a Korean commercial bank headquartered in Seoul with total assets of approximately $92 billion. KEB is the fifth largest commercial bank in Korea, and it provides a broad range of banking and other financial services throughout the world. In the United States, KEB owns and operates three wholly owned subsidiaries. Two of the subsidiaries, KEB NY and KEB LA, are lending subsidiaries that hold, service, and originate commercial loans and provide trade financing. The third subsidiary engages in servicing activities.[5]

The Board has determined by regulation that extending credit and servicing loans, and activities related to extending credit, are activities closely related to banking for purposes of section 4(c)(8) of the BHC Act. HFG has committed to conduct the proposed activities in accordance with the limitations set forth in Regulation Y and the Board's orders.

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[1] As the parent company of a foreign bank operating an agency in the United States, HFG is subject to the BHC Act by operation of section 8(a) of the International Banking Act of 1978 (12 U.S.C. § 3106(a)).

[2] 12 U.S.C. §§ 1843(c)(8) and 1843(j).

[3] 12 CFR 225.24.

[4] A commenter asserted that Goldman Sachs and "others" should join this application. Goldman Sachs owns less than 5 percent of the shares of HFG and does not require Board approval under the BHC Act with respect to the proposed transaction. No other shareholder of HFG is subject to the BHC Act and none requires approval under the act.

[5] KEB USA International Corp. engages in servicing activities that are permitted under section 4(c)(1)(C) of the BHC Act (12 U.S.C. § 1843(c)(1)(C)).

In reviewing the proposal, the Board is required by section 4(j)(2)(A) of the BHC Act to determine that the proposed acquisition "can reasonably be expected to produce benefits to the public . . . 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."[6] As part of its evaluation of these factors, the Board considers the financial and managerial resources of the companies involved and the effect of the proposal on those resources.[7]

In assessing the financial and managerial resources of the companies involved, the Board has considered, among other things, information provided by HFG, public comment, confidential reports of examination, other confidential supervisory information, and publicly reported financial and other information. In evaluating the financial factors of this proposal, the Board has considered a number of factors, including capital adequacy. HFG has capital ratios in excess of the minimum levels that would be required by the Basel Capital Accord and are considered equivalent to the capital that would be required of a U.S. banking organization. The transaction in the United States is a small part of the acquisition by HFG of a foreign bank in Korea. The Board has considered that the primary supervisor for HFG in Korea has reviewed the financial factors and approved the acquisition of KEB by HFG.

In addition, the Board has considered the managerial resources of HFG,[8] the supervisory experiences of the relevant banking supervisory agencies with HFG, and HFG's record of compliance with applicable U.S. banking laws.[9] The Board has also consulted with home country authorities responsible for supervising HFG and reviewed reports of examination from the appropriate federal and state supervisors of the U.S. operations of HFG that assessed its managerial resources. As noted, HFG's home country supervisor, the Korean Financial Services Commission, has approved the proposed acquisition. Based on all the facts of record, the Board has concluded that considerations relating to the financial and managerial resources of the organizations involved are consistent with approval.

Section 4(j)(2)(A) of the BHC Act also requires the Board to consider whether the proposal is likely to pose a significant risk to the stability of the United States banking or financial system. There would be only minimal linkages between HFG and the U.S. financial system if the proposal were approved. For instance, KEB NY and KEB LA have combined total U.S. assets of $626 million, and HFG's current U.S. assets, represented by Hana Bank's agency in New York, are approximately $600 million. The Board believes that the proposal would not pose a significant risk to the United States banking or financial system.

The Board has also considered carefully the competitive effects of the proposal in light of all the facts of record. HFG and KEB compete only in the Metropolitan New York-New Jersey lending market and represent a relatively small aggregate position within that market. The Metropolitan New York-New Jersey lending market is unconcentrated, and numerous competitors would remain in the market. Based on all the facts of record, the

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6 12 U.S.C. § 1843(j)(2)(A).

7 12 CFR 225.26.

8 A commenter expressed concern about HFG's managerial strength based on an article in a Korean newspaper that described a supervisory "caution" issued against Hana Bank for violation of certain insurance requirements in Korea. In connection with this notice, the Board has reviewed HFG's record of operation in the U.S. and has consulted with HFG's home country supervisor.

9 The commenter requested that the Board consider the proposal in light of the Community Reinvestment Act ("CRA") (12 U.S.C. § 2901 *et seq.*). The CRA does not provide for consideration of a notificant's CRA performance record in the evaluation of a notice to acquire a nondepository institution under section 4 of the BHC Act. The commenter also asked that the Board "explore" a 2003 judicial decision. However, that decision does not involve any entity affiliated with either of the parties to the proposed transaction.

Board concludes that HFG's proposed activities would have a de minimis effect on competition for the relevant nonbanking activities.

The Board expects that the proposed activities would result in benefits to the public by enhancing the ability of HFG and KEB to serve their customers within the United States. The Board concludes that the conduct of the proposed nonbanking activities within the framework of Regulation Y and Board precedent is not likely to result in adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interests, unsound banking practices, or a significant risk to the stability of the United States banking or financial system that would outweigh the public benefits of the proposal discussed above. Accordingly, based on all the facts of record, the Board has determined that the balance of the public benefits factor that it must consider under section 4(j) of the BHC Act is consistent with approval of the proposal.

Based on the foregoing, the Board has determined that the notice should be, and hereby is, approved.[10] In reaching its conclusion, the Board has considered all the facts of record in light of the factors that it is required to consider under the BHC Act. The Board's approval is specifically conditioned on compliance by HFG with the conditions imposed in this order and the commitments made to the Board in connection with the notice. The Board's approval is also subject to all the conditions set forth in Regulation Y, including those in sections 225.7 and 225.25(c),[11] and to the Board's authority to require such modification or termination of the activities of HFG and any of its subsidiaries as the Board finds necessary to ensure compliance with, and to prevent evasion of, the provisions of the BHC Act and the Board's regulations and orders issued thereunder. For purposes of these actions, the conditions and commitments are deemed to be conditions imposed in writing by the Board in connection with its findings and decision and, as such, may be enforced in proceedings under applicable law.

This transaction shall not be consummated 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 New York, acting pursuant to delegated authority.

By order of the Board of Governors, effective February 8, 2012.

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

Robert deV. Frierson
Deputy Secretary of the Board

[10] The commenter has requested that the Board hold a public meeting or hearing on the proposal. Section 4 of the BHC Act and the Board's rules thereunder provide for a hearing on a notice to acquire nonbanking companies 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 meeting 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 carefully the commenter's request in light of all the facts of record. In the Board's view, the commenter had ample opportunity to submit its views, and, in fact, submitted written comments that the Board has considered carefully in acting on the proposal. The commenter's request fails to demonstrate why the written comments do not present its views adequately and fails to identify disputed issues of fact that are material to the Board's decision that would be clarified by a public meeting or hearing. For these reasons, and based on all the facts of record, the Board has determined that a public meeting or hearing is not required or warranted in this case. Accordingly, the request for a public meeting or hearing on the proposal is denied.

[11] 12 CFR 225.7 and 225.25(c).

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Order Issued Under Bank Holding Company Act

Order Issued Under Section 3 of the Bank Holding Company Act

Industrial and Commercial Bank of China Limited
Beijing, People's Republic of China

China Investment Corporation
Beijing, People's Republic of China

Central Huijin Investment Ltd.
Beijing, People's Republic of China

Order Approving Acquisition of Shares of a Bank
FRB Order No. 2012–4 (May 9, 2012)

Industrial and Commercial Bank of China Limited ("ICBC"), China Investment Corporation ("CIC"), and Central Huijin Investment Ltd. ("Huijin"), all of Beijing, People's Republic of China (collectively, "Applicants"), have requested the Board's approval to become bank holding companies under section 3 of the Bank Holding Company Act of 1956, as amended ("BHC Act"),[1] by acquiring up to 80 percent of the voting shares of The Bank of East Asia (U.S.A.) National Association ("BEA-USA"), New York, New York.[2]

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published (76 *Federal Register* 21367 (April 15, 2011)). The time for filing comments has expired, and the Board has considered the proposal and all comments received in light of the factors set forth in section 3 of the BHC Act.

ICBC, with total assets of approximately $2.5 trillion, is the largest bank in China.[3] The government of China owns approximately 70.7 percent of ICBC's shares through the Ministry of Finance and CIC and Huijin.[4] No other shareholder owns more than 5 percent of ICBC's shares.

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[1] 12 U.S.C. § 1842.

[2] The Bank of East Asia, Limited ("BEA"), Hong Kong SAR, People's Republic of China, and its subsidiary, East Asia Holding Company, Inc. ("EAHC"), New York, New York, both bank holding companies, currently own all the voting shares of BEA-USA and will continue to own 20 percent of the voting shares of the bank after the proposed transaction. BEA and EAHC will continue to be bank holding companies with respect to BEA-USA. BEA has an option to sell the remaining shares of BEA-USA to ICBC, beginning 18 months after consummation of the transaction.

[3] Asset and ranking data are as of December 31, 2011.

[4] The Ministry of Finance owns approximately 35.3 percent and CIC, indirectly through Huijin, owns approximately 35.4 percent of ICBC's shares, respectively. The National Council for Social Security Fund holds approximately 4 percent of ICBC's shares. Commenters asserted that the government of China must file an application to become a bank holding company due to its control of CIC. The Board has a long-standing position that, as a legal matter, foreign governments are not "companies" for purposes of the BHC Act and, therefore, are not covered by the act. *See Banca*

ICBC engages primarily in retail and commercial banking throughout China, including Hong Kong SAR and Macau SAR. Outside China, ICBC operates subsidiary banks in Canada, Indonesia, Kazakhstan, Luxembourg, Malaysia, Thailand, Russia, the United Arab Emirates, and the United Kingdom and operates branches in a number of countries, including Australia, Germany, India, Japan, Luxembourg, Pakistan, Singapore, South Korea, Vietnam, Qatar, and the United Arab Emirates. In the United States, ICBC operates an uninsured state licensed branch in New York City and owns Industrial and Commercial Bank of China Financial Services LLC ("ICBCFS"), New York, New York, a registered broker–dealer that engages in securities brokerage and riskless principal activities.[5] ICBC is a qualifying foreign banking organization and upon consummation of the proposal, it would continue to meet the requirements for a qualifying foreign banking organization under Regulation K.[6]

CIC is an investment vehicle organized by the Chinese government for the purpose of investing its foreign exchange reserves. CIC controls Huijin, a Chinese government-owned investment company organized to invest in Chinese financial institutions.[7] In addition to ICBC, Huijin owns controlling interests in two Chinese banks that operate banking offices in the United States: Bank of China Limited and China Construction Bank Corporation, both also of Beijing.[8] Under the International Banking Act, any foreign bank that operates a branch, agency, or commercial lending company in the United States, and any company that controls the foreign bank, is subject to the BHC Act as if the foreign bank or company were a bank holding company.[9] As a result, CIC and Huijin are subject to the BHC Act as if they were bank holding companies.[10] Through the proposed acquisition of BEA-USA, Applicants would become bank holding companies under the BHC Act.

BEA-USA, with total consolidated assets of approximately $780 million and deposits of approximately $621 million,[11] engages in retail and commercial banking in the United States. BEA-USA operates 13 branches in New York and California.

Commerciale Italiana, 68 *Federal Reserve Bulletin* 423, 425 (1982). However, the Board has determined that foreign government-owned corporations are considered "companies" under the BHC Act. *See* Board letters to Patricia Skigen, Esq., dated August 19, 1988; to H. Rodgin Cohen, Esq., dated August 5, 2008; and to Arthur S. Long, Esq., dated November 26, 2008. The foreign government-owned companies that control ICBC — CIC and Huijin —have filed to become bank holding companies in this case.

[5] ICBC received approval to acquire ICBCFS under section 4(c)(8) of the BHC Act. 12 U.S.C. § 1843(c)(8). *See* Federal Reserve Bank of New York letter to Douglas Landy, Esq., dated June 25, 2010.

[6] 12 CFR 211.23(a) .

[7] CIC also owns a noncontrolling interest in Morgan Stanley, New York, New York. *See China Investment Corporation*, 96 *Federal Reserve Bulletin* B31 (2010) ("CIC Order").

[8] Bank of China Limited operates two grandfathered insured federal branches in New York City and a limited uninsured federal branch in Los Angeles and has received Board approval to establish an additional uninsured federal branch in Chicago. Bank of China Limited, FRB Order No. 2012-6 (May 9, 2012). Bank of China Limited also controls a wholly owned subsidiary bank, Nanyang Commercial Bank, Limited, Hong Kong SAR, People's Republic of China, that operates an uninsured federal branch in San Francisco. China Construction Bank Corporation operates an uninsured state-licensed branch and a representative office in New York City. Huijin also owns a controlling interest in Agricultural Bank of China Limited, Beijing, People's Republic of China, which operates a representative office in New York City and has received Board approval to establish an uninsured state-licensed branch in New York City. Agricultural Bank of China Limited, FRB Order No. 2012-5 (May 9, 2012).

[9] 12 U.S.C. § 3106.

[10] The Board previously provided certain exemptions to CIC and Huijin under section 4(c)(9) of the BHC Act, which authorizes the Board to grant to foreign companies exemptions from the nonbanking restrictions of the BHC Act when the exemptions would not be substantially at variance with the purposes of the act and would be in the public interest. *See* 12 U.S.C. §1843(c)(9). The exemptions provided to CIC and Huijin do not extend to ICBC, Bank of China Limited, China Construction Bank Corporation, or any other Chinese banking subsidiary of CIC or Huijin that operates a branch or agency in the United States. *See* Board letter dated August 5, 2008, to H. Rodgin Cohen, Esq.

[11] Deposit data are as of December 31, 2011.

Competitive Considerations

The Board has considered the competitive effects of the proposal in light of all the facts of the record. Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or would be in furtherance of any attempt to monopolize the business of banking in any relevant banking market. The BHC Act also prohibits the Board from approving a proposal that would substantially lessen competition in any relevant banking market, unless the anticompetitive effects of the proposal clearly are outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the community to be served.[12]

BEA-USA operates in New York and in California. As noted, Bank of China Limited maintains insured branches in New York City that compete directly with BEA-USA in the metropolitan New York-New Jersey-Pennsylvania-Connecticut ("Metropolitan New York") banking market.[13] CIC also owns a noncontrolling interest in Morgan Stanley, which competes in that market. The Board has reviewed the competitive effects of the proposal in the Metropolitan New York 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 total deposits in depository institutions in the market ("market deposits") controlled by relevant institutions,[14] and the concentration level of market deposits and the increase in that level as measured by the Herfindahl-Hirschman Index ("HHI") under the Department of Justice Merger Guidelines ("DOJ Guidelines") as if CIC controlled Morgan Stanley.[15]

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[12] 12 U.S.C. § 1842(c)(1). *See e.g., Emigrant Bancorp, Inc.,*82 *Federal Reserve Bulletin* 555 (1996). One commenter conjectured, without providing any supporting information, that this proposal would result in an anticompetitive effect for the United States banking system if ICBC's primary purpose is to control or strongly influence the U.S. financial system. In addition to the facts cited below, the Board notes that BEA-USA is relatively small and that BEA-USA, the ownership and operation of BEA-USA by Applicants, and the activities of Applicants in the United States are subject to the supervisory, examination, and enforcement authority of the federal banking agencies, including the Board, and to all applicable U.S. laws, including banking and financial laws. In addition, any subsequent bank acquisitions or commencement of additional banking activities by Applicants in the United States are subject to the same standards, including antitrust and financial stability standards, that are applicable to similar proposals by domestic organizations.

[13] The Metropolitan New York banking market includes Bronx, Dutchess, Kings, Nassau, New York, Orange, Putnam, Queens, Richmond, Rockland, Suffolk, Sullivan, Ulster, and Westchester Counties in New York; Bergen, Essex, Hudson, Hunterdon, Mercer, Middlesex, Monmouth, Morris, Ocean, Passaic, Somerset, Sussex, Union, and Warren Counties and the northern portion of Mercer County in New Jersey; Monroe and Pike Counties in Pennsylvania; and Fairfield County and portions of Litchfield and New Haven Counties in Connecticut.

Applicants do not currently compete with BEA-USA in any other relevant banking market. ICBC and China Construction Bank Corporation operate branch offices in the Metropolitan New York banking market. Bank of China Limited operates a branch in Los Angeles and Bank of China Limited's subsidiary, Nanyang Commercial Bank, Limited, operates a branch in San Francisco. None of these branches is insured by the Federal Deposit Insurance Corporation, and these branches generally cannot accept retail deposits.

[14] Call report, 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. The data are also 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, Inc.*, , 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).

[15] Under the DOJ 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 recently issued revised Horizontal Merger Guidelines, the DOJ has confirmed that its guidelines for bank mergers or acquisitions, which were issued in 1995, were not changed. Press Release, Department of Justice (August 19, 2010), available at www.justice.gov/opa/pr/2010/August/10-at-938.html.

Consummation of the acquisition would be consistent with Board precedent and within the thresholds in the DOJ Guidelines in the Metropolitan New York banking market. On consummation, the banking market would remain moderately concentrated as measured by the HHI, which would remain unchanged at 1401. In addition, numerous competitors would remain in the market, which would continue to have 270 insured depository institution competitors upon consummation of this proposal. The combined deposits of the relevant institutions in the Metropolitan New York banking market represent less than 1 percent of market deposits.

The DOJ also has reviewed the matter and has advised the Board that the DOJ does not believe that the acquisition of BEA-USA by CIC, Huijin, and ICBC would be likely to have a significantly adverse effect on competition in any relevant banking market. In addition, the Office of the Comptroller of the Currency ("OCC") and the Federal Deposit Insurance Corporation ("FDIC") have been afforded an opportunity to comment and have not objected to the transaction.

Based on all the facts of record, the Board has concluded that consummation of the proposal would not have a significantly adverse effect on competition or on the concentration of banking resources in any relevant banking market and that competitive factors are consistent with approval of the proposal.

Financial, Managerial, and Other Supervisory Considerations

Section 3 of the BHC Act requires the Board to consider the financial and managerial resources and future prospects of the companies and depository institutions involved in the proposal as well as the effectiveness of these companies in combatting money-laundering activities.[16] Section 3 of the BHC Act also requires the Board to determine that an applicant has provided adequate assurances that it will make available to the Board such information on its operations and activities and those of its affiliates that the Board deems appropriate to determine and enforce compliance with the BHC Act.[17]

The review was conducted in light of all the facts of record, including confidential supervisory and examination information regarding ICBC's U.S. operations and BEA-USA, publicly reported and other financial information, and information provided by Applicants and by public commenters. The Board also has consulted with the China Banking Regulatory Commission ("CBRC"), the agency with primary responsibility for the supervision and regulation of Chinese banking organizations, including ICBC.[18]

In evaluating financial factors, the Board reviews the financial condition of the applicants and the target depository institutions. In this evaluation, the Board considers a variety of information, including capital adequacy, asset quality, and earnings performance.[19] The Board also evaluates the financial condition of the combined organization and the impact of the proposed funding of the transaction. In assessing financial factors, the Board consistently has considered capital adequacy to be especially important.

Applicants are large relative to the size of BEA-USA and have substantial financial resources to consummate the proposal and to provide ongoing financial support to BEA-

[16] The discussion of the effectiveness of the anti-money-laundering efforts of Applicants and their home country supervisors is included in the explanation of the Board's assessment of whether Applicants are subject to comprehensive supervision or regulation on a consolidated basis by appropriate authorities in their home country.

[17] 12 U.S.C. § 1842(c)(3)(A).

[18] The CBRC approved ICBC's application to acquire 80 percent of BEA-USA on March 10, 2011.

[19] Commenters expressed concerns regarding ICBC's capital adequacy.

USA. As discussed more fully below, the CBRC requires Chinese banks to follow the Basel I Capital Accord with certain enhancements from the Basel II Capital Accord.[20] The capital levels of ICBC exceed the minimum levels that would be required under the Basel I Capital Accord and are considered to be equivalent to the capital levels that would be required of a U.S. banking organization seeking to acquire an organization of the size and profile of BEA-USA. The Board notes that ICBC engages in a relatively traditional set of commercial banking activities. ICBC's reported asset quality indicators, including nonperforming loans and reserves for loan losses, are consistent with approval of the proposal. ICBC has implemented enhancements to its internal risk management and internal control framework to monitor and manage its asset quality. ICBC's earnings performance also is consistent with approval.

The proposed transaction is structured as a cash purchase of shares. ICBC will use existing resources to fund the purchase of shares and has sufficient financial resources to effect the proposal. BEA-USA is well capitalized and would remain so on consummation. In light of the size of ICBC in relation to BEA-USA, the transaction would have a minimal impact on ICBC's financial condition. In addition, ICBC would have the financial resources to provide continued financial support to BEA USA as needed.

CIC and Huijin are government-owned investment companies that were capitalized by the government of China to invest the government's foreign exchange reserves. CIC's assets are primarily composed of long-term equity investments and financial assets such as equities and fixed-income securities. Huijin invests solely in the shares of Chinese financial institutions.

In considering the managerial resources of the organizations involved and the proposed combined organization, the Board has reviewed the examination records of ICBC's U.S. operations and BEA-USA, including assessments of their management, risk management systems, and operations. The Board has also considered ICBC's plans for implementing the proposal and for the proposed management of BEA-USA after consummation. As noted, the Board has consulted with the CBRC. In addition, the Board has considered the managerial resources and future prospects of CIC and Huijin in light of the fact that CIC and Huijin are government-owned investment companies. The Board also has considered its supervisory experiences and those of the other relevant bank supervisory agencies with the organizations, including consultations in connection with this proposal, and their records of compliance with applicable banking and anti-money-laundering laws. ICBC plans to gradually integrate BEA-USA into its operations and risk management systems, drawing on experiences from its integration of the Bank of East Asia (Canada), Toronto, Canada, which ICBC acquired in 2010. ICBC has represented that it will devote adequate financial and other resources to address all aspects of the post-acquisition integration process for this proposal.

The Board has considered the future prospects of Applicants and BEA-USA in light of their financial and managerial resources and the proposed business plan for BEA USA. ICBC plans to continue BEA-USA's lending and other activities in the markets and communities served by BEA-USA's branches. ICBC's management has the experience and resources to ensure that BEA-USA operates in a safe and sound manner. The Board has also considered the level of capital that Applicants will have on consummation to support BEA-USA's current operations and any future expansion.

[20] The CBRC also requires all large, internationally active banks, such as ICBC, to have a minimum tier 1 risk-based capital ratio of 9 percent and a total risk-based capital ratio of 11.5 percent. ICBC's capital ratios exceed these levels.

In addition, the Board has assessed whether Applicants have provided adequate assurances to provide information to the Board, as required by the BHC Act. Applicants have committed that, to the extent not prohibited by applicable law, they will make available to the Board such information on their operations and the operations of their affiliates that the Board deems necessary to determine and enforce compliance with the BHC Act, the International Banking Act, and other applicable federal laws. Applicants also have committed to cooperate with the Board to obtain any waivers or exemptions that may be necessary to enable them or their affiliates to make such information available to the Board. The Board has consulted with the CBRC about access to information. The CBRC has represented that it would facilitate the Board's access to information, and it has entered into a statement of cooperation with the Board and other U.S. banking regulators with respect to the sharing of supervisory information.[21] Moreover, U.S. bank regulators participated in the November 2009 supervisory college for ICBC hosted by the CBRC.

Based on all the facts of record, the Board has concluded that considerations relating to the financial and managerial resources and future prospects of the organizations involved in the proposal, as well as access to information by the Board, are consistent with approval.

Supervision or Regulation on a Consolidated Basis

In evaluating this application, and as required by section 3 of the BHC Act, the Board has considered whether Applicants are subject to comprehensive supervision or regulation on a consolidated basis by appropriate authorities in their home country.[22] The Board has long held that "the legal systems for supervision and regulation vary from country to country, and comprehensive supervision or regulation on a consolidated basis can be achieved in different ways.[23] In applying this standard, the Board has considered the Basel Core Principles for Effective Banking Supervision ("Basel Core Principles"),[24] which are recognized as the international standard for assessing the quality of bank supervisory systems, including with respect to comprehensive, consolidated supervision ("CCS").[25]

ICBC: For a number of years, authorities in China have continued to enhance the standards of consolidated supervision to which banks in China are subject, including through additional or refined statutory authority, regulations, and guidance; adoption of interna-

[21] *See* Memorandum of Understanding between the CBRC and the Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation, June 17, 2004

[22] 12 U.S.C. § 1842(c)(3)(B). As provided in Regulation Y, the Board determines whether a foreign bank is subject to consolidated home country supervision under the standards set forth in Regulation K. *See*12 CFR 225.13(a)(4). Regulation K provides that a foreign bank is subject to consolidated home country supervision if the foreign bank is supervised or regulated in such a manner that its home country supervisor receives sufficient information on the worldwide operations of the foreign bank (including the relationships of the bank to any affiliate) to assess the foreign bank's overall financial condition and compliance with law and regulation. 12 CFR 211.24(c)(1)(ii). In assessing this standard under section 211.24 of Regulation K, the Board considers, among other indicia of comprehensive, consolidated supervision, the extent to which the home country supervisors: (i) ensure that the bank has adequate procedures for monitoring and controlling its activities worldwide; (ii) obtain information on the condition of the bank and its subsidiaries and offices through regular examination reports, audit reports, or otherwise; (iii) obtain information on the dealings with and relationship between the bank and its affiliates, both foreign and domestic; (iv) receive from the bank financial reports that are consolidated on a worldwide basis or comparable information that permits analysis of the bank's financial condition on a worldwide consolidated basis; (v) evaluate prudential standards, such as capital adequacy and risk asset exposure, on a worldwide basis. No single factor is determinative, and other elements may inform the Board's determination.

[23] 57 *Federal Register* 12992, 12995 (April 15, 1992).

[24] Bank for International Settlements, Basel Committee on Banking Supervision, *Core Principles for Effective Banking Supervision*(October 2006), available at www.bis.org/publ/bcbs129.pdf.

[25] *See*, e.g., 93rd Annual Report of the Board of Governors of the Federal Reserve System (2006), at 76 ("The Core Principles, developed by the Basel Committee in 1997, have become the de facto international standard for sound prudential regulation and supervision of banks.").

tional standards and best practices; enhancements to the supervisory system arising out of supervisory experiences; upgrades to the CBRC in the areas of organization, technological capacity, staffing, and training; and increased coordination between the CBRC and other financial supervisory authorities in China.[26]

The Board has reviewed the record in this case and has determined that the enhancements to standards of bank supervision in China warrant a finding that ICBC is subject to CCS by its home country supervisors. In making this determination, the Board has considered that the CBRC is the principal supervisory authority of ICBC, including its foreign subsidiaries and affiliates, for all matters other than money laundering.[27] The CBRC has primary responsibility and authority for regulating the establishment and activities and the expansion and dissolution of banking institutions, both domestically in China and abroad. The CBRC monitors Chinese banks' consolidated financial condition, compliance with laws and regulations, and internal controls through a combination of on-site examinations, off-site surveillance through the review of required regulatory reports and external audit reports, and interaction with senior management.

Since its establishment in 2003, the CBRC has augmented its supervisory structure, staffing, and internal operations; enhanced its existing supervisory programs; and developed new policies and procedures to create a framework for the consolidated supervision of the largest banks in China. The CBRC also has strengthened its supervisory regime related to accounting requirements and standards for loan classification, internal controls, risk management, and capital adequacy, and it has developed and implemented a risk focused supervisory framework.

The CBRC has issued additional guidance in various supervisory areas, including stricter prudential requirements for capital, loan-loss allowance coverage, executive compensation, banks' equity investments in insurance companies, and enhanced risk-management requirements for operations, liquidity, derivatives, reputational, and market risk. The guidance is designed to make supervision more risk focused and to strengthen practices consistent with the Basel Core Principles.

The CBRC has its head office in Beijing and branch offices in other provinces. The head office sets policy and directs supervisory activities for the largest banks in China, including ICBC. Although some day-to-day supervisory activities are undertaken by the CBRC's branch offices, the head office directs these efforts and ensures consistency of approach through training programs and frequent communication with the branches.

The CBRC head office prepares annual examination plans for the largest Chinese banks, including ICBC. The plans encompass both on- and off-site activities. Applicable Chinese law and banking regulation do not require that on-site examinations be conducted at any specified interval. In practice, the CBRC performs on-site examinations of its largest banks frequently, although off-site surveillance is continuous. On-site examinations are scheduled

[26] The Board has previously approved applications from Chinese banks, including ICBC, to establish U.S. branches under a lower standard than the CCS standard. *See China Merchants Bank Co*., Limited, 94 *Federal Reserve Bulletin* C24 (2008); *Industrial and Commercial Bank of China Limited,*94 *Federal Reserve Bulletin* C114 (2008); *China Construction Bank Corporation*, 95 *Federal Reserve Bulletin* B54 (2009); and *Bank of Communications Co., Ltd.*(order dated April 8, 2011), 97 *Federal Reserve Bulletin* 49 (2nd Quar. 2011). In each case, the Board made a determination that the bank's home country supervisors were actively working to establish arrangements for the consolidated supervision of the bank. 12 U.S.C.§ 3105(d)(6).

[27] Before April 2003, the People's Bank of China ("PBOC") acted as both China's central bank and primary banking supervisor, including with respect to anti-money-laundering matters. In April 2003, the CBRC was established as the primary banking supervisor and assumed the majority of the PBOC's bank regulatory functions. The PBOC maintained its roles as China's central bank and primary supervisor for anti-money-laundering matters.

based on the CBRC's continuous off-site monitoring tools, analysis of the institution's periodic filings, results of the institution's internal stress testing, and the institution's overall risk profile and activities. On-site examinations by the CBRC typically cover, among other things, the major areas of operation: corporate governance and senior management responsibilities; capital adequacy; asset structure and asset quality (including structure and quality of loans); off-balance-sheet activities; earnings; liquidity; liability structure and funding sources; expansionary plans; internal controls (including accounting control and administrative systems); legal compliance; accounting supervision and internal auditing; and any other areas deemed necessary by the CBRC. The PBOC examines ICBC for compliance with anti-money-laundering laws and requirements.

Examination ratings are based on the CAMELS rating model and emphasize credit-risk management, the quality of the bank's loan portfolio, internal controls, liability structure, capital adequacy, liquidity, and the adequacy of reserves. The areas of emphasis reflect the fact that the largest Chinese banks, including ICBC, engage in traditional commercial banking and are not materially engaged in complex derivatives or other activities. Ratings are derived from off-site quantitative and qualitative analysis and on site risk reviews. Examination findings and areas of concern are discussed with senior management of the bank, and corrective actions taken by the bank are monitored by the CBRC. In 2009, the CBRC developed an information technology system to assist in on-site examinations by improving data analysis and regulatory information sharing.

Chinese banks are required to report key regulatory indicators to the CBRC periodically on general schedules. All Chinese banks are required to submit monthly, quarterly, semiannual, or annual reports relating to asset quality, lending concentrations, capital adequacy, earnings, liquidity, affiliate transactions, off-balance-sheet exposures, internal controls, and ownership and control.

Banks must report to the CBRC their unconsolidated capital adequacy ratios quarterly and their consolidated ratios semiannually. China's bank capital rules are based on the Basel I Capital Accord, while taking into account certain aspects of the Basel II Capital Accord. In addition, the CBRC, as a member of the Basel Committee on Banking Supervision, has supported the Basel III Capital Accord framework and implementation time frame. The CBRC can take enforcement actions when capital ratios or other financial indicators fall below specified levels. These actions may include issuing supervisory notices, requiring the bank to submit and implement an acceptable capital replenishment plan, restricting asset growth, requiring reduction of higher risk assets, restricting the purchase of fixed assets, and restricting dividends and other forms of distributions. Significantly undercapitalized banks may be required to make changes in senior management or restructure their operations.

ICBC, like other large Chinese banks, is required to be audited annually by an external accounting firm that meets the standards of Chinese authorities, including the Ministry of Finance, PBOC, and CBRC, and the audit results are shared with the CBRC and PBOC. The scope of the required audit includes a review of ICBC's financial statements, asset quality, capital adequacy, internal controls, and compliance with applicable laws. At its discretion, the CBRC may order a special audit at any time. In addition, in connection with its listing on the Shanghai and Hong Kong stock exchanges, ICBC is required to report financial statements under both International Financial Reporting Standards ("IFRS") and Chi-

nese Accounting Standards ("CAS").[28] These financial statements are audited by an international accounting firm under applicable IFRS auditing standards.[29]

ICBC conducts internal audits of its offices and operations, including its overseas operations, generally on an annual schedule. The internal audit results are shared with the CBRC, the PBOC, and ICBC's external auditors.

Chinese law imposes various prudential limitations on banks, including limits on transactions with affiliates and on large exposures.[30] Related-party transactions include credit extensions, asset transfers, and the provision of any type of services. Chinese banks are required to adopt appropriate policies and procedures to manage related-party transactions and the board of directors must appoint a committee to supervise such transactions and relationships. Applicable laws require all related-party transactions to be conducted on an arm's-length basis.

Chinese banking law also establishes single-borrower credit limits. Loans to a single borrower may not exceed 10 percent of the bank's total regulatory capital, the aggregate lending to a group of related companies may not exceed 15 percent of the bank's total regulatory capital, and the aggregate amount of credit granted to all related parties may not exceed 50 percent of the bank's total regulatory capital. The status of related-party transactions must be reported to the CBRC quarterly.

In addition, the CBRC has certain operational limitations for commercial banks in China relating to matters such as liquidity and foreign currency exposure. In 2009, the CBRC issued new rules concerning liquidity management and corporate governance. Compliance with these limits is monitored by the CBRC through periodic reports and reviewed during on-site examinations.

[28] Based primarily on newspaper reports, several commenters criticized the reliability and accuracy of Chinese accounting methods. These newspaper articles focus on Chinese firms that are listed on U.S. exchanges through a process called "reverse mergers" whereby the Chinese firm acquires a listed U.S. firm and thereby becomes a listed firm. These articles allege that the listed Chinese firms have reported unreliable financial statements audited by Chinese auditing firms. China's largest banks, such as ICBC, use the "Big Four" accounting firms. There is no evidence that Chinese accounting methods or practices at the large Chinese banks, such as ICBC, are unreliable. The International Monetary Fund's ("IMF") financial system stability assessment report and the accompanying detailed assessment report of observance with the Basel Core Principles, discussed in detail below, both found that "[s]ince 2005, [CAS] have substantially converged with [IFRS] and International Standards on Auditing, respectively." IMF, People's Republic of China, Financial System Stability Assessment at 57 (June 24, 2011); IMF and World Bank, People's Republic of China: Detailed Assessment Report of Observance with Basel Core Principles for Effective Banking Supervision at 9 (April 2012). In addition, the World Bank Report on Observance of Standards and Codes determined that CAS and IFRS are basically compatible and that the Chinese authorities and the International Accounting Standards Board have established a continuing convergence mechanism designed to achieve full convergence in 2012. World Bank, Report on Observance of Standards and Codes (ROSC) Accounting and Auditing – People's Republic of China at Executive Summary and at 12 (October 2009), available at www.worldbank.org/ifa/rosc_aa_chn.pdf.

[29] The commenters also asserted that the "Big Four" accounting firms in the United States, including the parent company of ICBC's auditor, Ernst & Young, were substantially fined for departing from U.S. generally accepted accounting principles ("U.S. GAAP"). The commenters argued, without providing any supporting data, that any operational deficiencies in the United States by Ernst & Young should be imputed to ICBC's auditor and financial statements, and they requested that the Board require ICBC to submit financial data audited by a fully independent auditing firm that has not been the subject of substantial criticisms by the Public Company Oversight Accounting Board ("PCAOB") or other regulatory body. The Board notes that the PCAOB did sanction Ernst & Young for failing to properly evaluate a specific company's sales returns reserves, which the PCAOB found were both a material component of that company's financial statements and not in conformity with U.S. GAAP. The PCAOB did not find that this was a widespread practice by Ernst & Young or indicative of behavior by any of its foreign accounting operations.

[30] The CBRC definition of an "affiliate" or a "related party" of a bank includes subsidiaries, associates/joint ventures, shareholders holding 5 percent or more of the bank's shares, and key management personnel (and immediate relatives) and those individuals' other business affiliations.

The CBRC is authorized to require any bank to provide information and to impose sanctions for failure to comply with such requests. If the CBRC determines that a bank is not in compliance with banking regulations and prudential standards, it may impose various sanctions depending upon the severity of the violation. The CBRC may suspend approval of new products or new offices, suspend part of the bank's operations, impose monetary penalties, and in more serious cases, replace management of the bank. The CBRC also has authority to impose administrative penalties, including warnings and fines for violations of applicable laws and rules. Criminal violations are transferred to the judicial authorities for investigation and prosecution.

ICBC is subject to supervision by several other financial regulators, including the State Administration for Foreign Exchange, China Securities Regulatory Commission ("CSRC"), and China Insurance Regulatory Commission ("CIRC"). These agencies receive periodic financial and operations reports, and they may conduct on-site examinations and impose additional reporting requirements. Chinese financial supervisors coordinate supervision and share supervisory information about Chinese financial institutions as appropriate.

Authorities in China also have increased cooperation with international groups and supervisory authorities in other countries regarding bank supervision. In particular, the CBRC has established mechanisms to cooperate with supervisory authorities in at least 25 other countries for the supervision of cross-border banking. In addition, the PBOC and CBRC officially joined the Basel Committee on Banking Supervision on behalf of China and since their accession, have actively participated in the revision of the Basel II Capital Accord, in the formulation of the Basel III Capital Accord, and in other working groups. China also is active in the ongoing work of the Financial Stability Board. In addition, the PBOC, CBRC, other financial supervisory agencies, and other agencies in China have taken joint measures to maintain financial stability.[31] Moreover, authorities in the United States and China that are responsible for the oversight of auditing services for public companies are engaged in continuing discussions with respect to enhancing cross-border cooperation, and the Board looks forward to timely negotiation of an agreement relating to cooperative actions by these authorities.

The IMF recently concluded a financial system stability assessment of China ("FSSA"), including an assessment of China's compliance with the Basel Core Principles.[32] The FSSA determined that China's overall regulatory and supervisory framework adheres to international standards.[33] The FSSA found that "[t]he laws, rules and guidance that CBRC operates under generally establish a benchmark of prudential standards that is of high quality and was drawn extensively from international standards and the [Basel Core Principles]

[31] China has established a system of preliminary indicators for monitoring financial stability, developed methodology and operational frameworks for monitoring financial risks, and published an annual China Financial Stability Report since 2005.

[32] The assessment reflects the regulatory and supervisory framework in place as of June 24, 2011. IMF, People's Republic of China, Financial System Stability Assessment (June 24, 2011), available at www.imf.org/external/pubs/ft/scr/2011/cr11321.pdf. The FSSA covers an evaluation of three components: (1) the source, probability, and potential impact of the main risks to macrofinancial stability in the near term; (2) the country's financial stability policy framework; and (3) the authorities' capacity to manage and resolve a financial crisis should the risks materialize. The FSSA is a key input to IMF surveillance. The FSSA is a forward-looking exercise, unlike the Board's assessment of the comprehensive, consolidated supervision of an applicant.

The IMF and World Bank separately publish a detailed assessment of the country's observance of the Basel Core Principles that discusses the country's adherence to the Basel Core Principles in much greater detail. *See* IMF and World Bank, People's Republic of China: Detailed Assessment Report of Observance with Basel Core Principles for Effective Banking Supervision (April 2012) ("DAR"), available at www.imf.org/external/pubs/ft/scr/2012/cr1278.pdf.

[33] FSSA at 39.

themselves."[34] The FSSA additionally noted that "[c]onsolidated supervision of banks and their direct subsidiaries and branches on the mainland or offshore is of high quality."[35] With respect to the CBRC, the FSSA found as follows:All the banks, auditors, ratings agencies and other market participants that the mission interacted with were unhesitating in their regard for the role that the CBRC has played in driving professionalism, risk management and international recognition of the Chinese banking system. In particular, the mission observed that [the CBRC] has been the key driving force in driving improvements in risk management, corporate governance and internal control and disclosure in Chinese banks.[36]

Based on its review, the FSSA rated China's overall compliance with the Basel Core Principles as satisfactory. In giving this overall rating, the FSSA noted several areas that merited improvement and made specific recommendations for continued advances in supervision and regulation.[37] The Chinese authorities noted that some of the recommendations of the FSSA are already being implemented, and others will be taken into account in the CBRC's plans to improve supervisory effectiveness.[38]

The Board has taken into account the FSSA's views that China is, overall, in satisfactory compliance with the Basel Core Principles and that there are areas for further improvement. The Board has also taken into account the responses by Chinese authorities to the FSSA report and the progress made by Chinese authorities to address the issues raised in that report.

Based on all the facts of record, including its review of the supervisory framework implemented by the CBRC for ICBC, the Board has determined that ICBC is subject to comprehensive supervision on a consolidated basis by its home country supervisors. This determination is specific to ICBC.[39] By statute, the Board must review this determination in processing future applications involving ICBC and also must make a determination of comprehensive, consolidated supervision in other applications involving different applicants from China.

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[34] FSSA at 59; DAR at 12.

[35] FSSA at 64; DAR at 16.

[36] DAR at 7.

[37] FSSA at 39-42 and 69-71; DAR at 99-101. China received a materially noncompliant rating in two of the thirty areas assessed by the FSSA. Specifically, the FSSA rated China as materially noncompliant for the Basel Core Principles on independence, accountability and transparency, and risk management process. DAR at 17 and 19. The FSSA stated that "budgeting arrangements, external headcount approval requirements and [the authority for the State Council to override] rules and decisions compromise CBRC effectiveness and could affect operational independence." FSSA at 64; DAR at 17. The FSSA viewed the guidance that the CBRC has issued in risk management to be consistent with international standards but found that banking institutions' compliance with CBRC guidance was lacking (although recognizing that the guidance on some risks "is recent and so could not be expected to be complied with as yet"). FSSA at 61; *see also* DAR at 53. The assessment team also believed that Chinese banks in general do not yet have robust enterprise-wide risk-management systems. FSSA at 66; DAR at 53-54. For comparison, the United Kingdom and Germany received three and two materially noncompliant ratings, respectively, and the United States received one materially noncompliant rating, in their recent financial system stability assessments.

[38] FSSA at 71-73; DAR at 101-103. Chinese authorities responded that, by law in China, the State Council of the People's Republic of China ("State Council") may alter or annul a rule or guideline of the CBRC only if the rule or guideline violates applicable law and that the State Council has never altered or annulled the rules and guidelines issued by the CBRC. Chinese authorities also noted that the State Council has supported the CBRC in undertaking banking regulation and supervision and that the CBRC has upgraded the number and quality of its staff over time. FSSA at 71-72; DAR at 102. In addition, Chinese authorities noted the significant improvements China has made in supervision as well as the relative simplicity of the Chinese banking system. FSSA at 72; DAR at 102-3. Despite the difference in views about the degree to which Chinese banks' risk management is commensurate with the current risk environment, Chinese authorities concurred with the FSSA that "continued improvements in banks' risk management are needed, as financial reform deepens and liberalization creates greater interconnectedness and complexities in the Chinese system." FSSA at 72; DAR at 103.

[39] *See* 58 *Federal Register* 6348, 6349 (January 12, 1993).

As part of the Board's supervisory program for foreign banks, the Board actively monitors changes to the supervisory systems in the home countries of foreign banks, as well as differences that may exist in the supervisory framework as it is applied by a home country to institutions of different types or sizes, and would continue to do so with respect to China. The Board also intends to further its relationship with Chinese supervisory authorities and continue to develop its understanding of Chinese banking matters.

CIC and Huijin: In connection with a prior application, the Board determined that CIC was subject to an appropriate type and level of CCS by its home country authorities, given its unique nature and structure.[40] There have been no material changes in the manner in which CIC is supervised or regulated by its home country authorities since the previous determination. Based on this and all the facts of record, the Board has determined that CIC continues to be subject to CCS.

The Board has not made a CCS determination with respect to Huijin. In the CIC Order, the Board noted that the system of comprehensive supervision or regulation may vary, depending on the nature of the acquiring company and the proposed investment.[41] The Board believes that, like CIC, Huijin is subject to an appropriate type and level of comprehensive regulation on a consolidated basis, given its unique nature and structure.

Huijin is a joint stock company established to invest in Chinese financial institutions and is wholly owned by the government of China through CIC.[42] Huijin's articles of association do not permit it to conduct any other commercial activities or interfere in the day-to-day business of the financial institutions it controls. Huijin is governed by a five-member board of directors and a three-member board of supervisors. As is the case with CIC, the members are appointed by the State Council.

Oversight of the operations of CIC and Huijin by the State Council and other agencies of the Chinese government allows for review of the worldwide investment strategy and portfolio of CIC and of Huijin's role as a major shareholder of Chinese financial institutions. On this basis, appropriate authorities in China would appear to have full access to and oversight of Huijin and its activities.

The Board also has taken into account that CIC and Huijin are not operating entities and that CIC's and Huijin's proposed investment in BEA-USA would be indirect and through a substantial foreign bank supervised and regulated by the CBRC. CIC and Huijin have represented that they do not directly engage in the business of banking and do not intervene in the day-to-day business operations of the Chinese financial institutions in which Huijin invests. CIC and Huijin have further represented that they were not involved in the decision by ICBC to enter into the proposed acquisition of BEA-USA or in the negotiation of the terms of the investment, and they conducted no additional due diligence on BEA-USA.

Based on all the facts of record, the Board has determined that Huijin is subject to comprehensive supervision on a consolidated basis by its appropriate home country authorities for purposes of this application.

Efforts to Ensure Against Money Laundering: The government of China has adopted a statutory regime regarding anti-money laundering ("AML") and suspicious activity reporting and has criminalized money-laundering activities and other financial crimes. The

[40] CIC Order.

[41] *Id*. at B33.

[42] Both CIC and Huijin have stated that there is a strict firewall between the two companies regarding their investment activities.

PBOC supervises and examines Chinese banks with respect to AML and coordinates efforts among other agencies.[43] The PBOC collects, monitors, analyzes, and disseminates suspicious transaction reports and large-value transaction reports.

The PBOC over time has increased requirements for its supervised institutions regarding AML compliance. The PBOC issued rules providing clarification of, or further strengthening the implementation of, operating procedures, customer due diligence and risk classification, recordkeeping, AML monitoring and reporting suspicious transactions, and the international remittance agency business. The PBOC also requires the designation of a chief AML compliance officer as a high-level manager to ensure provision of adequate AML resources and timely flow of information to employees responsible for AML compliance throughout the institution. In addition, the PBOC requires the risk rating of customers and the filing of reports on suspicious activity and certain other transactions. Banks are required to (1) establish a customer identification system, in accordance with applicable rules jointly promulgated by the PBOC and three functional financial services regulators;[44] (2) record the identities of customers and information relating to each transaction; and (3) retain retail transaction documents and books. Supervised institutions have been encouraged to move beyond a prescriptive-criteria basis to include a more expansive and risk-based approach to suspicious activity detection and reporting.

China participates in international fora that address the prevention of money laundering and terrorist financing. China became a member of the Financial Action Task Force ("FATF") in June 2007. China also is a member of the Eurasian Group ("EAG"), a FATF-style regional body that supports member countries in their efforts to create and maintain an appropriate legal and institutional framework to combat money laundering and terrorist financing in line with FATF standards.[45] EAG evaluates its member states' AML and counter-terrorist-financing ("CFT") systems for compliance with international standards.[46] In the most recent mutual evaluation report of China, dated February 17, 2012, the FATF considered China to be fully or largely compliant with almost all of the FATF recommendations and held that China has effective AML and CFT systems in force. As a result, the FATF has removed China from its regular follow-up process.[47]

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[43] As noted above, Huijin and CIC are investment vehicles that make investments in companies and debt securities and are directly overseen by a variety of government agencies in China, including the National Audit Office and the State Council.

[44] Those regulators are the CBRC, CSRC, and CIRC.

[45] China also is a party to other agreements that address money laundering or terrorist financing, including the U.N. Convention Against the Illicit Traffic of Narcotics and Psychotropic Substances, the U.N. Convention Against Transnational Organized Crime, the U.N. Convention Against Corruption, and the U.N. International Convention for the Suppression of the Financing of Terrorism.

[46] A commenter alleged that Chinese authorities have failed in the past to supervise Chinese banks operating in Macau SAR with respect to AML matters and referred to sanctions imposed on a Macau bank by the U.S. Department of the Treasury in 2007. The commenter also alleges that money-laundering risks exist in China because the follow-up reports to the mutual evaluation of China's progress in implementing recommendations of the FATF, undertaken by the EAG, rated China to be non-compliant or partially compliant on certain FATF recommendations. On this basis, the commenter requests that the Board delay any action on these applications until China is in full compliance with all recommendations of the FATF. This comment was submitted before the issuance of the most recent evaluation report on China, which found China to be largely compliant with FATF's AML requirements.

[47] FATF, China Mutual Evaluation 8th Follow-up Report, Anti-Money Laundering and Combating the Financing of Terrorism (February 17, 2012), available at www.fatf gafi.org/dataoecd/5/34/49847246.pdf. The report noted that China has made significant progress to address the remaining deficiencies and has "reached a satisfactory level of compliance with all six core Recommendations and eight of the [ten] key Recommendations." *Id*at para. 41. In one of the key Recommendations where China has not attained a satisfactory level of compliance (implementation of international instruments related to terrorist financing), China has substantially addressed part of the deficiency and continues to make progress. With respect to the other key Recommendation (freezing of terrorist-related assets), China has made significant progress since June 2011 to improve its implementation. In particular, China has implemented legislation establishing a legislative framework and

Moreover, the Chinese government issues rules on implementing United Nations sanctions and may take enforcement actions to ensure compliance with those sanctions. The PBOC is also responsible for disseminating information to the banking industry regarding U.N. sanctions and supervising the enforcement of those sanctions.

The PBOC supervises and regulates compliance by ICBC with AML requirements through a combination of on-site examinations and off-site monitoring. On site examinations focus on ICBC's compliance with AML laws and rules. The PBOC's headquarters conducts investigations of a financial institution's head office, and the PBOC's branches conduct investigations of the institution's branch offices in the same locality as the PBOC branches. During the course of an on-site examination, the PBOC will generally review account information, transaction records, and any other relevant materials. Upon completion of an investigation, if AML deficiencies are identified, the PBOC may issue sanctions and propose that remedial measures be imposed by appropriate government agencies or regulators against the financial institution and can refer any suspected money laundering to law enforcement authorities for further investigation. The PBOC performs off site monitoring through periodic reports and has established requirements for Chinese banks to submit such reports. In order to improve off-site supervision and monitoring of large-amount cash transactions, the PBOC developed an interactive information technology system for AML/CFT supervision that has been in operation since October 2010 in both the PBOC and financial institutions.

ICBC has policies and procedures to comply with Chinese laws and rules regarding AML. ICBC states that it has implemented measures consistent with the institution-specific recommendations of the FATF and that it has put in place policies, procedures, and controls to ensure ongoing compliance with all statutory and regulatory requirements, including designating AML compliance personnel and conducting routine employee training at all ICBC branches. ICBC's compliance with AML requirements is monitored by the PBOC and by ICBC's internal and external auditors. On consummation, BEA-USA's operations will be integrated into ICBC's global regulatory compliance system, which includes compliance with U.S. law.

Based on all the facts of record, the Board has determined that the AML efforts by Applicants and their home country supervisors are consistent with approval.

Convenience and Needs Considerations

In acting on a proposal under section 3 of the BHC Act, the Board also must consider the effects of the proposal on the convenience and needs of the communities to be served and take into account the records of the relevant insured depository institutions under the Community Reinvestment Act ("CRA").[48] 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, 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.[49]

administrative authority for enforcement and it has responded to foreign requests to freeze assets. The FATF was of the view that China should enact additional guidance to improve implementation, and Chinese authorities are currently drafting rules to do so. *Id* . at paras. 150-52 and 157-59.

[48] 12 U.S.C.§ 2901 et seq.; 12 U.S.C. § 1842(c)(2).

[49] 12 U.S.C.§ 2903.

The Board has considered all the facts of record, including evaluations of the CRA performance record of BEA-USA, data reported by BEA-USA under the Home Mortgage Disclosure Act ("HMDA"),[50] as well as other information provided by ICBC, confidential supervisory information, and public comments received on the proposal. Several commenters requested that the Board bar ICBC from expanding BEA-USA's existing branch network for a three- to five-year period and require ICBC to develop a comprehensive CRA plan to ensure that BEA-USA effectively serves all minority and underserved communities. Several commenters also requested that the Board require ICBC to submit a CRA plan or enter into commitments that will ensure BEA-USA provides service to all underserved and minority communities in its service areas.[51] In addition, several commenters raised concerns that BEA-USA might exclude African Americans, Hispanics, and Southeast Asians in the provision of its products and services. Other commenters alleged that BEA-USA excludes African Americans and Hispanics with respect to its home mortgage lending.

A. CRA Performance Evaluations

As provided in the CRA, the Board has considered the convenience and needs factor in light of the evaluations by the appropriate federal supervisors of the CRA performance record of the relevant insured depository institutions, including BEA-USA. 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.[52] As previously noted, CIC and Huijin control Bank of China Limited, which has two grandfathered federal branches whose deposits are insured by the FDIC. The branches received a "satisfactory" rating at their most recent CRA performance evaluation by the FDIC, as of August 18, 2008.[53] BEA-USA received an "outstanding" rating at its most recent CRA performance evaluation by the OCC, as of January 4, 2010.[54] BEA-USA received an "outstanding" rating under each of the lending and community development tests.[55] Examiners noted that a substantial majority of BEA-USA's loans were originated in its assessment areas, that the distribution of its loans reflects excellent penetration among businesses of different sizes in the assessment areas, and that the geographic distribution of loans reflects excellent dispersion throughout the assessment areas. Examiners also reported that BEA-USA's community development performance demonstrates excellent responsiveness to the needs of the assessment areas through loans, investments, and services.[56] ICBC has represented that it initially intends to maintain BEA-USA's existing business and will be prepared to expand offerings for BEA-USA's customers in the future.

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[50] 12 U.S.C. §§ 2801-2810.

[51] The Board consistently has stated that neither the CRA nor the federal banking agencies' CRA regulations require depository institutions to make pledges or enter into commitments or agreements with any organization and that the enforceability of any such third-party pledges, initiatives, and agreements are matters outside the CRA. *See Bank of America Corporation* , 90 *Federal Reserve Bulletin* 217, 232-33 (2004).

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

[53] ICBC's uninsured branch and the uninsured branches of other Chinese banks controlled by CIC and Huijin are not subject to the CRA.

[54] The evaluation period was January 1, 2006, to January 4, 2010.

[55] BEA-USA was evaluated under the intermediate small bank performance criteria, which only include a lending test and a community development test.

[56] For example, in the New York assessment area, BEA-USA made 15 community development loans totaling $18.6 million, including 5 loans for affordable housing, and 22 qualified investments totaling approximately $2.6 million, which consisted of $2.5 million in Fannie Mae investments and $100,000 in charitable donations. BEA-USA's staff also provided community development services during the review period, including financial literacy and homeownership seminars.

B. HMDA and Compliance with Fair Lending and Other Consumer Protection Laws

The Board has considered the HMDA data for 2009, 2010, and 2011 reported by BEA-USA in its combined assessment areas and the fair lending record of BEA-USA in light of public comments received on the proposal.[57] Several commenters alleged, based on HMDA data reported in 2009, that BEA-USA had engaged in disparate treatment of minority individuals in its one- to four-family home mortgage lending. Specifically, the commenters asserted that BEA-USA excludes African Americans and Hispanics in home purchase and refinance lending and that it discriminates against Asian Americans with incomes below 100 percent of the median income of the metropolitan statistical area in its refinance lending.

BEA-USA is predominantly a commercial lender and makes a limited number of one- to four-family mortgage loans. Its one- to four-family mortgage lending largely results from walk-in traffic at the bank's branches, most of which are in Asian American neighborhoods. Throughout its combined assessment areas, BEA-USA made 32 one- to four family mortgage loans in 2009, 26 in 2010, and 20 in 2011. During that same time period, BEA-USA received only one application for a one- to four-family mortgage loan from an African American and four applications from Hispanics. The HMDA data also indicate that BEA-USA made a material percentage of its one- to four-family mortgage loans to LMI borrowers (those with incomes of less than 80 percent of the area median income) in the bank's assessment areas. Between 2009 and 2011, 21 percent of BEA-USA's mortgage refinance loans and 35 percent of BEA-USA's conventional home purchase loans were made to LMI borrowers.[58]

Although the HMDA data might reflect certain disparities in the rates of loan applications, originations, denials, or pricing among members of different racial or ethnic groups in certain local areas, they provide an insufficient basis by themselves on which to conclude whether or not BEA-USA is excluding or imposing higher costs on any racial or ethnic group on a prohibited basis. The Board recognizes that HMDA data alone, even with the recent addition of pricing information, provide only limited information about the covered loans.[59] HMDA data, therefore, have limitations that make them an inadequate basis, absent other information, for concluding that an institution has engaged in illegal lending discrimination.

The Board is nevertheless concerned when HMDA data for an institution indicate disparities in lending and believes that all lending institutions are obligated to ensure that their lending practices are based on criteria that ensure not only safe and sound lending but also equal access to credit by creditworthy applicants regardless of their race or ethnicity. Moreover, the Board believes that all bank holding companies and their affiliates should conduct mortgage lending operations that are free of abusive lending practices and in compliance with all consumer protection laws.

[57] BEA-USA's combined CRA assessment areas consist of Kings, Manhattan, and Queens Counties, which are in the New York-New Jersey-Long Island, NY-NJ-PA Metropolitan Statistical Area; the entire San Francisco-San Mateo-Redwood City, California Metropolitan Division and the Alameda County portion of the Oakland-Fremont-Hayward, CA Metropolitan Division, both of which are part of the greater San Francisco-Oakland-Fremont, California Metropolitan Statistical Area; and the entire Los Angeles-Long Beach-Glendale Metropolitan Division.

[58] More than one-half of BEA-USA's branches are in low- to moderate-income communities.

[59] The data, for example, do not account for the possibility that an institution's outreach efforts may attract a larger proportion of marginally qualified applications than other institutions attract and do not provide for an independent assessment of whether an applicant who was denied credit was, in fact, creditworthy. In addition, credit history problems, excessive debt levels relative to income, and high loan amounts relative to the value of the real estate collateral (reasons most frequently cited for a credit denial or higher cost credit) are not available from HMDA data.

Because of the limitations of HMDA data, the Board has considered these data and taken into account other information, including examination reports that provide evaluations of compliance by BEA-USA with consumer protection laws. The Board also has consulted with the OCC, BEA-USA's primary federal supervisor.

The record of this application, including confidential supervisory information, indicates that BEA-USA has taken steps to ensure compliance with fair lending and other consumer protection laws and regulations. In BEA-USA's most recent CRA Performance Evaluation, examiners noted "no evidence of discriminatory or other illegal credit practices...." [60] In addition, BEA-USA's loan policies include information on prohibited discriminatory lending practices. BEA-USA's advertising and marketing policy contains specific guidance on practices that employees should avoid that would tend to discourage loan applicants on a prohibited basis. Additionally, the bank's employees involved in lending are required to participate in annual training that includes compliance with fair lending laws and other applicable laws and regulations. Moreover, ICBC has stated it intends to conduct a full review of BEA-USA's risk-management program for fair lending compliance after consummation of the proposal.

C. Conclusion on Convenience and Needs and CRA Performance

The Board has considered all the facts of record, including evaluations of the CRA performance record of BEA-USA and other relevant insured depository institutions, information provided by ICBC and BEA-USA, comments received on the proposal, and confidential supervisory information. Based on a review of the entire record, the Board concludes that considerations relating to the convenience and needs factor and the CRA performance records of the relevant insured depository institutions are consistent with approval.

Financial Stability

The Dodd-Frank Wall Street Reform and Consumer Protection Act amended section 3 of the BHC Act to require the Board also to consider "the extent to which a proposed acquisition, merger, or consolidation would result in greater or more concentrated risks to the stability of the United States banking or financial system." [61]

Financial Stability Standard

In reviewing applications and notices under sections 3 and 4 of the BHC Act, the Board expects that it will generally find a significant adverse effect if the failure of the resulting firm, or its inability to conduct regular-course-of-business transactions, would likely impair financial intermediation or financial market functioning so as to inflict material damage on the broader economy. This kind of damage could occur in a number of ways, including seriously compromising the ability of other financial institutions to conduct regular course-of-business transactions or seriously disrupting the provision of credit or other financial services.

On the other hand, certain types of transactions likely would have only a *de minimis* impact on an institution's systemic footprint and, therefore, are not likely to raise concerns about financial stability. For example, a proposal that involves an acquisition of less than

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[60] The Bank of East Asia, USA, National Association Community Reinvestment Act Performance Evaluation, January 4, 2010, at 5. Moreover, the CRA Performance Evaluation noted that BEA-USA's assessment areas do not arbitrarily exclude LMI areas. *Id* . at 4.

[61] Section 604(d) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376, codified at 12 U.S.C. § 1842(c)(7).

$2 billion in assets, results in a firm with less than $25 billion in total assets, or represents a corporate reorganization may be presumed not to raise financial stability concerns absent evidence that the transaction would result in a significant increase in interconnectedness, complexity, cross-border activities, or other risk factor.

Analysis of the Financial Stability Impact of this Proposal

In this case, the proposal would have a *de minimis* impact on Applicants' systemic footprint because BEA-USA has consolidated assets of approximately $780 million. The acquisition of BEA-USA would not meaningfully increase ICBC's size. The proposal also would not add any significant complexity to the overall operations of ICBC as BEA USA is a traditional commercial bank that focuses largely on commercial lending. As noted above, ICBC operates subsidiary banks worldwide, including in the United Kingdom and Canada. While BEA-USA would add to ICBC's cross-border activities, BEA-USA operates only in the United States and ICBC already engages in banking and financial services in the United States through its New York branch, which has assets of $1.5 billion, and its subsidiary U.S. broker-dealer.[62] Moreover, neither ICBC nor BEA-USA is a major provider of any product or service that the Board believes has the potential to be critical to the functioning of the U.S. financial system. Finally, the extent of BEA-USA's interconnectedness with the U.S. financial system and its contribution to the complexity of the U.S. financial system are both sufficiently small to be considered *de minimis*.

Based on these and all the other facts of record, the Board has determined that considerations relating to financial stability are consistent with approval.

Conclusion

Based on the foregoing and all the facts of record, the Board has approved the application by Applicants to acquire up to 80 percent of the voting shares of BEA-USA pursuant to section 3(a)(1) of the BHC Act. In reaching its conclusion, the Board has considered all the facts of record in light of the factors that it is required to consider under the BHC Act and other applicable statutes.[63] The Board conditions its decision on Applicants providing to the Board adequate information on their operations and activities as well as those of their affiliates to determine and enforce compliance by Applicants or their affiliates with applicable federal statutes. Should any restrictions on access to information on the operations or activities of Applicants or any of their affiliates subsequently interfere with the Board's ability to obtain information to determine and enforce compliance by Applicants or their affiliates with applicable federal statutes, the Board may require termination or divestiture of any of Applicants' or their affiliates' direct or indirect activities in the United States.

The Board's approval is specifically conditioned on compliance by Applicants with the conditions imposed in this order and the commitments made to the Board in connection with the application.[64] For purposes of this action, the conditions and commitments are deemed

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[62] ICBC has not been designated a global systemically important bank by the Basel Committee on Banking Supervision.

[63] Commenters also requested that the Board extend the comment period on the proposal. The Board already extended the comment period with respect to certain matters for ten days, allowing the commenters more than thirty-six days to submit comments. In the Board's view, the commenters have had ample opportunity to submit their views and, in fact, have provided written submissions that the Board has considered in acting on the proposal. Based on a review of all the facts of record, the Board has concluded that the record in this case is sufficient to warrant action at this time and that further delay in considering the proposal, extension of the comment period, or denial of the proposal on the grounds discussed above, is not warranted.

[64] Commenters requested that the Board hold a public meeting or hearing on the proposal. Section 3(b) of the BHC Act does not require the Board to hold a public hearing on an application unless the appropriate supervi-

to be conditions imposed in writing by the Board in connection with its findings and decision herein and, as such, may be enforced in proceedings under applicable law.[65]

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 New York, acting pursuant to delegated authority.

By order of the Board of Governors, effective May 9, 2012.

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

Robert deV. Frierson
Deputy Secretary of the Board

Orders Issued Under International Banking Act

Agricultural Bank of China Limited
Beijing, People's Republic of China

Order Approving Establishment of a Branch
FRB Order No. 2012–5 (May 9, 2012)

Agricultural Bank of China Limited ("ABC"), Beijing, People's Republic of China, a foreign bank within the meaning of the International Banking Act ("IBA"), has applied under section 7(d) of the IBA[1] to establish a state-licensed branch in New York, New York. The Foreign Bank Supervision Enhancement Act of 1991, which amended the IBA, provides that a foreign bank must obtain the approval of the Board to establish a branch in the United States.

Notice of the application, affording interested persons an opportunity to comment, has been published in a newspaper of general circulation in New York, New York (*The New York Post*, October 4, 2010). The time for filing comments has expired, and the Board has considered all comments received.

sory authority for the bank to be acquired makes a timely written recommendation of denial of the application. 12 CFR 225.16(e). The Board has not received such a recommendation from those authorities. Under its rules, the Board also may, in its discretion, hold a public meeting or hearing on an application to acquire a bank if necessary or appropriate to clarify material factual issues related to the application and to provide an opportunity for testimony. 12 CFR 225.16(e), 262.25(d). The Board has considered the commenters' requests in light of all the facts of record. In the Board's view, the commenters had ample opportunity to submit their views and, in fact, submitted written comments that the Board has considered in acting on the proposal. The commenters' requests fail to demonstrate why written comments do not present their views adequately or why a meeting or 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 meeting or hearing is not required or warranted in this case. Accordingly, the requests for a public meeting or hearing on the proposal are denied.

[65] Commenters asserted that the proposal would raise national security concerns. The Board notes that Congress has provided other U.S. agencies the authority to review national security issues in proposals by foreign companies to acquire U.S. companies. Commenters raised additional concerns that address matters beyond the statutory factors the Board is authorized to consider. *See Western Bancshares, Inc. v. Board of Governors*, 480 F.2d 749 (10th Cir. 1973).

[1] 12 U.S.C. § 3105(d).

ABC, with total assets of approximately $1.85 trillion, is the fourth largest bank in China.[2] The government of China owns approximately 83 percent of ABC's shares.[3] No other shareholder owns more than 5 percent of the shares of ABC.

ABC engages primarily in retail and commercial banking throughout China, including Hong Kong SAR and Macau SAR. Outside China, ABC operates a subsidiary in the United Kingdom, branches in Singapore and Korea, and representative offices in Japan, Germany, and Australia. In the United States, ABC operates a representative office in New York City. ABC is a qualifying foreign banking organization under Regulation K.[4]

The proposed New York branch would engage in wholesale deposit taking, lending, trade finance, and other banking services.

Under the IBA and Regulation K, in acting on an application by a foreign bank to establish a branch, the Board must consider whether the foreign bank (1) engages directly in the business of banking outside the United States; (2) has furnished to the Board the information it needs to assess the application adequately; and (3) is subject to comprehensive supervision on a consolidated basis by its home country supervisors.[5] In assessing the comprehensive, consolidated supervision standard, the Board has considered the Basel Core

2 Asset and ranking data are as of December 31, 2011.

3 The Ministry of Finance owns approximately 39 percent, and The National Council for Social Security Fund owns approximately 3.9 percent of ABC's shares. Central Huijin Investment Ltd. ("Huijin") owns approximately 40 percent of ABC's shares. Huijin was formed to assist in the restructuring of major Chinese banks. The government transferred shares of several Chinese banks, including ABC, to Huijin at the time of the recapitalization and restructuring of these banks between 2004 and 2006. Huijin also owns a majority interest in China Construction Bank Corporation ("CCB") and Bank of China Limited ("BOC"), and together with the Ministry of Finance, it owns a majority interest in Industrial and Commercial Bank of China Limited ("ICBC"), all of Beijing. CCB and ICBC each operate a branch in New York City, and BOC operates branches in New York City and Los Angeles. The government of China transferred the ownership of Huijin to China Investment Corporation ("CIC"), an investment fund that is also wholly owned by the government of China. CIC owns 9.9 percent of the shares of Morgan Stanley, New York, New York, a bank holding company that owns a bank in Utah and a bank in New York. Both CIC and Huijin are non-operating companies that hold investments on behalf of the government of China. Neither CIC nor Huijin engages directly in commercial or financial activities.

Under the IBA, any company that owns a foreign bank with a branch in the United States is subject to the Bank Holding Company Act ("BHC Act") as if it were a bank holding company. Because of their ownership of CCB, BOC, and ICBC, CIC and Huijin are subject to the BHC Act. The Board has provided certain exemptions to CIC and Huijin under section 4(c)(9) of the BHC Act (12 U.S.C. § 1843(c)(9)), which authorizes the Board to grant exemptions to foreign companies from the nonbanking restrictions of the BHC Act when the exemptions would not be substantially at variance with the purposes of the act and would be in the public interest. The exemptions provided to CIC and Huijin would not extend to ABC or any other banking subsidiary of CIC or Huijin that operates a branch or agency in the United States. *See*Board letter to H. Rodgin Cohen, Esq., dated August 5, 2008.

4 12 CFR 211.23(a).

5 12 U.S.C. § 3105(d)(2); 12 CFR 211.24. Regulation K provides that a foreign bank is subject to consolidated home country supervision if the foreign bank is supervised or regulated in such a manner that its home country supervisor receives sufficient information on the worldwide operations of the foreign bank (including the relationships of the bank to any affiliate) to assess the foreign bank's overall financial condition and compliance with law and regulation. 12 CFR 211.24(c)(1)(ii). In assessing this standard, the Board considers, among other indicia of comprehensive, consolidated supervision, the extent to which the home country supervisors: (i) ensure that the bank has adequate procedures for monitoring and controlling its activities worldwide; (ii) obtain information on the condition of the bank and its subsidiaries and offices through regular examination reports, audit reports, or otherwise; (iii) obtain information on the dealings with and relationship between the bank and its affiliates, both foreign and domestic; (iv) receive from the bank financial reports that are consolidated on a worldwide basis or comparable information that permits analysis of the bank's financial condition on a worldwide consolidated basis; (v) evaluate prudential standards, such as capital adequacy and risk asset exposure, on a worldwide basis. No single factor is determinative, and other elements may inform the Board's determination. The Board has long held that "the legal systems for supervision and regulation vary from country to country, and comprehensive supervision or regulation on a consolidated basis can be achieved in different ways." 57 *Federal Register* 12992, 12995 (April 15, 1992).

Principles for Effective Banking Supervision ("Basel Core Principles"),[6] which are recognized as the international standard for assessing the quality of bank supervisory systems, including with respect to comprehensive, consolidated supervision.[7] The Board also considers additional standards as set forth in the IBA and Regulation K.[8]

As noted above, ABC engages directly in the business of banking outside the United States. ABC also has provided the Board with information necessary to assess the application through submissions that address the relevant issues.

For a number of years, authorities in China have continued to enhance the standards of consolidated supervision to which banks in China are subject, including through additional or refined statutory authority, regulations, and guidance; adoption of international standards and best practices; enhancements to the supervisory system arising out of supervisory experiences; upgrades to the China Banking Regulatory Commission ("CBRC"), the agency with primary responsibility for the supervision and regulation of Chinese banking organizations, in the areas of organization, technological capacity, staffing, and training; and increased coordination between the CBRC and other financial supervisory authorities in China.[9]

The Board has reviewed the record in this case and has determined that the enhancements to standards of bank supervision in China with respect to ABC warrant a finding that ABC is subject to comprehensive, consolidated supervision by its home country supervisors. In making this determination, the Board has considered that the CBRC is the principal supervisory authority of ABC, including its foreign subsidiaries and affiliates, for all matters other than money laundering.[10] The CBRC has primary responsibility and authority for regulating the establishment and activities and the expansion and dissolution of banking institutions, both domestically in China and abroad. The CBRC has no objection to ABC's establishment of the proposed branch. The CBRC monitors Chinese banks' con-

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6 *See* Bank for International Settlements, Basel Committee on Banking Supervision, *Core Principles for Effective Banking Supervision* (October 2006), available at www.bis.org/publ/bcbs129.pdf.

7 *See e.g.,* 93rd Annual Report of the Board of Governors of the Federal Reserve System (2006), at 76 ("The Core Principles, developed by the Basel Committee in 1997, have become the de facto international standard for sound prudential regulation and supervision of banks.").

8 12 U.S.C. § 3105(d)(3)-(4); 12 CFR 211.24(c)(2)-(3). The additional standards set forth in section 7 of the IBA and Regulation K include the following: whether the bank's home country supervisor has consented to the establishment of the office; the financial and managerial resources of the bank; whether the bank has procedures to combat money laundering, whether there is a legal regime in place in the home country to address money laundering, and whether the home country is participating in multilateral efforts to combat money laundering; whether the appropriate supervisors in the home country may share information on the bank's operations with the Board; whether the bank has provided the Board with adequate assurances that it will make available to the Board such information on its operations and activities and those of its affiliates that the Board deems necessary to determine and enforce compliance with the IBA and other applicable federal banking statutes; whether the bank and its U.S. affiliates are in compliance with U.S. law; the needs of the community; the bank's record of operation. The Board also considers, in the case of a foreign bank that presents a risk to the stability of the United States, whether the home country of the foreign bank has adopted, or is making demonstrable progress toward adopting, an appropriate system of financial regulation for the financial system of such home country to mitigate such risk. 12 U.S.C. § 3105(d)(3)(E) .

9 The Board has previously approved applications from Chinese banks to establish U.S. branches under a lower standard than the comprehensive, consolidated supervision standard. *See China Merchants Bank Co., Limited*, 94 *Federal Reserve Bulletin* C24 (2008); *Industrial and Commercial Bank of China Limited*, 94 *Federal Reserve Bulletin* C114 (2008); *China Construction Bank Corporation*, 95 *Federal Reserve Bulletin* B54 (2009); and *Bank of Communications Co.Ltd.*, (order dated April 8, 2011), 97 *Federal Reserve Bulletin* 49 (2nd Quar. 2011). In each case, the Board made a determination that the bank's home country supervisors were actively working to establish arrangements for the consolidated supervision of the bank. 12 U.S.C. § 3105(d)(6).

10 Before April 2003, the People's Bank of China ("PBOC") acted as both China's central bank and primary banking supervisor, including with respect to anti-money-laundering matters. In April 2003, the CBRC was established as the primary banking supervisor and assumed the majority of the PBOC's bank regulatory functions. The PBOC maintained its roles as China's central bank and primary supervisor for anti-money-laundering matters.

solidated financial condition, compliance with laws and regulations, and internal controls through a combination of on-site examinations, off-site surveillance through the review of required regulatory reports and external audit reports, and interaction with senior management.

Since its establishment in 2003, the CBRC has augmented its supervisory structure, staffing, and internal operations; enhanced its existing supervisory programs; and developed new policies and procedures to create a framework for the consolidated supervision of the largest banks in China. The CBRC also has strengthened its supervisory regime related to accounting requirements and standards for loan classification, internal controls, risk management, and capital adequacy, and it has developed and implemented a risk focused supervisory framework.

The CBRC has issued additional guidance in various supervisory areas, including stricter prudential requirements for capital, loan-loss allowance coverage, executive compensation, banks' equity investments in insurance companies, and enhanced risk-management requirements for operations, liquidity, derivatives, reputational, and market risk. The guidance is designed to make supervision more risk focused and to strengthen practices consistent with the Basel Core Principles.

The CBRC has its head office in Beijing and branch offices in other provinces. The head office sets policy and directs supervisory activities for the largest banks in China, including ABC. Although some day-to-day supervisory activities are undertaken by the CBRC's branch offices, the head office directs these efforts and ensures consistency of approach through training programs and frequent communication with the branches.

The CBRC head office prepares annual examination plans for the largest Chinese banks, including ABC. The plans encompass both on- and off-site activities. Applicable Chinese law and banking regulation do not require that on-site examinations be conducted at any specified interval. In practice, the CBRC performs on-site examinations of its largest banks frequently, although off-site surveillance is continuous. On-site examinations are scheduled based on the CBRC's continuous off-site monitoring tools, analysis of the institution's periodic filings, results of the institution's internal stress testing, and the institution's overall risk profile and activities. On-site examinations by the CBRC typically cover, among other things, the major areas of operation: corporate governance and senior management responsibilities; capital adequacy; asset structure and asset quality (including structure and quality of loans); off-balance-sheet activities; earnings; liquidity; liability structure and funding sources; expansionary plans; internal controls (including accounting control and administrative systems); legal compliance; accounting supervision and internal auditing; and any other areas deemed necessary by the CBRC. The PBOC examines ABC for compliance with anti-money-laundering laws and requirements.

Examination ratings are based on the CAMELS rating model and emphasize credit-risk management, the quality of the bank's loan portfolio, internal controls, liability structure, capital adequacy, liquidity, and the adequacy of reserves. The areas of emphasis reflect the fact that the largest Chinese banks, including ABC, engage in traditional commercial banking and are not materially engaged in complex derivatives or other activities. Ratings are derived from off-site quantitative and qualitative analysis and on-site risk reviews. Examination findings and areas of concern are discussed with senior management of the bank, and corrective actions taken by the bank are monitored by the CBRC. In 2009, the CBRC developed an information technology system to assist in on-site examinations by improving data analysis and assisting in regulatory information sharing.

Chinese banks are required to report key regulatory indicators to the CBRC periodically on general schedules. All Chinese banks are required to submit monthly, quarterly, semiannual, or annual reports relating to asset quality, lending concentrations, capital adequacy, earnings, liquidity, affiliate transactions, off-balance-sheet exposures, internal controls, and ownership and control.

Banks must report to the CBRC their unconsolidated capital adequacy ratios quarterly and their consolidated ratios semiannually. China's bank capital rules are based on the Basel I Capital Accord, while taking into account certain aspects of the Basel II Capital Accord. In addition, the CBRC, as a member of the Basel Committee on Banking Supervision, has supported the Basel III Capital Accord framework and implementation time frame. The CBRC can take enforcement actions when capital ratios or other financial indicators fall below specified levels. These actions may include issuing supervisory notices, requiring the bank to submit and implement an acceptable capital replenishment plan, restricting asset growth, requiring reduction of higher risk assets, restricting the purchase of fixed assets, and restricting dividends and other forms of distributions. Significantly undercapitalized banks may be required to make changes in senior management or restructure their operations.

ABC, like other large Chinese banks, is required to be audited annually by an external accounting firm that meets the standards of Chinese authorities, including the Ministry of Finance, PBOC, and CBRC, and the audit results are shared with the CBRC and PBOC. The scope of the required audit includes a review of ABC's financial statements, asset quality, capital adequacy, internal controls, and compliance with applicable laws. At its discretion, the CBRC may order a special audit at any time. In addition, in connection with its listing on the Shanghai and Hong Kong stock exchanges, ABC is also required to report financial statements under both International Financial Reporting Standards ("IFRS") and Chinese Accounting Standards ("CAS"). These financial statements are audited by an international accounting firm under applicable IFRS auditing standards.[11]

ABC conducts internal audits of its domestic offices and operations on an annual schedule and of its overseas branches and offices biennially. The internal audit results are shared with the CBRC, PBOC, and ABC's external auditors. The proposed branch would be subject to internal audits.

Chinese law imposes various prudential limitations on banks, including limits on transactions with affiliates and on large exposures.[12] Related-party transactions include credit extensions, asset transfers, and the provision of any type of services. Chinese banks are required to adopt appropriate policies and procedures to manage related-party transactions, and the board of directors must appoint a committee to supervise such transactions

[11] CAS largely conform to IFRS, such that there currently are no material differences between financial statements produced for Hong Kong reporting requirements and Chinese reporting requirements. The International Monetary Fund's ("IMF") financial system stability assessment report and the accompanying detailed assessment report of observance with the Basel Core Principles, discussed in detail below, both found that "[s]ince 2005, [CAS] have substantially converged with [IFRS] and International Standards on Auditing, respectively." IMF, People's Republic of China, Financial System Stability Assessment at 57 (June 24, 2011); IMF and World Bank, People's Republic of China: Detailed Assessment Report of Observance with Basel Core Principles for Effective Banking Supervision at 9 (April 2012). In addition, the World Bank Report on Observance of Standards and Codes determined that CAS and IFRS are basically compatible and that the Chinese authorities and the International Accounting Standards Board have established a continuing convergence mechanism designed to achieve full convergence in 2012. World Bank, Report on Observance of Standards and Codes (ROSC) Accounting and Auditing – People's Republic of China at Executive Summary and at 12 (October 2009), available at www.worldbank.org/ifa/rosc_aa_chn.pdf .

[12] The CBRC definition of an "affiliate" or a "related party" of a bank includes subsidiaries, associates/joint ventures, shareholders holding 5 percent or more of the bank's shares, and key management personnel (and immediate relatives) and those individuals' other business affiliations.

and relationships. Applicable laws require all related-party transactions to be conducted on an arm's-length basis.

Chinese banking law also establishes single-borrower credit limits. Loans to a single borrower may not exceed 10 percent of the bank's total regulatory capital, the aggregate lending to a group of related companies may not exceed 15 percent of the bank's total regulatory capital, and the aggregate amount of credit granted to all related parties may not exceed 50 percent of the bank's total regulatory capital. The status of related-party transactions must be reported to the CBRC quarterly.

In addition, the CBRC has certain operational limitations for commercial banks in China relating to matters such as liquidity and foreign currency exposure. In 2009, the CBRC issued new rules concerning liquidity management and corporate governance. Compliance with these limits is monitored by the CBRC through periodic reports and reviewed during on-site examinations.

The CBRC is authorized to require any bank to provide information and to impose sanctions for failure to comply with such requests. If the CBRC determines that a bank is not in compliance with banking regulations and prudential standards, it may impose various sanctions depending upon the severity of the violation. The CBRC may suspend approval of new products or new offices, suspend part of the bank's operations, impose monetary penalties, and in more serious cases, replace management of the bank. The CBRC also has authority to impose administrative penalties, including warnings and fines for violations of applicable laws and rules. Criminal violations are transferred to the judicial authorities for investigation and prosecution.

ABC is subject to supervision by several other financial regulators, including the State Administration for Foreign Exchange, China Securities Regulatory Commission ("CSRC"), and China Insurance Regulatory Commission ("CIRC"). These agencies receive periodic financial and operations reports, and they may conduct on-site examinations and impose additional reporting requirements. Chinese financial supervisors coordinate supervision and share supervisory information about Chinese financial institutions as appropriate.

The IMF recently concluded a financial system stability assessment of China ("FSSA"), including an assessment of China's compliance with the Basel Core Principles.[13] The FSSA determined that China's overall regulatory and supervisory framework adheres to international standards.[14] The FSSA found that "[t]he laws, rules and guidance that CBRC operates under generally establish a benchmark of prudential standards that is of high quality and was drawn extensively from international standards and the [Basel Core Principles] themselves."[15] The FSSA additionally noted that "[c]onsolidated supervision of banks and

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[13] The assessment reflects the regulatory and supervisory framework in place as of June 24, 2011. IMF, *People's Republic of China, Financial System Stability Assessment* (June 24, 2011), available at www.imf.org/external/pubs/ft/scr/2011/cr11321.pdf. The FSSA covers an evaluation of three components: (1) the source, probability, and potential impact of the main risks to macrofinancial stability in the near term; (2) the country's financial stability policy framework; and (3) the authorities' capacity to manage and resolve a financial crisis should the risks materialize. The FSSA is a key input to IMF surveillance. The FSSA is a forward-looking exercise, unlike the Board's assessment of the comprehensive, consolidated supervision of an applicant.

The IMF and World Bank separately publish a detailed assessment of the country's observance of the Basel Core Principles that discusses the country's adherence to the Basel Core Principles in much greater detail. See IMF and World Bank, *People's Republic of China: Detailed Assessment Report of Observance with Basel Core Principles for Effective Banking Supervision* (April 2012) ("DAR"), available at www.imf.org/external/pubs/ft/scr/2012/cr1278.pdf.

[14] FSSA at 39.

[15] *Id*. at 59; DAR at 12.

their direct subsidiaries and branches on the mainland or offshore is of high quality."[16] With respect to the CBRC, the FSSA found as follows: All the banks, auditors, ratings agencies and other market participants that the mission interacted with were unhesitating in their regard for the role that the CBRC has played in driving professionalism, risk management and international recognition of the Chinese banking system. In particular, the mission observed that [the CBRC] has been the key driving force in driving improvements in risk management, corporate governance and internal control and disclosure in Chinese banks.[17] Based on its review, the FSSA rated China's overall compliance with the Basel Core Principles as satisfactory. In giving this overall rating, the FSSA noted several areas that merited improvement and made specific recommendations for continued advances in supervision and regulation.[18] The Chinese authorities noted that some of the recommendations of the FSSA are already being implemented and that others will be taken into account in the CBRC's plans to improve supervisory effectiveness.[19]

The Board has taken into account the FSSA's views that China is, overall, in satisfactory compliance with the Basel Core Principles and that there are areas for further improvement. The Board has also taken into account the responses by Chinese authorities to the FSSA report and the progress made by Chinese authorities to address the issues raised in that report.

Based on all the facts of record, including its review of the supervisory framework implemented by the CBRC for ABC, the Board has determined that ABC is subject to comprehensive supervision on a consolidated basis by its home country supervisors. This determination is specific to ABC.[20] By statute, the Board must review this determination in processing future applications involving ABC and also must make a determination of comprehensive, consolidated supervision in other applications involving different applicants from China.

As part of the Board's supervisory program for foreign banks, the Board actively monitors changes to the supervisory systems in the home countries of foreign banks, as well as differences that may exist in the supervisory framework as it is applied by a home country to

[16] FSSA at 64; DAR at 16.

[17] DAR at 7.

[18] FSSA at 39-42 and 69-71; DAR at 99-101. China received a materially noncompliant rating in two of the thirty areas assessed by the FSSA. Specifically, the FSSA rated China as materially noncompliant for the Basel Core Principles on independence, accountability and transparency, and risk management process. DAR at 17 and 19. The FSSA stated that "budgeting arrangements, external headcount approval requirements and [the authority for the State Council to override] rules and decisions compromise CBRC effectiveness and could affect operational independence." FSSA at 64; DAR at 17. The FSSA viewed the guidance that the CBRC has issued in risk management to be consistent with international standards but found that banking institutions' compliance with CBRC guidance was lacking (although recognizing that the guidance on some risks "is recent and so could not be expected to be complied with as yet"). FSSA at 61; *see also* DAR at 53. The assessment team also believed that Chinese banks in general do not yet have robust enterprise-wide risk-management systems. FSSA at 66; DAR at 53-54. For comparison, the United Kingdom and Germany received three and two materially noncompliant ratings, respectively, and the United States received one materially noncompliant rating, in their recent financial system stability assessments.

[19] FSSA at 71-73; DAR at 101-103. Chinese authorities responded that, by law in China, the State Council of the People's Republic of China ("State Council") may alter or annul a rule or guideline of the CBRC only if the rule or guideline violates applicable law and that the State Council has never altered or annulled the rules and guidelines issued by the CBRC. Chinese authorities also noted that the State Council has supported the CBRC in undertaking banking regulation and supervision and that the CBRC has upgraded the number and quality of its staff over time. FSSA at 71-72; DAR at 102. In addition, Chinese authorities noted the significant improvements China has made in supervision as well as the relative simplicity of the Chinese banking system. FSSA at 72; DAR at 102-3. Despite the difference in views about the degree to which Chinese banks' risk management is commensurate with the current risk environment, Chinese authorities concurred with the FSSA that "continued improvements in banks' risk management are needed, as financial reform deepens and liberalization creates greater interconnectedness and complexities in the Chinese system." FSSA at 72; DAR at 103.

[20] *See* 58 *Federal Register* 6348, 6349 (January 12, 1993).

institutions of different types or sizes, and would continue to do so with respect to China. The Board also intends to further its relationship with Chinese supervisory authorities and continue to develop its understanding of Chinese banking matters.

The government of China has adopted a statutory regime regarding anti-money laundering ("AML") and suspicious activity reporting and has criminalized money-laundering activities and other financial crimes. The PBOC supervises and examines Chinese banks with respect to AML and coordinates efforts among other agencies. The PBOC collects, monitors, analyzes, and disseminates suspicious transaction reports and large-value transaction reports.

The PBOC over time has increased requirements for its supervised institutions regarding AML compliance. The PBOC issued rules providing clarification of, or further strengthening the implementation of, operating procedures, customer due diligence and risk classification, recordkeeping, AML monitoring and reporting suspicious transactions, and the international remittance agency business. The PBOC also requires the designation of a chief AML compliance officer as a high-level manager to ensure provision of adequate AML resources and timely flow of information to employees responsible for AML compliance throughout the institution. In addition, the PBOC requires the risk rating of customers and the filing of reports on suspicious activity and certain other transactions. Banks are required to (1) establish a customer identification system in accordance with applicable rules jointly promulgated by the PBOC and three functional financial services regulators;[21] (2) record the identities of customers and information relating to each transaction; and (3) retain retail transaction documents and books. Supervised institutions have been encouraged to move beyond a prescriptive-criteria basis to include a more expansive and risk-based approach to suspicious activity detection and reporting.

China participates in international fora that address the prevention of money laundering and terrorist financing. China became a member of the Financial Action Task Force ("FATF") in June 2007. China also is a member of the Eurasian Group ("EAG"), a FATF-style regional body that supports member countries in their efforts to create and maintain an appropriate legal and institutional framework to combat money laundering and terrorist financing in line with FATF standards.[22] EAG evaluates its member states' AML and counter-terrorist financing ("CFT") systems for compliance with international standards. In the most recent mutual evaluation report of China, dated February 17, 2012, the FATF considered China to be fully or largely compliant with almost all of the FATF recommendations and held that China has effective AML and CFT systems in force. As a result, the FATF has removed China from its regular follow-up process.[23]

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[21] Those regulators are the CBRC, CSRC, and CIRC.

[22] China also is a party to other agreements that address money laundering or terrorist financing, including the U.N. Convention Against the Illicit Traffic of Narcotics and Psychotropic Substances, the U.N. Convention Against Transnational Organized Crime, the U.N. Convention Against Corruption, and the U.N. International Convention for the Suppression of the Financing of Terrorism.

[23] FATF, *China Mutual Evaluation 8th Follow-up Report, Anti-Money Laundering and Combating the Financing of Terrorism* (February 17, 2012), available at www.fatf gafi.org/dataoecd/5/34/49847246.pdf. The report noted that China has made significant progress to address the remaining deficiencies and has "reached a satisfactory level of compliance with all six core Recommendations and eight of the [ten] key Recommendations." Id at para. 41. In one of the key Recommendations where China has not attained a satisfactory level of compliance (implementation of international instruments related to terrorist financing), China has substantially addressed part of the deficiency and continues to make progress. With respect to the other key Recommendation (freezing of terrorist-related assets), China has made significant progress since June 2011 to improve its implementation. In particular, China has implemented legislation establishing a legislative framework and administrative authority for enforcement and has responded to foreign requests to freeze assets. The FATF was of the view that China should enact additional guidance to improve implementation, and Chinese authorities are currently drafting rules to do so. *Id*. at paras. 150-52 and 157-59.

Moreover, the Chinese government issues rules on implementing United Nations sanctions and may take enforcement actions to ensure compliance with those sanctions. The PBOC is also responsible for disseminating information to the banking industry regarding U.N. sanctions and supervising the enforcement of those sanctions.

The PBOC supervises and regulates compliance by ABC with AML requirements through a combination of on-site examinations and off-site monitoring. On site examinations focus on ABC's compliance with AML laws and rules. The PBOC's headquarters conducts investigations of a financial institution's head office, and the PBOC's branches conduct investigations of the institution's branch offices in the same locality as the PBOC branches. During the course of an on-site examination, the PBOC will generally review account information, transaction records, and any other relevant materials. Upon completion of an investigation, if AML deficiencies are identified, the PBOC may issue sanctions and propose that remedial measures be imposed by appropriate government agencies or regulators against the financial institution and can refer any suspected money laundering to law enforcement authorities for further investigation. The PBOC performs off site monitoring through periodic reports and has established requirements for Chinese banks to submit such reports. In order to improve off-site supervision and monitoring of large-amount cash transactions, the PBOC developed an interactive information technology system for AML/CFT supervision that has been in operation since October 2010 in both the PBOC and financial institutions.

ABC has policies and procedures to comply with Chinese laws and rules regarding AML. ABC states that it has implemented measures consistent with the recommendations of the FATF and that it has put in place policies, procedures, and controls to ensure ongoing compliance with all statutory and regulatory requirements, including designating AML compliance personnel and conducting routine employee training at all ABC branches. ABC's compliance with AML requirements is monitored by the PBOC and by ABC's internal and external auditors.

Based on all the facts of record, the Board has determined that the AML efforts by ABC and its home country supervisors are consistent with approval.

The Board has also considered the financial and managerial factors in this case. As noted above, the CBRC requires Chinese banks to follow the Basel I Capital Accord with certain enhancements from the Basel II Capital Accord.[24] The capital levels of ABC exceed the minimum levels that would be required under the Basel I Capital Accord and are considered to be equivalent to the capital levels that would be required of a U.S. banking organization. Managerial and other financial resources of ABC are consistent with approval, and ABC appears to have the experience and capacity to support the proposed branch. In addition, ABC has established controls and procedures for the proposed branch to ensure compliance with U.S. law and for its operations in general. In particular, ABC has stated that it will apply strict AML policies and procedures at the branch consistent with U.S. law and regulation and will establish an internal control system at the branch consistent with U.S. requirements to ensure compliance with those policies and procedures.

With respect to access to information about ABC's operations, the Board has reviewed the restrictions on disclosure in relevant jurisdictions in which ABC operates and has communicated with relevant government authorities regarding access to information. ABC has committed to make available to the Board such information on the operations of ABC and any of its affiliates that the Board deems necessary to determine and enforce compliance

[24] The CBRC also requires all large, internationally active banks, such as ABC, to have a minimum risk-based tier 1 capital ratio of 9 percent and total capital ratio of 11.5 percent. ABC's capital ratios exceed these levels.

with the IBA, the BHC Act, and other applicable federal laws. To the extent that the provision of such information to the Board may be prohibited by law or otherwise, ABC also has committed to cooperate with the Board to obtain any waivers or exemptions that may be necessary to enable it or its affiliates to make such information available to the Board. The Board also has consulted with the CBRC about access to information. The CBRC has represented that it would facilitate the Board's access to information and has entered into a statement of cooperation with the Board and other U.S. banking regulators with respect to the sharing of supervisory information.[25] In light of these commitments and other facts of record, and subject to the condition described below, the Board has determined that ABC has provided adequate assurances of access to any necessary information that the Board may request.

China has made progress toward adopting a system of financial regulation for its financial system to mitigate the risk to financial stability from its banks. The PBOC, CBRC, other financial supervisory agencies, and other agencies in China have taken joint measures to maintain financial stability. China has established a system of preliminary indicators for monitoring financial stability, developed methodology and operational frameworks for monitoring financial risks, and published an annual China Financial Stability Report since 2005. The CBRC has established mechanisms to cooperate with supervisory authorities in at least 25 other countries for the supervision of cross-border banking. In addition, the PBOC and CBRC officially joined the Basel Committee on Banking Supervision on behalf of China and since their accession, have actively participated in the revision of the Basel II Capital Accord, in the formulation of the Basel III Capital Accord, and in other working groups. China also is active in the ongoing work of the Financial Stability Board. U.S. bank regulators and other bank supervisors in pertinent jurisdictions participated in two supervisory colleges hosted by the CBRC: one for ICBC in 2009 and one for CCB in 2011. Moreover, authorities in the United States and China that are responsible for the oversight of auditing services for public companies are engaged in continuing discussions with respect to enhancing cross-border cooperation, and the Board looks forward to timely negotiation of an agreement relating to cooperative actions by these authorities.

On the basis of all the facts of record, and subject to the commitments made by ABC, as well as the terms and conditions set forth in this order, ABC's application to establish a branch is hereby approved. The Board conditions its decision on ABC providing to the Board adequate information on its operations and activities as well as those of its affiliates to determine and enforce compliance by ABC or its affiliates with applicable federal statutes. Should any restrictions on access to information on the operations or activities of ABC or any of its affiliates subsequently interfere with the Board's ability to obtain information to determine and enforce compliance by ABC or its affiliates with applicable federal statutes, the Board may require termination or divestiture of any of ABC's or its affiliates' direct or indirect activities in the United States. Approval of this application also is specifically conditioned on compliance by ABC with the commitments made to the Board in connection with this application and with the conditions in this order.[26] The commitments and conditions referred to above are conditions imposed in writing by the Board in connection with this decision and may be enforced in proceedings under 12 U.S.C. U.S.C. § 1818 against ABC and its affiliates.

By order of the Board of Governors, effective May 9, 2012.

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[25] *See* Memorandum of Understanding between the CBRC and the Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation, June 17, 2004.

[26] The Board's authority to approve the establishment of the proposed branch parallels the continuing authority of the New York State Department of Financial Services to license offices of a foreign bank.

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

Robert deV. Frierson
Deputy Secretary of the Board

Bank of China Limited
Beijing, People's Republic of China

Order Approving Establishment of a Branch
FRB Order No. 2012–6 (May 9, 2012)

Bank of China Limited ("BOC"), Beijing, People's Republic of China, a foreign bank within the meaning of the International Banking Act ("IBA"), has applied under section 7(d) of the IBA[1] to establish a federal branch in Chicago, Illinois. The Foreign Bank Supervision Enhancement Act of 1991, which amended the IBA, provides that a foreign bank must obtain the approval of the Board to establish a branch in the United States.

Notice of the application, affording interested persons an opportunity to comment, has been published in a newspaper of general circulation in Chicago (*The Chicago Sun-Times*, August 16, 2010). The time for filing comments has expired, and the Board has considered all comments received.

BOC, with total assets of approximately $1.87 trillion, is the third largest bank in China.[2] The government of China owns approximately 71 percent of BOC's shares.[3] No other shareholder owns more than 5 percent of the shares of BOC.[4]

BOC engages primarily in retail and commercial banking throughout China, including Hong Kong SAR and Macau SAR. Outside China, BOC operates a network of bank subsidiaries, branches, and representative offices in 29 countries. In the United States, BOC operates two insured federal branches in New York City and an uninsured limited federal

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[1] 12 U.S.C.§ 3105(d).

[2] Asset and ranking data are as of December 31, 2011.

[3] Central Huijin Investment Ltd. ("Huijin") owns approximately 67.6 percent, and The National Council for Social Security Fund holds approximately 3.3 percent of BOC's shares. Huijin was formed to assist in the restructuring of major Chinese banks. The government transferred shares of several Chinese banks, including BOC, to Huijin at the time of the recapitalization and restructuring of these banks between 2004 and 2006. Huijin also owns a majority interest in China Construction Bank Corporation ("CCB"), and together with the Chinese Ministry of Finance, it owns a majority interest in Industrial and Commercial Bank of China Limited ("ICBC") and Agricultural Bank of China Limited ("ABC"), all of Beijing. CCB and ICBC each operate a branch in New York City. The government of China transferred the ownership of Huijin to China Investment Corporation ("CIC"), an investment fund that is also wholly owned by the government of China. CIC owns 9.9 percent of the shares of Morgan Stanley, New York, New York, a bank holding company that owns a bank in Utah and a bank in New York. Both CIC and Huijin are non operating companies that hold investments on behalf of the government of China. Neither CIC nor Huijin engages directly in commercial or financial activities.

Under the IBA, any company that owns a foreign bank with a branch in the United States is subject to the Bank Holding Company Act ("BHC Act") as if it were a bank holding company. Because of their ownership of BOC, CCB, and ICBC, CIC and Huijin are subject to the BHC Act. The Board has provided certain exemptions to CIC and Huijin under section 4(c)(9) of the BHC Act (12 U.S.C. § 1843(c)(9)), which authorizes the Board to grant exemptions to foreign companies from the nonbanking restrictions of the BHC Act when the exemptions would not be substantially at variance with the purposes of the act and would be in the public interest. The exemptions provided to CIC and Huijin would not extend to BOC or any other banking subsidiary of CIC or Huijin that operates a branch or agency in the United States. *See* Board letter to H. Rodgin Cohen, Esq., dated August 5, 2008.

[4] HKSCC Nominees Limited holds an additional approximately 29 percent of the shares of BOC as the registered nominee of several shareholders, each of which owns less than 5 percent of the shares of BOC.

branch in Los Angeles, as well as nonbanking activities under section 4(c)(8) of the BHC Act.[5] BOC is a qualifying foreign banking organization under Regulation K.[6]

The proposed Chicago branch would engage in wholesale deposit taking, lending, trade finance, and other banking services.

Under the IBA and Regulation K, in acting on an application by a foreign bank to establish a branch, the Board must consider whether the foreign bank (1) engages directly in the business of banking outside the United States; (2) has furnished to the Board the information it needs to assess the application adequately; and (3) is subject to comprehensive supervision on a consolidated basis by its home country supervisors.[7] In assessing the comprehensive, consolidated supervision standard, the Board has considered the Basel Core Principles for Effective Banking Supervision ("Basel Core Principles"),[8]which are recognized as the international standard for assessing the quality of bank supervisory systems, including with respect to comprehensive, consolidated supervision.[9] The Board also considers additional standards as set forth in the IBA and Regulation K.[10]

As noted above, BOC engages directly in the business of banking outside the United States. BOC also has provided the Board with information necessary to assess the application through submissions that address the relevant issues.

For a number of years, authorities in China have continued to enhance the standards of consolidated supervision to which banks in China are subject, including through additional

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5 12 U.S.C. § 1843(c)(8). BOC also controls a wholly owned subsidiary bank, Nanyang Commercial Bank, Limited, Hong Kong SAR, People's Republic of China, that operates a federal branch in San Francisco.

6 12 CFR 211.23(a).

7 12 U.S.C. § 3105(d)(2); 12 CFR 211.24. Regulation K provides that a foreign bank is subject to consolidated home country supervision if the foreign bank is supervised or regulated in such a manner that its home country supervisor receives sufficient information on the worldwide operations of the foreign bank (including the relationships of the bank to any affiliate) to assess the foreign bank's overall financial condition and compliance with law and regulation. 12 CFR 211.24(c)(1)(ii). In assessing this standard, the Board considers, among other indicia of comprehensive, consolidated supervision, the extent to which the home country supervisors: (i) ensure that the bank has adequate procedures for monitoring and controlling its activities worldwide; (ii) obtain information on the condition of the bank and its subsidiaries and offices through regular examination reports, audit reports, or otherwise; (iii) obtain information on the dealings with and relationship between the bank and its affiliates, both foreign and domestic; (iv) receive from the bank financial reports that are consolidated on a worldwide basis or comparable information that permits analysis of the bank's financial condition on a worldwide consolidated basis; (v) evaluate prudential standards, such as capital adequacy and risk asset exposure, on a worldwide basis. No single factor is determinative, and other elements may inform the Board's determination. The Board has long held that "the legal systems for supervision and regulation vary from country to country, and comprehensive supervision or regulation on a consolidated basis can be achieved in different ways." 57 *Federal Register* 12992, 12995 (April 15, 1992).

8 *See* Bank for International Settlements, Basel Committee on Banking Supervision, *Core Principles for Effective Banking Supervision*(October 2006), available at www.bis.org/publ/bcbs129.pdf .

9 *See e.g.,* 93rd Annual Report of the Board of Governors of the Federal Reserve System (2006), at 76 ("The Core Principles, developed by the Basel Committee in 1997, have become the de facto international standard for sound prudential regulation and supervision of banks.").

10 12 U.S.C. § 3105(d)(3)-(4); 12 CFR 211.24(c)(2)-(3). The additional standards set forth in section 7 of the IBA and Regulation K include the following: whether the bank's home country supervisor has consented to the establishment of the office; the financial and managerial resources of the bank; whether the bank has procedures to combat money laundering, whether there is a legal regime in place in the home country to address money laundering, and whether the home country is participating in multilateral efforts to combat money laundering; whether the appropriate supervisors in the home country may share information on the bank's operations with the Board; whether the bank has provided the Board with adequate assurances that it will make available to the Board such information on its operations and activities and those of its affiliates that the Board deems necessary to determine and enforce compliance with the IBA and other applicable federal banking statutes; whether the bank and its U.S. affiliates are in compliance with U.S. law; the needs of the community; the bank's record of operation. The Board also considers, in the case of a foreign bank that presents a risk to the stability of the United States, whether the home country of the foreign bank has adopted, or is making demonstrable progress toward adopting, an appropriate system of financial regulation for the financial system of such home country to mitigate such risk. 12 U.S.C. § 3105(d)(3)(E).

or refined statutory authority, regulations, and guidance; adoption of international standards and best practices; enhancements to the supervisory system arising out of supervisory experiences; upgrades to the China Banking Regulatory Commission ("CBRC"), the agency with primary responsibility for the supervision and regulation of Chinese banking organizations, in the areas of organization, technological capacity, staffing, and training; and increased coordination between the CBRC and other financial supervisory authorities in China.[11]

The Board has reviewed the record in this case and has determined that the enhancements to standards of bank supervision in China with respect to BOC warrant a finding that BOC is subject to comprehensive, consolidated supervision by its home country supervisors. In making this determination, the Board has considered that the CBRC is the principal supervisory authority of BOC, including its foreign subsidiaries and affiliates, for all matters other than money laundering.[12] The CBRC has primary responsibility and authority for regulating the establishment and activities and the expansion and dissolution of banking institutions, both domestically in China and abroad. The CBRC has no objection to BOC's establishment of the proposed branch. The CBRC monitors Chinese banks' consolidated financial condition, compliance with laws and regulations, and internal controls through a combination of on-site examinations, off-site surveillance through the review of required regulatory reports and external audit reports, and interaction with senior management.

Since its establishment in 2003, the CBRC has augmented its supervisory structure, staffing, and internal operations; enhanced its existing supervisory programs; and developed new policies and procedures to create a framework for the consolidated supervision of the largest banks in China. The CBRC also has strengthened its supervisory regime related to accounting requirements and standards for loan classification, internal controls, risk management, and capital adequacy, and it has developed and implemented a risk focused supervisory framework.

The CBRC has issued additional guidance in various supervisory areas, including stricter prudential requirements for capital, loan-loss allowance coverage, executive compensation, banks' equity investments in insurance companies, and enhanced risk-management requirements for operations, liquidity, derivatives, reputational, and market risk. The guidance is designed to make supervision more risk focused and to strengthen practices consistent with the Basel Core Principles.

The CBRC has its head office in Beijing and branch offices in other provinces. The head office sets policy and directs supervisory activities for the largest banks in China, including BOC. Although some day-to-day supervisory activities are undertaken by the CBRC's branch offices, the head office directs these efforts and ensures consistency of approach through training programs and frequent communication with the branches.

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[11] The Board has previously approved applications from Chinese banks to establish U.S. branches under a lower standard than the comprehensive, consolidated supervision standard. *See China Merchants Bank Co., Limited*, 94 *Federal Reserve Bulletin* C24 (2008); *Industrial and Commercial Bank of China Limited*, 94 *Federal Reserve Bulletin* C114 (2008); *China Construction Bank Corporation,* 95 *Federal Reserve Bulletin* B54 (2009); and *Bank of Communications Co., Ltd.* (order dated April 8, 2011), 97 *Federal Reserve Bulletin* 49 (2nd Quar. 2011). In each case, the Board made a determination that the bank's home country supervisors were actively working to establish arrangements for the consolidated supervision of the bank. 12 U.S.C. § 3105(d)(6).

[12] Before April 2003, the People's Bank of China ("PBOC") acted as both China's central bank and primary banking supervisor, including with respect to anti-money-laundering matters. In April 2003, the CBRC was established as the primary banking supervisor and assumed the majority of the PBOC's bank regulatory functions. The PBOC maintained its roles as China's central bank and primary supervisor for anti-money-laundering matters.

The CBRC head office prepares annual examination plans for the largest Chinese banks, including BOC. The plans encompass both on- and off-site activities. Applicable Chinese law and banking regulation do not require that on-site examinations be conducted at any specified interval. In practice, the CBRC performs on-site examinations of its largest banks frequently, although off-site surveillance is continuous. On-site examinations are scheduled based on the CBRC's continuous off-site monitoring tools, analysis of the institution's periodic filings, results of the institution's internal stress testing, and the institution's overall risk profile and activities. On-site examinations by the CBRC typically cover, among other things, the major areas of operation: corporate governance and senior management responsibilities; capital adequacy; asset structure and asset quality (including structure and quality of loans); off-balance-sheet activities; earnings; liquidity; liability structure and funding sources; expansionary plans; internal controls (including accounting control and administrative systems); legal compliance; accounting supervision and internal auditing; and any other areas deemed necessary by the CBRC. The PBOC examines BOC for compliance with anti-money-laundering laws and requirements.

Examination ratings are based on the CAMELS rating model and emphasize credit-risk management, the quality of the bank's loan portfolio, internal controls, liability structure, capital adequacy, liquidity, and the adequacy of reserves. The areas of emphasis reflect the fact that the largest Chinese banks, including BOC, engage in traditional commercial banking and are not materially engaged in complex derivatives or other activities. Ratings are derived from off-site quantitative and qualitative analysis and on site risk reviews. Examination findings and areas of concern are discussed with senior management of the bank, and corrective actions taken by the bank are monitored by the CBRC. In 2009, the CBRC developed an information technology system to assist in on site examinations by improving data analysis and regulatory information sharing.

Chinese banks are required to report key regulatory indicators to the CBRC periodically on general schedules. All Chinese banks are required to submit monthly, quarterly, semiannual, or annual reports relating to asset quality, lending concentrations, capital adequacy, earnings, liquidity, affiliate transactions, off-balance-sheet exposures, internal controls, and ownership and control.

Banks must report to the CBRC their unconsolidated capital adequacy ratios quarterly and their consolidated ratios semiannually. China's bank capital rules are based on the Basel I Capital Accord, while taking into account certain aspects of the Basel II Capital Accord. In addition, the CBRC, as a member of the Basel Committee on Banking Supervision, has supported the Basel III Capital Accord framework and implementation time frame. The CBRC can take enforcement actions when capital ratios or other financial indicators fall below specified levels. These actions may include issuing supervisory notices, requiring the bank to submit and implement an acceptable capital replenishment plan, restricting asset growth, requiring reduction of higher risk assets, restricting the purchase of fixed assets, and restricting dividends and other forms of distributions. Significantly undercapitalized banks may be required to make changes in senior management or restructure their operations.

BOC, like other large Chinese banks, is required to be audited annually by an external accounting firm that meets the standards of Chinese authorities, including the Ministry of Finance, PBOC, and CBRC, and the audit results are shared with the CBRC and PBOC. The scope of the required audit includes a review of BOC's financial statements, asset quality, capital adequacy, internal controls, and compliance with applicable laws. At its discretion, the CBRC may order a special audit at any time. In addition, in connection with its listing on the Shanghai and Hong Kong stock exchanges, BOC is also required to report financial statements under both International Financial Reporting Standards ("IFRS") and

Chinese Accounting Standards ("CAS"). These financial statements are audited by an international accounting firm under applicable IFRS auditing standards.[13]

BOC conducts internal audits of its offices and operations, including its overseas operations, generally on an annual schedule. The internal audit results are shared with the CBRC, the PBOC, and BOC's external auditors. The proposed branch would be subject to internal audits.

Chinese law imposes various prudential limitations on banks, including limits on transactions with affiliates and on large exposures.[14] Related-party transactions include credit extensions, asset transfers, and the provision of any type of services. Chinese banks are required to adopt appropriate policies and procedures to manage related-party transactions, and the board of directors must appoint a committee to supervise such transactions and relationships. Applicable laws require all related-party transactions to be conducted on an arm's-length basis.

Chinese banking law also establishes single-borrower credit limits. Loans to a single borrower may not exceed 10 percent of the bank's total regulatory capital, the aggregate lending to a group of related companies may not exceed 15 percent of the bank's total regulatory capital, and the aggregate amount of credit granted to all related parties may not exceed 50 percent of the bank's total regulatory capital. The status of related-party transactions must be reported to the CBRC quarterly.

In addition, the CBRC has certain operational limitations for commercial banks in China relating to matters such as liquidity and foreign currency exposure. In 2009, the CBRC issued new rules concerning liquidity management and corporate governance. Compliance with these limits is monitored by the CBRC through periodic reports and reviewed during on-site examinations.

The CBRC is authorized to require any bank to provide information and to impose sanctions for failure to comply with such requests. If the CBRC determines that a bank is not in compliance with banking regulations and prudential standards, it may impose various sanctions depending upon the severity of the violation. The CBRC may suspend approval of new products or new offices, suspend part of the bank's operations, impose monetary penalties, and in more serious cases, replace management of the bank. The CBRC also has authority to impose administrative penalties, including warnings and fines for violations of applicable laws and rules. Criminal violations are transferred to the judicial authorities for investigation and prosecution.

[13] CAS largely conform to IFRS, such that there currently are no material differences between financial statements produced for Hong Kong reporting requirements and Chinese reporting requirements. The International Monetary Fund's ("IMF") financial system stability assessment report and the accompanying detailed assessment report of observance with the Basel Core Principles, discussed in detail below, both found that "[s]ince 2005, [CAS] have substantially converged with [IFRS] and International Standards on Auditing, respectively." IMF, *People's Republic of China, Financial System Stability Assessment* at 57 (June 24, 2011); IMF and World Bank, *People's Republic of China: Detailed Assessment Report of Observance with Basel Core Principles for Effective Banking Supervision* at 9 (April 2012). In addition, the World Bank Report on Observance of Standards and Codes determined that CAS and IFRS are basically compatible and that the Chinese authorities and the International Accounting Standards Board have established a continuing convergence mechanism designed to achieve full convergence in 2012. World Bank, *Report on Observance of Standards and Codes (ROSC) Accounting and Auditing – People's Republic of China*at Executive Summary and at 12 (October 2009), available at www.worldbank.org/ifa/rosc_aa_chn.pdf.

[14] The CBRC definition of an "affiliate" or a "related party" of a bank includes subsidiaries, associates/joint ventures, shareholders holding 5 percent or more of the bank's shares, and key management personnel (and immediate relatives) and those individual's other business affiliations.

BOC is subject to supervision by several other financial regulators, including the State Administration for Foreign Exchange, China Securities Regulatory Commission ("CSRC"), and China Insurance Regulatory Commission ("CIRC"). These agencies receive periodic financial and operations reports, and they may conduct on-site examinations and impose additional reporting requirements. Chinese financial supervisors coordinate supervision and share supervisory information about Chinese financial institutions as appropriate.

The IMF recently concluded a financial system stability assessment of China ("FSSA"), including an assessment of China's compliance with the Basel Core Principles.[15] The FSSA determined that China's overall regulatory and supervisory framework adheres to international standards.[16]The FSSA found that "[t]he laws, rules and guidance that CBRC operates under generally establish a benchmark of prudential standards that is of high quality and was drawn extensively from international standards and the [Basel Core Principles] themselves."[17] The FSSA additionally noted that "[c]onsolidated supervision of banks and their direct subsidiaries and branches on the mainland or offshore is of high quality."[18] With respect to the CBRC, the FSSA found as follows:

All the banks, auditors, ratings agencies and other market participants that the mission interacted with were unhesitating in their regard for the role that the CBRC has played in driving professionalism, risk management and international recognition of the Chinese banking system. In particular, the mission observed that [the CBRC] has been the key driving force in driving improvements in risk management, corporate governance and internal control and disclosure in Chinese banks.[19]

Based on its review, the FSSA rated China's overall compliance with the Basel Core Principles as satisfactory. In giving this overall rating, the FSSA noted several areas that merited improvement and made specific recommendations for continued advances in supervision and regulation.[20] The Chinese authorities noted that some of the recommendations of

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[15] The assessment reflects the regulatory and supervisory framework in place as of June 24, 2011. IMF, *People's Republic of China, Financial System Stability Assessment* (June 24, 2011), available at www.imf.org/external/pubs/ft/scr/2011/cr11321.pdf. The FSSA covers an evaluation of three components: (1) the source, probability, and potential impact of the main risks to macrofinancial stability in the near term; (2) the country's financial stability policy framework; and (3) the authorities' capacity to manage and resolve a financial crisis should the risks materialize. The FSSA is a key input to IMF surveillance. The FSSA is a forward-looking exercise, unlike the Board's assessment of the comprehensive consolidated supervision of an applicant.

The IMF and World Bank separately publish a detailed assessment of the country's observance of the Basel Core Principles that discusses the country's adherence to the Basel Core Principles in much greater detail. *See* IMF and World Bank, *People's Republic of China: Detailed Assessment Report of Observance with Basel Core Principles for Effective Banking Supervision* (April 2012) ("DAR"), available at www.imf.org/external/pubs/ft/scr/2012/cr1278.pdf.

[16] FSSA at 39.

[17] Id. at 59; DAR at 12.

[18] FSSA at 64; DAR at 16.

[19] DAR at 7.

[20] FSSA at 39-42 and 69-71; DAR at 99-101. China received a materially noncompliant rating in two of the thirty areas assessed by the FSSA. Specifically, the FSSA rated China as materially noncompliant for the Basel Core Principles on independence, accountability and transparency, and risk management process. DAR at 17 and 19. The FSSA stated that "budgeting arrangements, external headcount approval requirements and [the authority for the State Council to override] rules and decisions compromise CBRC effectiveness and could affect operational independence." FSSA at 64; DAR at 17. The FSSA viewed the guidance that the CBRC has issued in risk management to be consistent with international standards but found that banking institutions' compliance with CBRC guidance was lacking (although recognizing that the guidance on some risks "is recent and so could not be expected to be complied with as yet"). FSSA at 61; *see also* DAR at 53. The assessment team also believed that Chinese banks in general do not yet have robust enterprise-wide risk-management systems. FSSA at 66; DAR at 53-54. For comparison, the United Kingdom and Germany received three and two materially noncompliant ratings, respectively, and the United States received one materially noncompliant rating, in their recent financial system stability assessments.

the FSSA are already being implemented and that others will be taken into account in the CBRC's plans to improve supervisory effectiveness.[21]

The Board has taken into account the FSSA's views that China is, overall, in satisfactory compliance with the Basel Core Principles and that there are areas for further improvement. The Board has also taken into account the responses by Chinese authorities to the FSSA report and the progress made by Chinese authorities to address the issues raised in that report.

Based on all the facts of record, including its review of the supervisory framework implemented by the CBRC for BOC, the Board has determined that BOC is subject to comprehensive supervision on a consolidated basis by its home country supervisors. This determination is specific to BOC.[22] By statute, the Board must review this determination in processing future applications involving BOC and also must make a determination of comprehensive, consolidated supervision in other applications involving different applicants from China.

As part of the Board's supervisory program for foreign banks, the Board actively monitors changes to the supervisory systems in the home countries of foreign banks, as well as differences that may exist in the supervisory framework as it is applied by a home country to institutions of different types or sizes, and would continue to do so with respect to China. The Board also intends to further its relationship with Chinese supervisory authorities and continue to develop its understanding of Chinese banking matters.

The government of China has adopted a statutory regime regarding anti money laundering ("AML") and suspicious activity reporting and has criminalized money laundering activities and other financial crimes. The PBOC supervises and examines Chinese banks with respect to AML and coordinates efforts among other agencies. The PBOC collects, monitors, analyzes, and disseminates suspicious transaction reports and large-value transaction reports.

The PBOC over time has increased requirements for its supervised institutions regarding AML compliance. The PBOC issued rules providing clarification of, or further strengthening the implementation of, operating procedures, customer due diligence and risk classification, recordkeeping, AML monitoring and reporting suspicious transactions, and the international remittance agency business. The PBOC also requires the designation of a chief AML compliance officer as a high-level manager to ensure provision of adequate AML resources and timely flow of information to employees responsible for AML compliance throughout the institution. In addition, the PBOC requires the risk rating of customers and the filing of reports on suspicious activity and certain other transactions. Banks are required to (1) establish a customer identification system in accordance with applicable rules jointly promulgated by the PBOC and three functional financial services regulators;[23]

[21] FSSA at 71-73; DAR at 101-103. Chinese authorities responded that, by law in China, the State Council of the People's Republic of China ("State Council") may alter or annul a rule or guideline of the CBRC only if the rule or guideline violates applicable law and that the State Council has never altered or annulled the rules and guidelines issued by the CBRC. Chinese authorities also noted that the State Council has supported the CBRC in undertaking banking regulation and supervision and that the CBRC has upgraded the number and quality of its staff over time. FSSA at 71-72; DAR at 102. In addition, Chinese authorities noted the significant improvements China has made in supervision as well as the relative simplicity of the Chinese banking system. FSSA at 72; DAR at 102-3. Despite the difference in views about the degree to which Chinese banks' risk management is commensurate with the current risk environment, Chinese authorities concurred with the FSSA that "continued improvements in banks' risk management are needed, as financial reform deepens and liberalization creates greater interconnectedness and complexities in the Chinese system." FSSA at 72; DAR at 103.

[22] *See* 58 *Federal Register* 6348, 6349 (January 12, 1993).

[23] Those regulators are the CBRC, CSRC, and CIRC.

(2) record the identities of customers and information relating to each transaction; and (3) retain retail transaction documents and books. Supervised institutions have been encouraged to move beyond a prescriptive-criteria basis to include a more expansive and risk-based approach to suspicious activity detection and reporting.

China participates in international fora that address the prevention of money laundering and terrorist financing. China became a member of the Financial Action Task Force ("FATF") in June 2007. China also is a member of the Eurasian Group ("EAG"), a FATF-style regional body that supports member countries in their efforts to create and maintain an appropriate legal and institutional framework to combat money laundering and terrorist financing in line with FATF standards.[24] EAG evaluates its member states' AML and counter-terrorist financing ("CFT") systems for compliance with international standards. In the most recent mutual evaluation report of China, dated February 17, 2012, the FATF considered China to be fully or largely compliant with almost all of the FATF recommendations and held that China has effective AML and CFT systems in force. As a result, the FATF has removed China from its regular follow-up process.[25]

Moreover, the Chinese government issues rules on implementing United Nations sanctions and may take enforcement actions to ensure compliance with those sanctions. The PBOC is also responsible for disseminating information to the banking industry regarding U.N. sanctions and supervising the enforcement of those sanctions.

The PBOC supervises and regulates compliance by BOC with AML requirements through a combination of on-site examinations and off-site monitoring. On site examinations focus on BOC's compliance with AML laws and rules. The PBOC's headquarters conducts investigations of a financial institution's head office, and the PBOC's branches conduct investigations of the institution's branch offices in the same locality as the PBOC branches. During the course of an on-site examination, the PBOC will generally review account information, transaction records, and any other relevant materials. Upon completion of an investigation, if AML deficiencies are identified, the PBOC may issue sanctions and propose that remedial measures be imposed by appropriate government agencies or regulators against the financial institution and can refer any suspected money laundering to law enforcement authorities for further investigation. The PBOC performs off site monitoring through periodic reports and has established requirements for Chinese banks to submit such reports. In order to improve off-site supervision and monitoring of large amount cash transactions, the PBOC developed an interactive information technology system for AML/CFT supervision that has been in operation since October 2010 in both the PBOC and financial institutions.

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[24] China also is a party to other agreements that address money laundering or terrorist financing, including the U.N. Convention Against the Illicit Traffic of Narcotics and Psychotropic Substances, the U.N. Convention Against Transnational Organized Crime, the U.N. Convention Against Corruption, and the U.N. International Convention for the Suppression of the Financing of Terrorism.

[25] *FATF, China Mutual Evaluation 8th Follow-up Report, Anti-Money Laundering and Combating the Financing of Terrorism*(February 17, 2012), available at www.fatf-gafi.org/dataoecd/5/34/49847246.pdf. The report noted that China has made significant progress to address the remaining deficiencies and has "reached a satisfactory level of compliance with all six core Recommendations and eight of the [ten] key Recommendations." Id at para. 41. In one of the key Recommendations where China has not attained a satisfactory level of compliance (implementation of international instruments related to terrorist financing), China has substantially addressed part of the deficiency and continues to make progress. With respect to the other key Recommendation (freezing of terrorist-related assets), China has made significant progress since June 2011 to improve its implementation. In particular, China has implemented legislation establishing a legislative framework and administrative authority for enforcement and has responded to foreign requests to freeze assets. The FATF was of the view that China should enact additional guidance to improve implementation, and Chinese authorities are currently drafting rules to do so. Id. at paras. 150-52 and 157-59.

BOC has policies and procedures to comply with Chinese laws and rules regarding AML. BOC states that it has implemented measures consistent with the recommendations of the FATF and that it has put in place policies, procedures, and controls to ensure ongoing compliance with all statutory and regulatory requirements, including designating AML compliance personnel and conducting routine employee training at all BOC branches. BOC's compliance with AML requirements is monitored by the PBOC and by BOC's internal and external auditors.

Based on all the facts of record, the Board has determined that the AML efforts by BOC and its home country supervisors are consistent with approval.

The Board has also considered the financial and managerial factors in this case. The CBRC requires Chinese banks to follow the Basel I Capital Accord with certain enhancements from the Basel II Capital Accord.[26] The capital levels of BOC exceed the minimum levels that would be required under the Basel I Capital Accord and are considered to be equivalent to the capital levels that would be required of a U.S. banking organization. Managerial and other financial resources of BOC are consistent with approval, and BOC appears to have the experience and capacity to support the proposed branch. In addition, BOC has established controls and procedures for the proposed branch to ensure compliance with U.S. law and for its operations in general. In particular, BOC has stated that it will apply strict AML policies and procedures at the branch consistent with U.S. law and regulation and will establish an internal control system at the branch consistent with U.S. requirements to ensure compliance with those policies and procedures.

With respect to access to information about BOC's operations, the Board has reviewed the restrictions on disclosure in relevant jurisdictions in which BOC operates and has communicated with relevant government authorities regarding access to information. BOC has committed to make available to the Board such information on the operations of BOC and any of its affiliates that the Board deems necessary to determine and enforce compliance with the IBA, the BHC Act, and other applicable federal laws. To the extent that the provision of such information to the Board may be prohibited by law or otherwise, BOC also has committed to cooperate with the Board to obtain any waivers or exemptions that may be necessary to enable it or its affiliates to make such information available to the Board. The Board also has consulted with the CBRC about access to information. The CBRC has represented that it would facilitate the Board's access to information and has entered into a statement of cooperation with the Board and other U.S. banking regulators with respect to the sharing of supervisory information.[27] In light of these commitments and other facts of record, and subject to the condition described below, the Board has determined that BOC has provided adequate assurances of access to any necessary information that the Board may request.

China has made progress toward adopting a system of financial regulation for its financial system to mitigate the risk to financial stability from its banks. The PBOC, CBRC, other financial supervisory agencies, and other agencies in China have taken joint measures to maintain financial stability. China has established a system of preliminary indicators for monitoring financial stability, developed methodology and operational frameworks for monitoring financial risks, and published an annual China Financial Stability Report since 2005. The CBRC has established mechanisms to cooperate with supervisory authorities in at least 25 other countries for the supervision of cross-border banking. In addition, the

[26] The CBRC also requires all large, internationally active banks, such as BOC, to have a minimum risk-based tier 1 capital ratio of 9 percent and total capital ratio of 11.5 percent. BOC's capital ratios exceed these levels.

[27] *See* Memorandum of Understanding between the CBRC and the Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation, June 17, 2004.

PBOC and CBRC officially joined the Basel Committee on Banking Supervision on behalf of China and since their accession, have actively participated in the revision of the Basel II Capital Accord, in the formulation of the Basel III Capital Accord, and in other working groups. China also is active in the ongoing work of the Financial Stability Board. U.S. bank regulators and other bank supervisors in pertinent jurisdictions participated in two supervisory colleges hosted by the CBRC: one for ICBC in 2009 and one for CCB in 2011. Moreover, authorities in the United States and China that are responsible for the oversight of auditing services for public companies are engaged in continuing discussions with respect to enhancing cross-border cooperation, and the Board looks forward to timely negotiation of an agreement relating to cooperative actions by these authorities.

The IBA establishes criteria that must be met before the Board can approve the establishment of a branch outside the foreign bank's home state. BOC's home state is New York. Under section 5(a)(1) of the IBA, as amended by section 104 of the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994,[28] a foreign bank, with the approval of the Board and the Office of the Comptroller of the Currency ("OCC"), may establish and operate a federal branch in any state outside its home state to the extent that a national bank with the same home state as the foreign bank could do so under section 36(g) of the National Bank Act. Section 36(g), which previously authorized states to "opt-in" to interstate de novo branching, was amended by section 613 of the Dodd-Frank Wall Street Reform and Consumer Protection Act to permit national banks to establish interstate de novo branches nationwide.[29] The Board has determined that all the other criteria referred to in sections 5(a)(1) and 5(a)(3) of the IBA, including the criteria in section 7(d) of the IBA, have been met.[30] In view of all the facts of record, the Board is permitted to approve the establishment of an interstate de novo federal branch by BOC under section 5(a) of the IBA.

On the basis of all the facts of record, and subject to the commitments made by BOC, as well as the terms and conditions set forth in this order, BOC's application to establish a branch is hereby approved. The Board conditions its decision on BOC providing to the Board adequate information on its operations and activities as well as those of its affiliates to determine and enforce compliance by BOC or its affiliates with applicable federal statutes. Should any restrictions on access to information on the operations or activities of BOC or any of its affiliates subsequently interfere with the Board's ability to obtain information to determine and enforce compliance by BOC or its affiliates with applicable federal statutes, the Board may require termination or divestiture of any of BOC's or its affiliates' direct or indirect activities in the United States. Approval of this application also is specifically conditioned on compliance by BOC with the commitments made to the Board in

[28] 12 U.S.C. § 3103(a)(1).

[29] 12 U.S.C. § 36(g)(1)(A).

[30] Section 36(g) of the National Bank Act and section 5(a) of the IBA require that certain conditions of section 44 of the Federal Deposit Insurance Act ("FDI Act") be met in order for the Board to approve a de novo interstate federal branch. *See* 12 U.S.C. § 36(g)(2) and 12 U.S.C.§ 3103(a)(3)(C) (referring to sections 44(b)(1), 44(b)(3), and 44(b)(4) of the FDI Act, 12 U.S.C. §§ 1831u(b)(1), (b)(3), and (b)(4)). The Board has determined that BOC is in compliance with state filing requirements. Community reinvestment considerations are also consistent with approval, as BOC's two insured New York City branches received a Community Reinvestment Act ("CRA") rating of "satisfactory" from the OCC at their most recent CRA performance evaluation dated August 18, 2008. BOC was adequately capitalized as of the date the application was filed, and on consummation of this proposal, BOC would continue to be adequately capitalized and adequately managed.

In accordance with section 5(a)(3)(B)(ii) of the IBA (12 U.S.C. § 3103(a)(3)(B)(ii)) and section 211.24(c)(3)(i)(B) of Regulation K (12 CFR 211.24(c)(3)(i)(B)), the Board has consulted with the Department of the Treasury regarding capital equivalency.

connection with this application and with the conditions in this order.[31] The commitments and conditions referred to above are conditions imposed in writing by the Board in connection with this decision and may be enforced in proceedings under 12 U.S.C. § 1818 against BOC and its affiliates.

By order of the Board of Governors, effective May 9, 2012.

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

Robert deV. Frierson
Deputy Secretary of the Board

Final Enforcement Decision Issued by the Board

In the Matter of Louis A. DeNaples, An Institution-Affiliated Party of First National Community Bancorp, Dunmore, Pennsylvania, and Urban Financial Group, Inc., Bridgeport, Connecticut

FRB Docket No. 09-191-B-I

This is an administrative proceeding pursuant to the Federal Deposit Insurance Act ("the FDI Act") in which the Enforcement Counsel for the Board seeks an order requiring Respondent, Louis A. DeNaples, to cease and desist from his alleged continuing violation of section 19 of the FDI Act, 12 U.S.C. § 1829.

Under section 19, an individual who has agreed to enter into a pretrial diversion or similar program in connection with certain criminal charges must seek the Board's consent in order to continue as an institution-affiliated party of a bank holding company. Here, it is undisputed that Respondent did not seek that consent after he entered into an agreement with a state district attorney withdrawing charges of perjury in exchange for promises by the Respondent, but he did continue to be an institution-affiliated party at two bank holding companies. Respondent argues that no consent is required and that he may continue to serve as an institution-affiliated party because the withdrawal agreement was not an "agree[ment] to enter into a pretrial diversion or similar program" as that term is defined under section 19. As discussed below, however, the Board determines that the withdrawal agreement does constitute the type of program covered by section 19, and that by failing to seek the Board's consent to his continued service as an institution-affiliated party, the Respondent has deprived the Board of its statutorily-mandated opportunity to review whether to permit his continued involvement with those companies. The Board also rejects other procedural and substantive arguments raised by Respondent. Therefore, upon review of the administrative record and additional filings made to the Board, the Board issues this Final Decision adopting the Recommended Decision ("Recommended Decision") of Administrative Law Judge C. Richard Miserendino (the "ALJ"), except as modified herein, and orders the issuance of the attached Order to Cease and Desist.

[31] The Board's authority to approve the establishment of the proposed branch parallels the continuing authority of the OCC to license offices of a foreign bank. The Board's approval of this application does not supplant the authority of the OCC to license the proposed office of BOC in accordance with any terms or conditions that it may impose.

I. Statement of the Case

A. Statutory and Regulatory Framework

A number of provisions of the FDI Act are implicated in this administrative enforcement action. Section 19 of the FDI Act ("section 19"), 12 U.S.C. § 1829, makes it illegal for any person to become or continue to be an institution-affiliated party with respect to any bank holding company ("BHC"), own or control a BHC, or participate in the conduct of the affairs of a BHC without the consent of the Board if that person has been convicted of a criminal offense involving dishonesty or a breach of trust or money laundering, or has agreed to enter into a pretrial diversion or similar program in connection with such an offense. 12 U.S.C. § 1829(a)(1)(A), (d)(1).[1] A person is an institution-affiliated party of a bank holding company if, among other things, he or she is an officer, director, employee, or controlling stockholder of the BHC, or has filed or is required to file a change in control notice under the Change in Bank Control Act, 12 U.S.C. § 1817(j). 12 U.S.C. § 1813(u), 1818(b)(3) (applying the penalty provisions of section 1818 to bank holding companies in the same way as they apply to state member banks); In re Pharaon, 83 Federal Reserve Bulletin 347, 348 n.2 (1997).

Section 8(b) of the FDI Act, 12 U.S.C. § 1818(b), spells out the substantive requirements for issuing a cease-and-desist order. A cease-and-desist order may be imposed when the agency has reasonable cause to believe that the respondent has engaged or is about to engage in an unsafe or unsound practice in conducting the business of a depository institution, or that the respondent has violated or is about to violate a law, rule, or regulation or condition imposed in writing by the agency. 12 U.S.C. § 1818(b)(1). A cease-and-desist order may require the respondent to take affirmative action the agency determines to be appropriate to correct or remedy any conditions resulting from the violation or practice with respect to which such order is issued. 12 U.S.C. § 1818(b)(6)(F). The power to issue cease-and-desist orders includes the authority to place limitations on the activities of the respondent. 12 U.S.C. § 1818(b)(7).

Under section 8(b) and the Board's regulations, the ALJ is responsible for conducting proceedings on a notice of charges relating to a proposed order to cease and desist. 12 U.S.C. § 1818(b). The ALJ issues a recommended decision that is referred to the Board together with any exceptions to those recommendations filed by the parties. The Board makes the final findings of fact, conclusions of law, and determination whether to issue the requested orders. 12 CFR 263.38.

Respondent asserts that an additional section of the FDI Act is relevant to this proceeding. Section 8(g) of the Act sets forth a separate procedure and substantive basis for addressing certain misconduct by bank officials and employees. Under section 8(g), a federal banking agency may issue a pre-hearing order of removal or prohibition against a bank official or employee if (1) a judgment of conviction or an agreement to enter a pretrial diversion or other similar program is entered against the respondent in connection with certain specified crimes or any crime involving dishonesty or breach of trust which is punishable by imprisonment for a term exceeding one year; and (2) continued service or participation by the respondent would threaten the interests of depositors or impair public confidence in a depository institution. 12 U.S.C. § 1818(g)(1)(C). Section 8(g)(3) sets out a procedure for post-deprivation process in the case of an order issued under section 8(g)(1), in which the respondent may seek to show that his or her continued participation in the institution's affairs would not pose a threat to the institution's depositors or impair public confidence in

[1] The same conduct is proscribed for institution-affiliated parties of insured depository institutions absent the approval of the Federal Deposit Insurance Corporation. 12 U.S.C. § 1829(a)(1).

the institution. 12 U.S.C. §1818(g)(3).

B. Facts[2]

[2] First National Community Bancorp ("First National"), Dunmore, Pennsylvania, and Urban Financial Group, Inc. ("Urban Financial"), Bridgeport, Connecticut, are registered bank holding companies. Respondent is currently chairman and a director of First National, owns 10.26 percent of its voting shares, and is a member of a group that owns approximately 19.87 percent of its voting shares. Respondent is the largest shareholder of Urban Financial, owning approximately 45 percent of its shares. Accordingly, Respondent is an institution-affiliated party of both First National and Urban Financial. 12 U.S.C. § 1813(u).

On January 30, 2008, the District Attorney of Dauphin County, Pennsylvania ("District Attorney") filed a criminal complaint against Respondent that charged him with four counts of perjury in connection with testimony Respondent gave to the Pennsylvania Gaming Control Board while in the process of obtaining a gaming license for a casino he owned. Respondent took a leave of absence from his position as chairman and director of First National shortly after the charges were filed and to date remains on leave of absence.

On April 15, 2009, after months of negotiations, Respondent and the District Attorney entered into an Agreement for Withdrawal of Charges ("Withdrawal Agreement"). Under the written terms of the Agreement, the District Attorney agreed to withdraw all of the criminal charges but reserved the right to reinstate the charges upon a material breach of any term of the Withdrawal Agreement by Respondent. Respondent in turn agreed, among other things, to transfer his interest in the casino to a trust for the benefit of his daughter, transfer to the trust any profits accrued in the casino during the period of suspension of his gaming license, pay the cost of prosecution, and provide quarterly reports to the District Attorney regarding his compliance with the Withdrawal Agreement for two years following execution. Based on the Withdrawal Agreement, the Board initiated this enforcement proceeding against Respondent.

Following the ALJ's issuance of his Recommended Decision, the Court of Common Pleas of Dauphin County, Pennsylvania, at Respondent's request, issued two Orders relevant to this matter. The first, issued May 18, 2011 ("Expungement Order"), was a form order providing that Respondent's "arrest record regarding these charges shall be expunged" and directing "all criminal justice records upon whom this order is served" to "expunge and destroy" documents pertaining to the proceedings. The Expungement Order did not mention the Withdrawal Agreement. The second, issued September 19, 2011 ("Clarifying Order"), "clarified" the prior order by stating, in part: "Encompassed within the Expungement Order was the Agreement for Withdrawal of Charges ('Withdrawal Agreement'). Since it has been completely and forever expunged, the Withdrawal Agreement is of no force or effect."

C. Procedural History

On November 23, 2009, the Board issued a Notice of Charges and of Hearing Issued Pursuant to section 8(b) of the FDI Act ("Notice") alleging that Respondent had not sought or received the Board's permission to continue to be an institution-affiliated party within the meaning of section 19(a)(1)(A)(ii), despite the fact that he entered into a pretrial diver-

[2] Except where specifically noted, the stated facts are undisputed by the parties. *See* Enforcement Counsel's Statement of Material Facts Not in Dispute ("FRB SOF"), filed March 25, 2010, and Respondent's Statement of Undisputed Material Facts ("Resp. SOF"), filed April 5, 2010.

sion agreement to resolve criminal charges. The Notice sought a cease-and-desist order requiring Respondent to resign his position as director of First National and submit an acceptable plan to the Board for the prompt divestiture of his controlling shareholdings in First National and Urban Financial.[3] Respondent timely filed an answer to the Notice, admitting that he is the chairman (albeit on a leave of absence) of First National; that he owns 10.26 percent of the voting shares of First National and has been a member of a control group that filed a notice of change in bank control with the Federal Reserve; and that he owns 45 percent of the voting shares of Urban Financial. Respondent further admitted that he has not sought or received the Board's permission to be an institution-affiliated party of First National or Urban Financial after entering into the agreement. Respondent denied that he has violated section 19, asserting that the agreement into which he entered was not a "pretrial diversion or similar program" within the meaning of section 19.

On February 12, 2010, Enforcement Counsel filed a Motion to Strike Respondent's Request for Production of Documents. Respondent's production request had generally sought discovery concerning whether Respondent's continued participation in First National and Urban Financial would cause harm to the institutions. The ALJ granted Enforcement Counsel's Motion to Strike on the grounds that discovery concerning harm to the financial institutions was not materially relevant to a proceeding brought under section 8(b).

Enforcement Counsel and Respondent each filed motions for summary disposition accompanied by statements of material facts not in dispute. On July 23, 2010, Respondent filed a Motion for Leave to File a Notice of Supplemental Authority in Support of his Cross-Motion for Summary Disposition and the corresponding Notice of Supplemental Authority ("First Notice of Supplemental Authority"), which was denied by the ALJ on August 11, 2010.

On February 18, 2011, the ALJ issued a Recommended Decision advising that Enforcement Counsel's Motion for Summary Disposition be granted and that Respondent's Cross-Motion for Summary Disposition be denied, and recommending the issuance of the cease and-desist order against Respondent.[4] Respondent subsequently filed exceptions to the ALJ's Recommended Decision and the matter was referred to the Board for final decision. *See*12 CFR 263.38-39. On March 29, 2011, the Board issued a notice acknowledging that the complete record of the matter had been submitted to the Board. *See*12 CFR 263.40.

Nonetheless, on April 4, 2011, Respondent filed with the Board a Request to Reopen the Record and Notice of Supplemental Authority in Support of his Exceptions ("Second Notice of Supplemental Authority"), which was opposed by Enforcement Counsel. On April 27, 2011, Respondent filed a Reply in Support of Notice of Supplemental Authority ("Third Notice of Supplemental Authority") which contained further new documentary evidence in support of Respondent's exceptions. Enforcement Counsel duly opposed that supplemental filing as well. On May 25, 2011, Respondent filed a Motion for Immediate Dismissal of Cease and Desist Proceedings based on the issuance of a state court order granting his petition for expungement of his criminal record ("First Motion for Immediate

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[3] On November 24, 2009, the Office of the Comptroller of the Currency ("OCC") issued a substantially similar Notice of Charges seeking a cease-and-desist order requiring Respondent's resignation from his position as chairman and director of First National Community Bank ("Bank"). In his Recommended Decision, the ALJ consolidated the proceedings for the Board's Notice and the OCC's Notice of Charges. On March 23, 2012, the OCC entered order requiring Respondent to cease and desist from his continuing violation of section 19, including by resigning from all positions that he holds as an institution-affiliated party.

[4] The ALJ's Recommended Decision also recommended that the OCC grant the OCC Enforcement Counsel's motion for summary disposition and issue the OCC Enforcement Counsel's requested cease-and-desist order. As noted earlier, the OCC issued its final decision adopting this recommendation on March 23, 2012.

Dismissal"). This was followed by a second Motion for Immediate Dismissal of Cease and Desist Proceedings based on a clarification of the state court expungement order ("Second Motion for Immediate Dismissal"). Enforcement Counsel opposed both motions. Despite the fact that these various filings were made after the Board notified parties that the record was closed, the Board has considered them in its final decision.

II. Discussion

This proceeding raises several novel issues for the Board. First, the Board must consider Respondent's argument that a cease-and-desist proceeding under section 8(b) of the FDI Act is improper procedurally, and that the only way the Board could obtain the relief sought would have been to proceed under section 8(g). Second, the Board must decide whether by entering into the Withdrawal Agreement, Respondent entered into a "pretrial diversion or similar program" within the meaning of section 19 of the FDI Act. Finally, the Board must address the effect of the Expungement Order and the Clarifying Order on that determination.

Most of these issues were raised before the ALJ,[5] who recommended issuance of a cease and-desist order against Respondent under section 8(b) based on Respondent's violations of section 19.[6] The ALJ's recommended decision held that the Board had authority to proceed under section 8(b) to address violations of section 19. It also held that the Withdrawal Agreement was a "pretrial diversion or similar program" under section 19, and that state law did not govern the interpretation of that phrase. For the reasons set forth below, the Board affirms the ALJ's recommended decision and determines that the subsequent expungement of Respondent's criminal record does not divest the Board of authority to proceed to remedy a violation of section 19. The Board therefore issues the attached cease-and-desist order against Respondent.

A. The Board may enforce Section 19 through a cease-and-desist proceeding under Section 8(b)

Under section 8(b), the Board has the authority to serve on an institution-affiliated party within its regulatory jurisdiction a notice of charges seeking a cease-and-desist order if, in the Board's opinion, the institution-affiliated party "is violating or has violated . . . a law." 12 U.S.C. § 1818(b)(1). In the present case, after Respondent entered into the Withdrawal Agreement, the Board initiated a notice of charges against Respondent because it believed Respondent was violating section 19 of the FDI Act by continuing, without the consent of the Board, to be an institution-affiliated party of First National and Urban Financial after entering into a pretrial diversion or similar program. Section 19 is "a law" and, moreover, is within the same statute as section 8(b). The statutory language thus clearly supports the Board's authority to pursue a cease-and-desist order under section 8(b) to remedy a violation of section 19.

Despite the apparently clear statutory language, Respondent contends that section 8(b) cannot be used to enforce section 19 because he claims that section 19 is only a criminal statute. Respondent also argues that, to the extent the Board can address the involvement in banking of an individual who enters into a "pretrial diversion or other similar program," Sec-

[5] The ALJ did not address the effect of the Expungement Order or the Clarifying Order, which were issued after the issuance of the Recommended Decision.

[6] Respondent did not argue, either before the ALJ or in his Exceptions, that he was not an institution-affiliated party of First National or of Urban Financial or that his Withdrawal Agreement was not entered into in connection with a prosecution for an offense involving dishonesty within the meaning of section 19(a)(1). Accordingly, these issues are waived. 12 CFR 263.39(b).

tion 8(g) governs because it is more specific than section 8(b) and because using section 8(b) for this purpose essentially renders the bank officer removal provision of section 8(g) superfluous. Respondent cites Feinberg v. FDIC, 420 F.Supp. 109 (D.D.C. 1976), to argue that only section 8(g) can be used for removal because it provides constitutionally guaranteed substantive and procedural safeguards that are lacking in section 8(b).

Respondent's first argument fails because the structure of section 19 alone shows that it is not purely a criminal statute, and because, even if it were, it would support an administrative enforcement action under section 8 of the FDI Act. Subsection 19(a)(1) prohibits certain conduct, including serving, without the appropriate regulator's consent, as an institution-affiliated party after agreeing to enter into a pretrial diversion or similar program related to a crime of dishonesty. 12 U.S.C. § 1829(a)(1). Subsection 19(b) creates a criminal penalty for "[w]hoever knowingly violates subsection (a)." 12 U.S.C. § 1829(b) (emphasis added). While the statute thus provides that a subset of the conduct prohibited in subsection 19(a)(1), namely "knowing" violations, may be criminally punished, this by no means limits the breadth or administrative enforceability of the prohibition contained in subsection 19(a)(1). Moreover, even assuming section 19 were purely a criminal statute, section 8(b) allows for the Board to require compliance with it through a cease-and-desist proceeding under section 8(b). *See* Cousin v. OTS, 73 F.3d 1242, 1251 (2d Cir. 1996) (criminal bribery charge is sufficient to support removal under the analogous provision of the Home Owners' Loan Act).

Respondent's second argument is based on what he sees as a conflict between section 8(g) of the FDI Act, which sets forth a procedure for suspension or prohibition of institution-affiliated parties involved in certain crimes, and the approach taken by Board Enforcement Counsel here, which used the more general authority in section 8(b) of the FDI Act to issue a cease-and-desist order for a violation of section 19 of that Act, which in turn refers to similar crimes. In short, Respondent argues that the Board may not use section 8(b) to remove Respondent from his position, but may only use the procedures set forth in section 8(g); to hold otherwise, argues Respondent, would render section 8(g) superfluous. In support of this argument, Respondent cites a general canon of statutory interpretation which states "[w]hen both specific and general provisions cover the same subject, the specific provision will control, especially if applying the general provision would render the specific provision superfluous." Norwest Bank Minn. Nat. Ass'n v. FDIC, 312 F.3d 447, 451 (D.C. Cir. 2002). Respondent's argument fails, however, because section 8(g) and section 19 do not "cover the same subject." Section 19 covers cases in which a respondent has been convicted of, or has agreed to enter a pretrial diversion or similar program in connection with a prosecution for, any crimes involving "dishonesty or a breach of trust or money laundering." By contrast, section 8(g) limits its reference to crimes of dishonesty or breach of trust to those crimes punishable by imprisonment of at least a year.

Additionally, as Respondent correctly notes, section 8(g) calls for different procedures than section 8(b). This difference in procedures does not, however, make it impermissible for Enforcement Counsel to proceed under section 8(b), as Respondent argues. Rather, so long as the procedures provided for in each subsection comply with constitutional standards of due process, the decision on how to proceed is entirely within the discretion of the Board.[7] Feinberg, cited by Respondent, does not suggest otherwise. In that case, the district court

[7] Respondent argues that the permissive term "may" in section 8(b) (providing that if an institution-affiliated party "is violating . . . a law," the agency "may issue . . . a notice of charges" in respect thereof) means only that "while Enforcement Counsel can decide whether to bring an action to remove a banking official, such an action, if pursued[,] must be prosecuted under section 8(g)." Respondent's Brief in Support of Exceptions at 11. There is nothing in the statutory language of section 8(b) that compels or even permits this interpretation, and the Board declines to adopt it.

struck down on due process grounds an earlier version of section 8(g) (not section 8(b)) because it did not provide for any hearing, either before or after issuance of a prohibition order, substantially limited judicial review, and would likely result in a permanent loss of property of the individual being suspended. Feinberg, 420 F.Supp. at 112, 119-21. But section 8(b), under which Enforcement Counsel proceeded, already has all of the constitutional protections identified by the Feinberg court, so Feinberg provides no basis for challenging Enforcement Counsel's choice of enforcement mechanism.[8] Moreover, section 8(b) provides for a pre-deprivation notice and hearing, rather than the post-deprivation mechanism provided in section 8(g), so from a constitutional standpoint its protections are even greater. *See* 12 U.S.C. § 1818(b)(1), (h).

Respondent makes much of the fact that section 8(g) describes an additional "harm" factor as necessary to remove an institution-affiliated party, while neither section 19 nor section 8(b) contains such a requirement.[9] However, Congress could reasonably have decided, as the FDI Act indicates, that before initiating an action under section 8(g) to deprive an individual of his or her position without a prior hearing, the banking agencies must have a strong interest in proceeding, based on the potential for harm to the public interest. This heightened harm requirement acts as a check on an agency's ability to remove individuals without a prior hearing except where the public interest is at its highest. In contrast, a cease-and-desist order under section 8(b) serves occasions where the agency determines it is unnecessary to act against an individual immediately and chooses to provide pre-deprivation procedures instead. This may be because the agency sees less immediate harm, such as when, as here, the institution-affiliated party has already taken a leave of absence from his banking positions. Rather than rendering section 8(g) superfluous, the provisions of section 8(b) simply provide a different tool for agencies to use under certain circumstances where the agency decides it is more appropriate. The fact that Enforcement Counsel availed itself of one enforcement tool over another is not impermissible.

Moreover, the Board's decision to use the pre-deprivation hearing procedures of section 8(b), which unlike section 8(g) does not contain an explicit harm standard, does not negate the strong public interest in requiring agency review before an individual with a history of crimes involving dishonesty or breach of trust is permitted to continue as an institution-affiliated party. Congress, by prohibiting such involvement absent agency approval, has already determined that individuals whose conduct is among the offenses listed in section 19 cause continuing harm to the public confidence in financial institutions. Because under section 8(b) the individual has an opportunity to challenge the basis for a cease-and-desist order before it is issued, the agency need not make a special showing of harm beyond the fact that the requirements of section 19 have been met. As Feinberg noted, "[t]he fundamental requisite of due process of law is the opportunity to be heard." 420 F.Supp. at 119 (quoting Grannis v. Ordean, 234 U.S. 385, 394 (1914)). In reviewing section 8(b) and

[8] Section 8(g) has since been amended, and the Supreme Court has found it to be constitutionally sound. *See* FDIC v. Mallen, 486 U.S. 230, 248 (1988).

[9] The Board notes that Respondent appears to misconstrue section 8(g) by suggesting the Board must show harm to the institution or the public in order to remove an individual under section 8(g). Section 8(g) actually places the burden on respondents to disprove harm. The Board must initially determine that an individual's continued service as an institution-affiliated party would cause harm before issuing a prohibition notice, but to challenge this notice, the respondent must "show that the continued service to or participation in the conduct of the affairs of the depository institution by such party does not, or is not likely to, pose a threat to the interests of the bank's depositors or threaten to impair public confidence in the depository institution." 12 U.S.C.§ 1818(g)(1)(A), (3).

the Board's regulations, and how they were applied in these proceedings, the Board sees no reason to find Respondent has been denied his constitutional right to be heard.[10]

B. The Withdrawal Agreement as executed is an agreement "to enter into a pretrial diversion or similar program."

Respondent asserts that the ALJ erred in finding that Respondent "agreed to enter into a pretrial diversion or similar program" within the meaning of section 19 when he signed the Withdrawal Agreement. *See* 12 U.S.C. § 1829. Section 19 does not define "pretrial diversion or similar program." Respondent contends that state law should govern this question, and that under the law of Pennsylvania the Withdrawal Agreement does not constitute a pretrial diversion program.

Respondent argues in this regard that the Board must follow the interpretation in the FDIC Statement of Policy for section 19 of the FDI Act ("FDIC Policy Statement"). *See* www.fdic.gov/regulations/laws/rules/5000-1300.html. That Policy Statement provides in part that "[w]hether a program constitutes a pretrial diversion is determined by relevant federal, state, or local law, and will be considered by the FDIC on a case-by-case basis." The FDIC Policy Statement is, however, just that — a statement of policy of the FDIC. It is not legally binding on any party (save, perhaps, for the FDIC itself), *see*Ctr. for Auto Safety v. NHTSA, 452 F.3d 798, 807 (D.C. Cir. 2006) (general statements of policy "neither determine rights or obligations nor occasion legal consequences"). In any case, the FDIC Policy Statement is certainly not binding on the Board, which has sole interpretive and policy authority over section 19 with respect to bank holding companies.[11] The Board has never formally adopted the FDIC Policy Statement or any other policy interpreting "pretrial diversion or similar program" in section 19. Therefore, the Board is not bound by the FDIC Policy Statement and may exercise its own authority to interpret the term.

Though not authoritative for the Board, the FDIC Policy Statement contains a useful description of features that are generally part of a pretrial diversion or similar program.[12] The Board takes a similar view and will look for two characteristics in determining whether an agreement to enter a pretrial diversion or similar program exists: the agreement provides for (1) a suspension or eventual dismissal of charges or criminal prosecution, and (2) a voluntary agreement by the accused to treatment, rehabilitation, restitution or other noncriminal or nonpunitive alternatives. This is in line with the "ordinary" meanings of the term discussed in the Recommended Decision.

In making this determination, the Board is not bound, as Respondent has asserted, to follow state or local law definitions of "pretrial diversion." *See* Taylor v. United States, 495 U.S. 447, 451 (1990) (absent a plain indication to the contrary, federal laws are not construed so that their application depends on state law) (citing Dickerson v. New Banner Institute, Inc., 460 U.S. 103, 119-120 (1983); Mississippi Band of Choctaw Indians v. Holyfield, 490 U.S. 30, 43 (1989). The phrase "pretrial diversion or similar program" is found in

[10] As a related matter, the Board also affirms the ALJ's Order Granting Motion to Strike Production of Documents. Respondent had sought discovery related to the harm to the institution posed by his remaining as a director. For the reasons discussed above, the ALJ was correct in ruling such discovery was not relevant to this matter.

[11] *See* Collins v. NTSB, 351 F.3d 1246, 1254 (D.C. Cir. 2003) (where expert enforcement agencies have mutually exclusive authority over separate sets of regulated persons, each expert agency is entitled to deference in its interpretation of the statute). Section 19 is such a statute, with the FDIC having exclusive authority over participation in insured depository institutions, and the Board having exclusive authority over participation in bank holding companies and savings and loan holding companies.

[12] The FDIC Policy Statement states that a pretrial diversion or similar program "is characterized by a suspension or eventual dismissal of charges or criminal prosecution upon agreement by the accused to treatment, rehabilitation, restitution, or other noncriminal or nonpunitive alternatives." 63 *Federal Register* 66184-85.

a federal statute setting standards to be applied by federal banking agencies regarding parties who may be associated with federally-regulated depository institutions and holding companies. By requiring prior consent, section 19 ensures that the Board, as the federal regulator of bank holding companies, has an opportunity to scrutinize individuals when certain conduct —including the individual agreeing to enter into a pretrial diversion or similar program—has occurred, and make a judgment as to the benefits and risks of their continued involvement in banking. State law definitions of "pretrial diversion" are not meant to address this concern. Thus, the phrase must be interpreted as a matter of federal law.

However, state or local law may be relevant in some circumstances. For example, a program referred to by state authorities as a "pretrial diversion" program would likely meet the characteristics of a pretrial diversion or similar program under section 19. Nonetheless, the terminology used by a state— or the parties to an agreement – is not dispositive of whether a program is a "pretrial diversion or similar program" as that phrase is used in section 19. Accordingly, Respondent's contention that only state law definitions should govern the Board's interpretation of section 19 is rejected.

Similarly, Respondent's contention that the parties' subjective intent governs is also rejected. Under federal common law of contracts, although the parties' intent is the "paramount goal" in construing a contract, "[c]ourts are to consider 'not the inner, subjective intent of the parties, but rather the intent a reasonable person would apprehend in considering the parties' behavior.'" Baldwin v. Univ. of Pittsburgh Med. Ctr., 636 F.3d 69, 75 (3d Cir. 2011) (quoting Am. Eagle Outfitters v. Lyle & Scott Ltd., 584 F.3d 575, 582 (3d Cir. 2009)). The words of a contract "clearly manifest the parties' intent if they are capable of only one objectively reasonable interpretation." Baldwin, 636 F.3d at 76. Moreover, the results would not differ under Pennsylvania law. *See* Mellon Bank, N.A. v. Aetna Business Credit, Inc., 619 F2.d 1001, 1009-10 (3d Cir. 1980) (quoting Best v. Realty Management Corp., 101 A.2d 438, 440 (Pa. Super. 1953)) (finding that Pennsylvania courts do not psychically delve into the minds of the parties; rather, "[w]hen a written contract is clear and unequivocal, its meaning must be determined by its contents alone.").

In this case, the Withdrawal Agreement unequivocally states that the District Attorney would withdraw charges against Respondent but retained the right to reinstate charges upon material breach of any term of the Withdrawal Agreement by Respondent. *See* Answer ¶ 9 10, Resp. SOF ¶ 11. In exchange, Respondent was required to transfer his ownership interest in his casino to his daughter, transfer any profits that accrued from the casino to his daughter's trust, provide quarterly reports to the District Attorney regarding his compliance with the Withdrawal Agreement, and pay the cost of the prosecution of the case. *See* Resp. SOF ¶ 13. Thus, the Withdrawal Agreement on its face contains the characteristics of an agreement to enter a pretrial diversion or similar program: the District Attorney withdrew criminal perjury charges against Respondent conditioned on Respondent agreeing to certain noncriminal alternatives. Notwithstanding any subjective intent the signatories may have had (or have now) to avoid implication of section 19, the terms of the Withdrawal Agreement constitute an agreement to enter a pretrial diversion or similar program.

As an additional matter, Respondent has excepted to the ALJ's denial of his First Notice of Supplemental Authority, which proffered evidence meant to show the Respondent did not admit guilt to the charges underlying the Withdrawal Agreement and that the claims lacked

prosecutorial merit.[13] The Board agrees with the ALJ that this evidence would not aid in the determination of whether the Withdrawal Agreement constitutes an agreement to enter a pretrial diversion or similar program. Contrary to Respondent's assertions, an admission of guilt is not a standard prerequisite for all pretrial diversion programs. *See* National Association of Pretrial Services Agencies, Performance Standards and Goals for Pretrial Diversion/Intervention, Standard Commentary to Standard 4.4, p. 13 (Nov. 2008) (hereinafter "NAPSA Standards") ("Those potential participants who maintain their innocence should not be denied enrollment [in a pretrial diversion] if, after an opportunity to consult with counsel, they make an informed decision to take the diversion option."). Thus, evidence that Respondent did not admit guilt would not raise a dispute as to whether the Withdrawal Agreement was an agreement to enter into a pretrial diversion or similar program.

Respondent's argument that the Withdrawal Agreement could not be a pretrial diversion or similar program because cases that lack prosecutorial merit cannot be funneled into pretrial diversion or similar programs is also rejected. *See* Respondent DeNaples' Notice of Supplemental Authority in Support of His Cross-Motions for Summary Judgment at 4-5; *see also* NAPSA Standards, Standard 1.4 ("All cases considered for pretrial diversion/intervention should have prosecutorial merit."). The Withdrawal Agreement on its face indicates that the District Attorney agreed to withdraw charges based upon Respondent's agreeing to the terms therein and with the explicit understanding that the District Attorney could refile charges if Respondent materially breached the Withdrawal Agreement. This alone suggests that the District Attorney did not consider the case to lack prosecutorial merit. Cf. NAPSA Standards, Commentary to Standard 1.4 ("One of the underpinnings of diversion is that if defendant fails to comply with the program, he or she will be returned to the court for prosecution."). While Respondent's evidence may be relevant in evaluating a request for consent filed with the Board under section 19, should Respondent choose to submit one, it is not relevant in determining whether the Withdrawal Agreement is an agreement to enter into a pretrial diversion or similar program and whether Respondent is therefore required by section 19 to file such a request before continuing as an institution-affiliated party of a bank holding company, which is the subject of this proceeding.[14] Accordingly, the ALJ did not err in excluding Respondent's evidence.

For the reasons discussed above, the Board finds that by entering the Withdrawal Agreement, Respondent "agreed to enter into a pretrial diversion or similar program" within the meaning of section 19.[15]

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[13] The evidence submitted with the First Notice of Supplemental Authority consists of filings in the matter of United States v. D'Elia before the United States District Court for the Middle District of Pennsylvania. Respondent was not a party to this matter, which concerned whether Mr. D'Elia could receive a reduction of his current sentence based on information he provided regarding the criminal charges against Respondent that are the basis for the section 19 violation. In his First Notice of Supplemental Authority, Respondent cites language in an order by the district court which states in a summary of facts that the criminal charges against Respondent were withdrawn with no admission of guilt. Respondent also refers to language in the government's motion for reduction of sentence that he argues indicates the prosecutor withdrew the case against him because it was non-meritorious.

[14] Moreover, contrary to Respondent's assertions, the evidence he presented to the ALJ does not indicate that the District Attorney's case lacked prosecutorial merit. *See*First Notice of Supplemental Authority, Ex. B. The evidence is equivocal at best. It consists of a motion for sentence reduction filed in a matter to which neither the Respondent nor the District Attorney was a party. Moreover, although the motion states at one point that the "District Attorney decided the case could not be successfully prosecuted," the basic purpose of the motion is to argue that a different defendant's sentence should be reduced because information that the defendant provided was instrumental in helping the District Attorney secure the Withdrawal Agreement against Respondent.

[15] For the reasons discussed above, the Board also rejects Respondent's claim that he was inappropriately denied oral argument and an evidentiary hearing before the ALJ. Because Respondent did not deny the existence or validity of the relevant terms of the Withdrawal Agreement, the ALJ correctly determined that additional evi-

C. Respondent's Post-Record Notices of Supplemental Authority and Motions for Immediate Dismissal

After the Board notified parties that the record of these proceedings was complete, Respondent made two filings seeking to reopen the record to include additional affidavits and other materials: the Second and Third Notices of Supplemental Authority. He subsequently submitted two separate Motions for Immediate Dismissal, to which Enforcement Counsel responded. The Board has considered these filings and for the reasons discussed below rejects Respondent's submissions of additional material for the record, and denies his motions for immediate dismissal.

First, Respondent has not adequately explained why he did not raise the issues presented in these supplemental filings in the proceedings below. Respondent contends that "he repeatedly pressed for a hearing and the opportunity to present the affiants' live testimony" and only "learned that he would not receive the hearing to which he was entitled" when the ALJ issued his Recommended Decision. Third Notice of Supplemental Authority at 3. However, Respondent does not explain why the affidavits and other materials were not presented in support of his Cross-Motion for Summary Disposition and Opposition to the FRB's Motion for Summary Disposition. Under the Board's rules, motions and oppositions for summary disposition "must be supported by documentary evidence, which may take the form of . . . affidavits and any other evidentiary materials that the moving party contends support his or her position." 12 CFR 263.29. Respondent cannot now complain that he did not have an opportunity to present these materials merely because he did not receive a hearing.[16]

More importantly, none of the materials provided with the Second and Third Notice of Supplemental Authority are relevant to these proceedings. The exhibits to the Second Notice of Supplemental Authority and Exhibits A and C to the Third Notice of Supplemental Authority aim at establishing the subjective intent of the parties to the Withdrawal Agreement.[17] However, as explained above, the parties' subjective intent is not relevant to interpreting an unequivocal agreement.

In Respondent's Third Notice of Supplemental Authority, he further argues that the proffered Superseding Addendum to Agreement for Withdrawal of Charges ("Superseding Addendum") is dispositive evidence because it ostensibly makes its provisions retroactive to the effective date of the Withdrawal Agreement and states "[t]here are no prohibitions or

dence or a hearing were not necessary to decide whether the Withdrawal Agreement was an agreement to enter into pretrial diversion or similar program. For the same reasons, the Board denies Respondent's request for oral argument at this stage of the proceedings.

16 The Board observes that the affidavits contained in the First and Second Notice of Supplemental Authority were only obtained after the ALJ issued his Recommended Decision. The affidavits relate primarily to the negotiation and signing of the Withdrawal Agreement that occurred in 2008 and 2009, however, and there is no reason given for Respondent failing to obtain these affidavits earlier during the proceedings below if he considered them to be relevant.

17 Exhibit A of Respondent's Second Notice of Supplemental Authority and Exhibit C of Respondent's Third Notice of Supplemental Authority are both affidavits by the District Attorney in which he states he has no interest in Respondent entering into a pretrial diversion or similar program. Exhibits B and C of Respondent's Second Notice of Supplemental Authority are affidavits from Respondent's defense attorneys explaining that Respondent did not intend to enter into a pretrial diversion or similar program and that the defense counsel's investigation for the criminal case revealed no wrongdoing by Respondent. Exhibit A in Respondent's Third Notice of Supplemental Authority is the Superseding Addendum to Agreement for Withdrawal of Charges, discussed below. Exhibits B and D in the Third Notice of Supplemental Authority do not relate to the issues of this case. Exhibit C is a Pennsylvania Supreme Court opinion concerning grand jury secrecy violations which mentions in passing that the District Attorney had entered a nolle prosequi in connection with the perjury charges against Respondent. Exhibit D in Respondent's Third Notice of Supplemental Authority is a report by a special prosecutor which described flaws the grand jury proceedings but ultimately recommended investigation of the grand jury proceedings be abandoned.

restrictions placed on Mr. DeNaples, nor is any action by him required." The Board notes, however, that the Superseding Addendum does not directly rescind or modify the original Withdrawal Agreement or any of its provisions. Because where specific contract provisions conflict with more general ones, the specific provisions control, *see* Southwestern Elec. Coop., Inc. v. FERC, 347 F.3d 975, 982 (D.C. Cir. 2003), the Board interprets the quoted sentence as simply stating that on the date the Superseding Addendum was executed, no prohibitions or restrictions remained on Respondent.[18] *See also* Lesko v. Frankford Hospital, 11 A.3d 917, 923 (Pa. 2011). Thus, the Superseding Addendum is irrelevant to the issue of whether Respondent agreed to enter into a pretrial diversion or similar program.

The Board also denies Respondent's motions for immediate dismissal. These motions, filed after the Board notified parties that the record of these proceedings was complete, related to a state court order expunging the criminal records pertaining to the withdrawn criminal charges against Respondent. The Board has considered these motions and denies them for the reasons discussed below.

Respondent's motions are based on orders he obtained from the Court of Common Pleas of Dauphin County, Pennsylvania. As noted above, on May 18, 2011 that court issued an Expungement Order expunging the criminal records pertaining to the withdrawn criminal charges against Respondent. That order was clarified on September 14, 2011, in the Clarification Order, which explained that pursuant to the Expungement Order, Respondent's arrest record had been expunged "such that no one, including law enforcement, state licensing authorities, or other governmental officials, is permitted access to the record even by court order under Pennsylvania law." The Clarification Order stated any information nonetheless maintained pursuant to Pennsylvania law should be considered residual in nature and not as a record of the proceeding. Finally, the Clarification Order asserted that "encompassed within the Expungement Order was the Agreement for Withdrawal of Charges ('Withdrawal Agreement') . . . . Since it has been completely expunged, the Withdrawal Agreement is of no force or effect."

Respondent contends that because of the Expungement Order, as explained by the Clarification Order, the Board may no longer enforce section 19 against him. In support, he cites language in the FDIC Policy Statement which states a section 19 application for consent is not required for an individual who has had a criminal conviction expunged. FDIC Policy Statement, section B(2) ("A conviction which has been completely expunged is not considered a conviction of record and will not require an application [under section 19].").

The Board rejects this argument. In the first place, as noted above, the Board is not bound by the FDIC Policy Statement. Under section 19, the Board, not the FDIC, must consent to an individual continuing as an institution-affiliated party of a bank holding company. 12 U.S.C.§ 1829(d). The Board has not adopted the FDIC Policy Statement, and the Board's lack of a formal policy of its own does not entitle Respondent to rely instead on the FDIC Policy Statement.[19]

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[18] Even if Respondent had presented a document purporting, in 2011, to rescind the Withdrawal Agreement executed in 2009, the Board does not believe such a document would affect the outcome here. At the time Board Enforcement Counsel initiated this action and the ALJ issued his recommended decision, Respondent was in violation of section 19 because he had entered into pretrial diversion or similar program and did not have the Board's authorization to remain as an institution-affiliated party of First National or Urban Financial. A later rescission of the pretrial diversion agreement would not change that history.

[19] Even if the FDIC's legal interpretation of section 19 could have some preclusive effect on the Board, the section of the Policy Statement that relates to expungement is not a legal interpretation, since the statutory provision never uses the term "expungement" or refers to the concept. The FDIC's position in this regard is therefore purely one of its own policy, which the Board need not follow. The parties have also disputed whether or

In the second place, the FDIC Policy Statement itself does not address the question presented here, which is whether an individual's agreement to enter into a pretrial diversion or similar program is negated, for purposes of section 19, by the later expungement of the underlying criminal charge. The FDIC Policy Statement, like section 19 itself, treats convictions and pretrial diversions separately. *See* 12 U.S.C. §1829(a)(1)(A) (requiring prior agency approval for "any person who has been convicted of any criminal offense involving dishonesty . . . or has agreed to enter into a pretrial diversion or similar program . . . " (emphasis added); FDIC Policy Statement at B(1) (discussing, in connection with whether an application under section 19 is required, convictions and the effect of complete expungement thereof), B(2) (discussing pretrial diversion programs without mention of expungement). Thus, nothing in the FDIC Policy Statement suggests that an application under section 19 would not be required by the FDIC if an individual who had agreed to enter into a pretrial diversion or similar program had later had his or her underlying criminal charge expunged.

The plain language of section 19 provides that prior Board approval is required of "any person who has . . . agreed to enter into a pretrial diversion or similar program." As the Supreme Court determined in a similar context in holding that an expunged state criminal conviction could continue to be a predicate offense for federal firearms prohibitions, "So far as the face of the [federal] statute is concerned, . . . expunction under state law does not alter the historical fact of the conviction . . . ." Dickerson v. New Banner Institute, Inc., 460 U.S. 103, 115 (1983).[20] Likewise, a subsequent expungement of a criminal charge does not alter the historical fact that Respondent agreed to the Withdrawal Agreement, i.e. that Respondent "has agreed to enter into a pretrial diversion or similar program." *See*12 U.S.C. § 1829(a)(1)(A) (emphasis added).

There are important reasons why expungement of a criminal charge should not affect the consequences of a respondent's agreement to enter into a pretrial diversion or similar program. Pretrial diversion is a method to avoid a full criminal prosecution by agreeing to explicit conditions; in many states, expungement of the criminal record is the automatic or at least the expected conclusion of this process once the program's conditions have been fulfilled. *See* Pretrial Justice Institute, Pretrial Diversion and the Law: A Sampling of Four Decades of Appellate Court Rulings, V-2-6 (2006) available at www.napsa.org/publications/ptdivcaselaw.pdf. Respondent's interpretation would mean that at the point where the individual's involvement in the pretrial diversion program concludes, its existence would in effect be nullified for purposes of section 19; it would be as though the individual had never "agree[d] to enter into" the program at all. This appears inconsistent with the clearly-expressed intent of Congress, which was to require the FDIC or the Board, as appropriate, to pass on the fitness of any individual who has agreed to enter into such a program to participate in the affairs of federally-regulated financial institutions. While the existence of an expungement order may be relevant in evaluating an individual when that individual applies for consent under section 19, it does not, as Respondent argues, eliminate the prior approval requirement clearly stated in that section. In addition, some states do not permit expungement even upon successful conclusion of a pretrial diversion program. Id. It would be anomalous for a federal agency to require a prior application from an individual who had entered into a pretrial diversion program in a non-expungement state, but to permit, without review, the involvement in banking of an individual whose state permits

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not Respondent's expungement is "complete" as used in the recent amendments to the FDIC Policy Statement. *See* 76 *Federal Register*28033. Because the Board is not following the FDIC Policy Statement, the Board need not resolve this issue.

[20] Subsequent Congressional action to overturn this ruling and provide that expunged convictions should generally not be considered in connection with firearms limitations, *see* Pub. L. 99-408, § 101(5), 100 Stat. 449, only underscores the fact that Congress knows how to address the issue of expungement if it so chooses. It has not done so in section 19.

expungement.

Section 19 grants the Board the right, and the obligation, to scrutinize individuals who have entered into a pretrial diversion or similar program before permitting their continued involvement in banking. Absent clear statutory language indicating otherwise, the Board does not believe Congress intended to make this right dependent on a given state's policy regarding expungement and will not interpret section 19 to apply in such a non-uniform manner. *See* Holyfield, 490 U.S. at 43 ("federal statutes are generally intended to have uniform nationwide application"). Thus, despite the recent Expungement Order and Clarification Order, Respondent remains in violation of section 19 for the simple reason that in April 2009 he signed the Withdrawal Agreement, thereby entering into a pretrial diversion or similar program as those terms are defined in section 19, and he has not sought or obtained Board approval for his continued activities as an institution-affiliated party of First National or Urban Financial.

Conclusion

For these reasons, the Board orders the issuance of the attached Order to Cease and Desist.

By Order of the Board of Governors, this 10th day of April, 2012.

Jennifer J. Johnson
Secretary of the Board

In the Matter of Louis A. DeNaples, An Institution-Affiliated Party of First National Community Bancorp, Dunmore, Pennsylvania, and Urban Financial Group, Inc., Bridgeport, Connecticut

FRB Docket No. 09-191-B-I

Order to Cease and Desist

WHEREAS, pursuant to section 8(b) of the Federal Deposit Insurance Act, as amended, (the "FDI Act") (12 U.S.C. § 1818(b)), the Board of Governors of the Federal Reserve System (the "Board") is of the opinion, for the reasons set forth in the accompanying Final Decision, that a final Order to Cease and Desist should issue against Louis A. DeNaples ("DeNaples"), an institution-affiliated party, as defined in section 3(u) of the FDI Act (12 U.S.C. § 1813(u)), of First National Community Bancorp, Dunmore, Pennsylvania, a registered bank holding company ("First National"), and Urban Financial Group, Inc., Bridgeport, Connecticut, a registered bank holding company ("Urban Financial").

NOW, THEREFORE, IT IS HEREBY ORDERED, pursuant to section 8(b) of the FDI Act, 12 U.S.C. § 1818(b), that:

1. DeNaples shall not violate section 19 of the FDI Act, 12 U.S.C. § 1829.
2. Upon the effective date of this Order, DeNaples shall unconditionally resign as a director of First National.
3. Within 30 days of the effective date of this Order, DeNaples shall submit an acceptable written plan to divest his controlling interests in First National and Urban Financial. An acceptable divestiture plan shall, at a minimum, including the following:
    a. Statements setting forth the number of voting shares and any other equity interests of:
        i. First National; and
        ii. Urban Financial,

        that are owned or controlled by DeNaples, as of the date of this Order;

b. Statements setting forth the number of voting shares and any other equity interests of:
   i. First National; and
   ii. Urban Financial,
   that are owned or controlled by any person acting in concert with DeNaples, within the meaning of 12 CFR 225.41(a)(2) of the Board's Regulation Y, as of the date of this Order.
c. Statements disclosing the number of voting shares and any other equity interests of:
   i. First National; and
   ii. Urban Financial,
   that are owned or controlled by any member of DeNaples' immediate family, within the meaning of 12 CFR 225.41(a)(3) of the Board's Regulation Y, as of the date of this Order.
d. A schedule for the divestiture of First National voting shares owned or controlled by DeNaples such that after the divestiture DeNaples would not own or control personally or acting in concert with other persons shares that would require prior notice under 12 CFR 225.41(c), as if the shares owned or controlled personally or acting in concert with other persons had been acquired after the divestiture.
e. A schedule for the divestiture of Urban Financial voting shares owned or controlled by DeNaples such that after the divestiture DeNaples would not own or control personally, or acting in concert with other persons, shares that would require prior notice under 12 CFR 225.41(c), as if the shares owned or controlled personally or acting in concert with other persons had been acquired after the divestiture.
f. The plan shall include a schedule such that the divestitures shall be completed within 180 days after the effective date of the Order.
g. The plan shall provide that the divestiture of the shares shall be:
   i. to third parties unrelated to DeNaples in arms-length transactions; or
   ii. if to any person who has previously acted in concert with DeNaples with respect to First National or Urban Financial, or would be considered to be acting in concert with DeNaples at the time of the divestiture (including persons presumed to be acting in concert with DeNaples as set forth in 12 CFR 225.41(d)), the plan shall include adequate assurances (through a trust or otherwise) such that DeNaples would not have the ability to act in concert with, or exercise any control or controlling influence over the shares of First National or Urban Financial, respectively. The mechanism and the individuals or entities who control the shares in any manner through a trust or otherwise shall be subject to the approval of the Board.
h. The plan shall further provide for disclosure of any financial or personal relationships between DeNaples, and his related interests (as defined in 12 CFR 215.3(n), on the one hand, and each acquirer and his or her related interests, on the other hand, of any shares of First National or Urban Financial divested pursuant to the plan.

4. Respondent shall fully comply with all of the terms of any acceptable divestiture plan submitted.
5. Respondent shall submit his written divestiture plan and other correspondence with respect to this Order to:
   a. Richard M. Ashton
   Deputy General Counsel
   Board of Governors of the Federal Reserve System
   20th & C Sts., NW
   Washington, DC 20551
   b. Thomas Baxter

General Counsel
Federal Reserve Bank of New York
33 Liberty Street
New York, New York 10045
(with respect to Urban Financial)

c. Jeanne Rentezelas
Federal Reserve Bank of Philadelphia
10 Independence Mall
Philadelphia, PA 19106-1574
(with respect to First National)

6. Any violation of this Order shall subject Respondent to appropriate penalties under 12 U.S.C. § 1818(i).
7. The Board delegates to the Board's General Counsel (or his delegee), with the concurrence of the Director of the Division of Banking Supervision and Regulation (or his delegee), the authority to determine the acceptability of any divestiture plan submitted by Respondent pursuant to this Order, to accept modifications to any previously accepted divestiture plan, and to grant extensions of time.
8. This Order, and each and every provision hereof, is and shall remain fully effective and enforceable until expressly stayed, modified, terminated or suspended in writing by the Board.

This Order is effective 30 days after service on the Respondent.

By Order of the Board of Governors, this 10th day of April, 2012.

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM

Jennifer J. Johnson
Secretary of the Board

Federal Reserve
BULLETIN
December 2012
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Legal Developments: Third Quarter, 2012

Orders Issued Under Bank Holding Company Act

Order Issued Under Section 3 of the Bank Holding Company Act

Old National Bancorp
Evansville, Indiana

Order Approving Acquisition of a Bank Holding Company
FRB Order No. 2012–9 (August 30, 2012)

Old National Bancorp ("ONB"), Evansville, Indiana, has requested the Board's approval under section 3 of the Bank Holding Company Act ("BHC Act") [1] to acquire Indiana Community Bancorp ("ICB") and thereby indirectly acquire its subsidiary bank, Indiana Bank and Trust Company ("IBTC"), both of Columbus, Indiana. Immediately following the proposed acquisition, IBTC would be merged into ONB's subsidiary bank, Old National Bank ("ONBK"), Evansville.[2]

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published (77 *Federal Register* 33460 (2012)). The time for filing comments has expired, and the Board has considered the application and all comments received in light of the factors set forth in section 3 of the BHC Act.

ONB, with total consolidated assets of approximately $8.6 billion, is the 113th largest insured depository organization in the United States, controlling approximately $6.7 billion in deposits.[3] ONBK, ONB's only insured subsidiary depository institution, operates in Illinois, Indiana, Kentucky, and Ohio.[4] ONBK is the fourth largest depository institution in Indiana, controlling deposits of approximately $4.6 billion, which represent approximately 4.7 percent of the total amount of deposits of insured depository institutions in that state.[5]

ICB, with total consolidated assets of approximately $968 million, controls IBTC, which operates only in Indiana. IBTC is the 25th largest insured depository institution in Indiana, controlling approximately $860 million in deposits. On consummation of this proposal, ONB would remain the fourth largest insured depository organization in Indiana, controlling deposits of approximately $5.6 billion, which represent approximately 5.6 percent of the total amount of deposits of insured depository institutions in the state.

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1 12 U.S.C. §1842.

2 The merger of IBTC into ONBK is subject to approval by the Office of the Comptroller of the Currency under the Bank Merger Act.

3 National deposit, asset, and ranking data are as of March 31, 2012, and are updated to reflect mergers through that date. In this context, insured depository institutions include commercial banks, savings associations, and savings banks.

4 ONB owns all of the capital stock of ONBK.

5 State deposit, asset, and ranking data are as of June 30, 2011.

Competitive Considerations

Section 3 of the BHC Act prohibits the Board from approving a proposal that would result in a monopoly or would be in furtherance of any attempt to monopolize the business of banking in any relevant banking market. The BHC Act also prohibits the Board from approving a proposal that would substantially lessen competition in any relevant banking market unless the anticompetitive effects of the proposal are clearly outweighed in the public interest by the probable effect of the proposal in meeting the convenience and needs of the community to be served.[6]

ONB and ICB have subsidiary depository institutions that compete directly in the Louisville, Kentucky banking market and in the Indiana banking markets of Indianapolis and Seymour.[7] The Board has reviewed the competitive effects of the proposal in these 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 shares of total deposits in depository institutions in the markets ("market deposits") controlled by ONB and ICB,[8] 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 Merger Guidelines ("DOJ Guidelines"),[9] and other characteristics of the markets.

A. Banking Markets within Established Guidelines

Consummation of the proposal would be consistent with Board precedent and within the DOJ Guidelines in the Indianapolis[10] and Louisville[11] banking markets. On consummation of the proposal, both markets would remain moderately concentrated, as measured by the HHI, and a number of competitors would remain in each banking market.[12]

6 12 U.S.C. § 1842(c)(1).

7 The Louisville banking market encompasses Salem, Indiana, where ITBC has a branch. ITBC has operations only in Indiana.

8 Deposit and market share data are as of June 30, 2011, updated to reflect mergers through June 4, 2012, 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).

9 Under the DOJ 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 issued revised Horizontal Merger Guidelines in 2010, the DOJ has confirmed that its guidelines for bank mergers or acquisitions, which were issued in 1995, were not changed. Press Release, Department of Justice (August 19, 2010), available at www.justice.gov/opa/pr/2010/August/10-at-938.html.

10 The Indianapolis banking market is defined as Boone, Hamilton, Hancock, Hendricks, Johnson, Marion, Morgan, and Shelby Counties, Indiana; and Green Township in Madison County, Indiana.

11 The Louisville banking market is defined as Bullitt, Henry, Jefferson, Meade, Nelson, Oldham, Shelby, and Spencer Counties, Kentucky; the Bedford census county division in Trimble County, Kentucky; the Fort Knox and West Point census county divisions and the cities of Vine Grove and Radcliff in Hardin County, Kentucky; the city of Irvington in Breckinridge County, Kentucky; Clark, Floyd, Harrison, and Washington Counties, Indiana; and Crawford County, Indiana (excluding Patoka Township). Although the Louisville market is located primarily in Kentucky, it also includes Salem, Indiana, where IBTC operates a branch and competes directly with ONBK.

12 In the Indianapolis banking market, ONBK would remain the tenth largest depository institution, controlling deposits of $738.3 million, representing approximately 2.4 percent of market deposits. The HHI would increase by 1 point to 1409, and 42 other competitors would remain in the market. In the Louisville banking market,

B. Banking Market Exceeding Established Guidelines

ONB and ICB compete directly in the Seymour banking market.[13] This market warrants a detailed review of the competitive effects of the proposal because the concentration level on consummation would exceed the threshold levels in the DOJ Guidelines.

ONBK is the seventh largest of ten insured depository institutions in the Seymour banking market, controlling deposits of approximately $29.8 million, which represent approximately 4 percent of market deposits. IBTC is the second largest insured depository institution in the market, controlling deposits of approximately $190.6 million, which represent approximately 25.5 percent of market deposits. On consummation, ONB would become the largest insured depository organization in the market. The HHI would increase by 203 points to 2107, and the pro forma market share of the combined entity would be approximately 29.5 percent.

After consummation of the proposal, eight other commercial bank competitors would remain, some with a significant presence in the market. The second largest bank competitor in the market would control 27.6 percent of market deposits, and four other bank competitors in the market each would control between 5 percent and 17 percent of market deposits.

In addition, one active community credit union in the Seymour banking market, Centra Credit Union, offers a wide range of consumer products, operates street-level branches, and has broad membership criteria that include most of the market's residents.[14] Accordingly, the Board has concluded that the activities of this credit union exert a competitive influence that mitigates, in part, the potential effects of the proposal.

Centra Credit Union controls approximately $18.3 million in deposits in the market that, on a 50 percent weighted basis, represents approximately 2.4 percent of market deposits. After inclusion of these deposits, ONB would control approximately 28.8 percent of market deposits, and the HHI would increase by 193 points to 2013, an increase that is within DOJ Guidelines.

C. View of Other Agencies and Conclusion on Competitive Considerations

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

Based on all the facts of record, the Board has concluded that consummation of the proposal would not have a significantly adverse effect on competition or on the concentration of resources in any relevant banking market. Accordingly, based on all the facts of record, the Board has determined that competitive considerations are consistent with approval.

ONBK would become the 24th largest depository institution, controlling deposits of approximately $136.8 million, representing less than 1 percent of market deposits. The HHI would remain unchanged at 972, and 44 other competitors would remain in the market.

[13] The Seymour banking market is defined as Jackson County, Indiana.

[14] The Board previously has considered competition from certain active credit unions as a mitigating factor. *See, e.g., The PNC Financial Services Group, Inc.*, 93 *Federal Reserve Bulletin* C65 (2007); *Regions Financial Corporation*, 93 *Federal Reserve Bulletin* C16 (2007); *Wachovia Corporation*, 92 *Federal Reserve Bulletin* C183 (2006); and *F.N.B. Corporation*, 90 *Federal Reserve Bulletin* 481 (2004).

Other Section 3(c) Considerations

Section 3(c) of the BHC Act requires the Board to take into consideration a number of other factors in acting on bank acquisition applications. Those factors include the financial and managerial resources (including consideration of the competence, experience, and integrity of the officers, directors, and principal shareholders) and future prospects of the company and banks concerned; the effectiveness of the company in combatting money laundering; the convenience and needs of the community to be served; and the extent to which the proposal would result in greater or more concentrated risks to the stability of the United States banking or financial system. The Board has considered all these factors and, as described below, has determined that they are consistent with approval of the application. The review was conducted in light of all the facts of record, including supervisory and examination information from various U.S. banking supervisors of the institutions involved, publicly reported and other financial information, and information provided by ONB.

A. Financial, Managerial, and Other Supervisory Considerations

In evaluating financial factors in expansionary proposals by banking organizations, the Board reviews the financial condition of the organizations involved on both a parent-only and consolidated basis, as well as the financial condition of the subsidiary depository institutions and the organizations' significant nonbanking operations. In this evaluation, the Board considers a variety of information, including capital adequacy, asset quality, and earnings performance. The Board evaluates the financial condition of the combined organization, including its capital position, asset quality, 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 costs 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.

The Board has considered the financial factors of the proposal. ONB and ONBK are well capitalized and would remain so on consummation of the proposed acquisition. The proposed transaction is a bank holding company merger, structured as a share exchange. Asset quality and earnings prospects are consistent with approval, and ONB appears to have adequate resources to absorb the costs of the proposal and the proposed integration of the institutions' operations. Based on its review of the record, the Board finds that ONB has sufficient financial resources to effect the proposal.

The Board also has considered the managerial resources of the organizations involved and of the proposed combined organization. The Board has reviewed the examination records of ONB, ONBK, ICB, and IBTC, including assessments of their management, risk-management systems, and operations. In addition, the Board has considered its supervisory experiences and those of other relevant bank supervisory agencies with the organizations and their records of compliance with applicable banking and anti-money-laundering laws. The Board also has considered ONB's plans for implementing the proposal, including the proposed management after consummation of the proposal. In addition, the Board has considered the future prospects of the organizations involved in the proposal in light of the financial and managerial resources and the proposed business plan.

ONB and ONBK each are considered to be well managed. ONB would implement its risk-management policies, procedures, and controls at the combined organization. In addition, ONB's management has the experience and resources to ensure that the combined organization operates in a safe and sound manner. Furthermore, ONB has demonstrated a

record of successfully integrating other banking organizations into its operations and risk-management systems after acquisitions.

On June 4, 2012, ONBK entered into a Stipulation and Consent to the Issuance of a Consent Order (the "Consent Order") with the Office of the Comptroller of the Currency ("OCC") relating to deficiencies in ONBK's overall program for Bank Secrecy Act/anti-money-laundering ("BSA/AML") compliance. The Consent Order requires ONBK to, among other things, take the following actions: develop and implement a comprehensive BSA action plan, including an effective institution-wide BSA risk-assessment program that accurately identifies BSA/AML risks; ensure that ONBK management reviews, updates, and implements its risk-based processes to obtain and analyze appropriate customer due diligence information to monitor for and investigate suspicious activity; ensure adherence to a written program of internal controls for appropriate identification, analysis, and monitoring of transactions with greater than normal risk; maintain an effective BSA independent testing function; ensure and maintain sufficient personnel with requisite expertise and skills; and ensure adherence to a comprehensive BSA/AML training program.

ONBK's BSA/AML program deficiencies were identified by the OCC in early 2011. Since that time, ONBK has devoted significant time and resources toward improving its BSA/AML program and has made substantial progress towards fully addressing program weaknesses. Major advancements to correct the deficiencies include the following steps: the purchase and installation of a new transaction-monitoring system; an enhanced BSA Risk Assessment for all ONBK activities and products; strengthening of ONBK's core BSA/AML management teams by hiring employees experienced in those areas; enhancements to customer due diligence processes; and enhancement and supplementation of the BSA/AML expertise, staffing, and methodologies within ONBK's Internal Audit function. ONBK expects to complete its corrective actions in the third quarter of 2012.

The Board has consulted with the OCC, the responsible federal banking agency for ONBK, concerning this proposal. The OCC has confirmed that ONBK has taken corrective actions to address the matters described in the Consent Order. The OCC also has confirmed that the weaknesses identified related to policies and procedures and that there was no evidence of money laundering or other unlawful activities at ONBK. The OCC supports the proposal and does not believe that the acquisition will detract the bank from fully addressing its remaining BSA weaknesses in a timely manner. Furthermore, ONB has committed to the Board that it will fully address and resolve all BSA/AML weaknesses and violations identified in the Consent Order and that until such time as they have been fully addressed, ONB will provide quarterly progress reports to the Federal Reserve Bank of St. Louis.

Based on all the facts of record, the Board has concluded that considerations relating to the financial and managerial resources and future prospects of the organizations involved are consistent with approval.

B. Convenience and Needs Considerations

In acting on a proposal under section 3 of the BHC Act, the Board must consider the effects of the proposal on the convenience and needs of the community to be served and take into account the records of the relevant depository institutions under the Community Reinvestment Act ("CRA").[15] The CRA requires federal financial supervisory agencies to encourage insured depository institutions to help meet the credit needs of the local commu-

[15] 12 U.S.C. § 1842(c)(2); 12 U.S.C. § 2901 *et seq*.

nities in which they operate, consistent with their safe and sound operation,[16] 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 neighborhoods, in evaluating bank expansionary proposals.[17]

The Board has considered the convenience and needs factor and the CRA performance records of ONBK and IBTC in light of all the facts of record. As provided in the CRA, the Board evaluates the record of performance of an institution in light of examinations by the appropriate federal supervisors of the CRA performance records of the relevant institutions.[18] ONBK received a "satisfactory" rating at its most recent CRA performance evaluation by the OCC, as of June 30, 2008, and IBTC received a "satisfactory" rating at its most recent CRA performance evaluation by the Federal Reserve Bank of St. Louis, as of August 4, 2008.

Based on a review of the entire record, the Board has concluded that considerations relating to convenience and needs considerations and the CRA performance records of the relevant insured depository institutions are consistent with approval.

C. Financial Stability

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

Based on all the facts of record, including those described above, the Board has determined that all the factors it must consider under section 3(c) of the BHC Act 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 BHC Act and other applicable statutes. The Board's approval is specifically conditioned on compliance by ONB with all the conditions imposed in this order and the commitments made to the Board in connection with the application, including receipt of all required regulatory approvals. For purposes of this action, the conditions and commitments are deemed to be conditions imposed in writing by the Board in connection with its findings and decision herein and, as such, may be enforced in proceedings under applicable law.

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

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[16] 12 U.S.C. § 2901(b).

[17] 12 U.S.C. § 2903.

[18] The Interagency Questions and Answers Regarding Community Reinvestment provide that 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. 75 *Federal Register* 11642 at 11665 (2010).

By order of the Board of Governors, effective August 30, 2012.

Voting for this action: Chairman Bernanke, Vice Chair Yellen, and Governors Duke, Tarullo, Raskin, and Stein. Absent and not voting: Governor Powell.

Margaret McCloskey Shanks
Associate Secretary of the Board

Order Issued Under Section 4 of the Bank Holding Company Act

BB&T Corporation

Winston-Salem, North Carolina

Order Approving the Acquisition of a Savings Association
FRB Order No. 2012–8 (July 31, 2012)

BB&T Corporation ("BB&T"), 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 Act and section 225.24 of the Board's Regulation Y [1] to acquire all the voting shares of BankAtlantic, a subsidiary federal savings association of BankAtlantic Bancorp, Inc. ("BA Bancorp"), a savings and loan holding company, both of Fort Lauderdale, Florida.[2]

Notice of the proposal, affording interested persons an opportunity to submit comments, has been published in the *Federal Register* (77 *Federal Register* 1072 (January 9, 2012)) and the time for filing comments has expired. The Board has considered all comments received on the proposal.[3]

BB&T, with total consolidated assets of approximately $174.8 billion, is the 18th largest depository organization in the United States, as measured by asset size.[4] BB&T is the eighth largest depository organization in the United States, as measured by deposits, and controls deposits of approximately $142.4 billion, which represent approximately 1.58 percent of the total amount of deposits of insured depository institutions in the United States. BB&T controls two insured depository institutions, Branch Bank and BB&T Financial,

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1 12 U.S.C. §§ 1843(c)(8) and (j); 12 CFR 225.24.

2 Immediately following the proposed acquisition, BankAtlantic would be merged into BB&T's lead subsidiary bank, Branch Banking and Trust Company ("Branch Bank") (total assets of $168.9 billion), also of Winston-Salem. That merger proposal is subject to approval by the Federal Deposit Insurance Corporation ("FDIC") under the Bank Merger Act and by the North Carolina Banking Commission ("State") under state law. The State approved the merger on March 14, 2012, and the FDIC approved the merger on July 16, 2012, conditioned on the Federal Reserve's approval of this notice.

3 During the application process, BB&T restructured its original proposal, which would have resulted in BA Bancorp retaining its obligation to pay its Trust Preferred Securities ("TPS") holders. TPS holders objected to this proposal, contending that (a) the manner in which the proposal was structured was illegal; (b) the proposed transaction violated BA Bancorp's obligations to its creditors and exposed BA Bancorp, BankAtlantic, and BB&T to litigation; (c) the proposed transaction would be inconsistent with sound prudential regulation; and (d) the proposed compensation structure would permit insiders to exploit the banking system and evade prudential regulation. The first three of these comments uniquely related to the original proposal and are no longer relevant in light of the restructured proposal. The comment on compensation as well as objections (b) and (c) were also formally withdrawn after the restructured proposal was submitted.

4 National deposit, asset, and ranking data are as of December 31, 2011, and include mergers through that date. In this context, insured depository institutions include commercial banks, savings associations, and savings banks.

F.S.B. ("FSB"), Columbus, Georgia.[5] Branch Bank operates branches in Alabama, Florida, Georgia, Indiana, Kentucky, Maryland, North Carolina, South Carolina, Tennessee, Texas, Virginia, West Virginia, and the District of Columbia. In Florida, Branch Bank is the fifth largest depository institution, controlling deposits of approximately $12.6 billion.[6]

BA Bancorp, with total consolidated assets of $3.8 billion, controls BankAtlantic, which operates only in Florida.[7] BankAtlantic is the 17th largest depository institution in Florida, controlling deposits of approximately $3.5 billion.

On consummation of the proposal, BB&T would become the 17th largest depository organization in the United States, with total consolidated assets of approximately $178.6 billion. BB&T would control deposits of approximately $145.9 billion, which represent 1.63 percent of the total amount of deposits of insured depository institutions in the United States.

Interstate and Deposit Cap Analyses

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Pub. L. No. 111-203, 124 Stat. 1601 (2010) ("Dodd-Frank Act"), amended section 4 of the BHC Act to prohibit the Board from approving an application by a bank holding company to acquire an insured depository institution, including a savings association, if the home state of the insured depository institution is a state other than the home state of the bank holding company, 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 ("nationwide deposit cap").[8] The nationwide deposit cap was intended to help guard against undue concentrations of economic power.[9] For purposes of the BHC Act, the home state of BB&T is North Carolina, and the home state of BankAtlantic is Florida.[10]

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 $8.9 trillion.[11] On consummation of the proposed transaction, BB&T would control approximately 1.63 percent of the total amount of deposits in insured depository institutions in the

[5] Branch Bank is BB&T's largest subsidiary depository institution, as measured by both assets and deposits. FSB, a federal savings bank, offers, primarily through the Internet, credit card and merchant services, consumer and commercial outdoor equipment loans, marine and recreational vehicle loans, retail auto loans, and prepaid card products.

[6] State deposit, asset, and ranking data are as of June 30, 2011.

[7] BA Bancorp, in turn, is controlled by BFC Financial Corporation, Inc., a publicly traded savings and loan holding company.

[8] Dodd-Frank Act § 623(b), codified at 12 U.S.C. § 1843(i)(8). For a detailed discussion of the nationwide deposit cap, *see Bank of America Corporation/LaSalle*, (order dated Sept. 14, 2007), 93 *Federal Reserve Bulletin* C109, C109-C110 (3rd Quar. 2007); *Bank of America Corporation/Fleet*, (order dated Mar. 8, 2004), 90 *Federal Reserve Bulletin* 217, 219-220 (Spring 2004) ("Fleet Order").

[9] *See* Fleet Order at 219.

[10] 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 federal savings association, the home state is the state in which the home office of the savings association is located. 12 U.S.C. § 1841(o)(4)(E).

[11] Deposit data are calculated based on reports filed by insured depository institutions and are as of December 31, 2011. Each bank insured by the 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 (*l*), on the institution's Consolidated Report of Condition and Income. Each insured savings association similarly must report its total deposits on the institution's Thrift Financial Report. 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.

United States. Accordingly, in light of all the facts of record, the Board is not prohibited from approving the proposal under section 4(j) of the BHC Act.

Factors Governing Board Review of the Transaction

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.[12] The Board requires that savings associations acquired by bank holding companies or financial holding companies conform their direct and indirect activities to those permissible for bank holding companies under section 4(c)(8) of the Act.[13] BB&T has committed that all the activities of BankAtlantic will conform to those activities that are permissible under section 4 of the BHC Act and Regulation Y within the act's two-year conformance period after the acquisition.

Section 4(j)(2)(A) of the BHC Act requires the Board to consider whether the proposed acquisition of BankAtlantic "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."[14] As part of its evaluation of those 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, and the public benefits of the proposal.[15] In acting on a notice to acquire a savings association, the Board also reviews the records of performance of the relevant insured depository institutions under the Community Reinvestment Act ("CRA").[16]

Competitive Considerations

As part of the Board's consideration of the factors under section 4 of the BHC Act, the Board has considered the competitive effects of BB&T's acquisition of BankAtlantic in light of all the facts of record. BB&T and BankAtlantic compete directly in three banking markets, all in Florida: Fort Pierce Metropolitan Statistical Area ("Fort Pierce"), Miami-Fort Lauderdale-Pompano Metropolitan Statistical Area ("Miami-Fort Lauderdale-Pompano"), and West Palm Beach Metropolitan Statistical Area ("West Palm Beach").[17] The Board has reviewed the competitive effects of the proposal in each of these banking markets in light of all the facts of record. In particular, the Board has considered the number of

[12] 12 CFR 225.28(b)(4)(ii).

[13] A savings association operated by a bank holding company may engage only in activities that are permissible for bank holding companies under section 4(c)(8) of the BHC Act. 12 CFR 225.28(b)(4)(ii).

[14] 12 U.S.C. §1843(j)(2)(A). Section 604(e) of the Dodd-Frank Act added "risk to the stability of the United States banking or financial system" to the list of possible adverse effects.

[15] *See* 12 CFR 225.26; *see, e.g., Bank of America Corporation/Countrywide*, (order dated June 5, 2008), 94 *Federal Reserve Bulletin* C81 (2nd Quar. 2008); *Wachovia Corporation,* (order dated Sept. 29, 2006), 92 *Federal Reserve Bulletin* C138 (3rd Quar. 2006); *BancOne Corporation*, (order dated May 14, 1997), 83 *Federal Reserve Bulletin* 602 (1997).

[16] 12 U.S.C. § 2901 *et seq*. In assessing the merger proposal of BankAtlantic into Branch Bank under the Bank Merger Act, the FDIC is required to take into consideration the same factors that are reviewed by the Board under the BHC Act, including the effects of the acquisition on financial stability and on the convenience and needs of the community to be served. 12 U.S.C. § 1828(c)(5).

[17] Fort Pierce is defined as St. Lucie County and Martin County (excluding the towns of Indiantown and Hobe Sound). Miami-Fort Lauderdale-Pompano is defined as Broward and Miami-Dade Counties. West Palm Beach is defined as Palm Beach County east of Loxahatchee and the towns of Indiantown and Hobe Sound in Martin County.

competitors that would remain in the markets, the relative shares of total deposits in depository institutions in the markets ("market deposits") controlled by BB&T and BankAtlantic, the concentration levels of market deposits as measured by the Herfindahl-Hirschman Index ("HHI") under the Department of Justice Merger Guidelines ("DOJ Guidelines"),[18] and other characteristics of the markets.

Consummation of the proposal would be consistent with Board precedent and within the thresholds in the DOJ Guidelines in each of the three banking markets. On consummation of the proposal, one market would remain unconcentrated, and two markets would remain moderately concentrated, all as measured by the HHI. The changes in the HHI's measure of concentration would be minimal, and numerous competitors would remain in all three banking markets.[19]

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

Based on all the facts of record, the Board concludes that consummation of the proposed transaction would not have a significantly adverse effect on competition or on the concentration of resources in any relevant banking market and is consistent with approval.

Financial and Managerial Resources

The Board has considered the financial and managerial resources of BB&T, its subsidiaries, and BankAtlantic and the effect of the transaction on those resources, in light of confidential reports of examination, other supervisory information from the primary federal supervisor of the organizations involved in the proposal, publicly reported and other financial information, information provided by BB&T and BankAtlantic, and other relevant information. The Board also consulted with the FDIC, the primary federal supervisor of BB&T's lead subsidiary depository institution, Branch Bank, and the Office of the Comptroller of the Currency ("OCC"), the primary federal supervisor of BankAtlantic and FSB.

In evaluating financial resources in expansionary proposals by banking organizations, the Board reviews the financial condition of the organizations involved on both a parent-only and consolidated basis, as well as the financial condition of the subsidiary insured

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[18] Under the DOJ 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 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 DOJ has stated that the higher-than-normal HHI thresholds for screening bank mergers and acquisitions for anticompetitive effects implicitly recognize the competitive effects of limited-purpose and other nondepository financial entities. Although the DOJ and the Federal Trade Commission recently issued revised Horizontal Merger Guidelines, the DOJ has confirmed that its guidelines for bank mergers or acquisitions, which were issued in 1995, were not changed. Press Release, Department of Justice (August 19, 2010), available at www.justice.gov/opa/pr/2010/August/10-at-938.html.

[19] The HHI would decrease in each market as follows: 18 points to 1013 in Fort Pierce, 3 points to 703 in Miami-Fort Lauderdale-Pompano, and 11 points to 1009 in West Palm Beach. Those decreases result from a pre-merger weighting of BankAtlantic'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 resulting pro forma shares of BB&T's market deposits would be as follows: 4.9 percent in Fort Pierce, 4.0 percent in Miami-Fort Lauderdale-Pompano, and 4.5 percent in West Palm Beach.

depository institutions and the organizations' significant nonbanking operations. In this evaluation, the Board considers a variety of information, including capital adequacy, asset quality, and earnings performance. In assessing financial factors, the Board consistently has considered capital adequacy to be especially important. The Board evaluates the financial condition of the combined organization at consummation, 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 costs of the proposal and the proposed integration of the operations of the institutions.

The Board has considered the financial factors of the proposal. BB&T's regulatory capital ratios are well above the minimums required of well-capitalized bank holding companies and would remain so on consummation of the proposal. BB&T's subsidiary depository institutions are well capitalized and would remain so after consummation. BB&T would acquire approximately $2.1 billion in loans and assume approximately $3.3 billion in deposits from BankAtlantic, as well as approximately $285 million in outstanding TPS. The transaction would be funded with available cash on hand, and there are no plans to raise additional capital or issue any debt obligations in connection with the transaction. Asset quality and earnings prospects also are consistent with approval.

The Board also has considered the managerial resources of the organizations involved and of the proposed combined organization. The Board has reviewed the examination records of BB&T, its subsidiary insured depository institutions, and BankAtlantic, including assessments of their management expertise, internal controls, risk management systems, and operations. In addition, the Board has considered its supervisory experiences and those of other relevant financial supervisory agencies with the organizations and the organizations' records of compliance with applicable banking laws and with anti-money-laundering laws. The Board has also considered the comments it received on the proposal.

BB&T and its subsidiary depository institutions are considered to be well managed. BB&T would implement its risk-management policies, procedures, and controls at the combined organization, which are regarded as satisfactory. In addition, BB&T's management has the experience and resources to ensure the successful integration of the two organizations and the safe and sound operation of the combined organization.[20]

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 in the proposal are consistent with approval under section 4 of the BHC Act.

Convenience and Needs Considerations

As noted, the Board reviews the records of performance under the CRA of the relevant insured depository institutions when acting on a notice to acquire any insured depository institution, including a savings association.[21] 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,[22]and requires the appropriate federal financial supervisory agency to take into

[20] Two commenters referenced an SEC lawsuit alleging that the chairman of BA Bancorp had engaged in a pattern of misleading BA Bancorp's investors through selective and untimely disclosures with respect to problem loans. The individuals named in the lawsuit will not be associated with BB&T or BankAtlantic after consummation of the proposed transaction.

[21] 12 U.S.C. § 2901 *et seq*.

[22] 12 U.S.C. § 2901(b).

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.[23]

The Board has considered all the facts of record, including reports of examination of the CRA performance records of BB&T's subsidiary insured depository institutions and of BankAtlantic, data reported by BB&T and BankAtlantic under the CRA and the Home Mortgage Disclosure Act ("HMDA"),[24] other information provided by BB&T, and confidential supervisory information. The Board has also considered the public comments received on the proposal regarding the depository institutions' CRA, fair lending, and HMDA performance.

A. CRA Performance Evaluations

As provided in the CRA, the Board has evaluated the proposal in light of the examinations by the appropriate federal supervisors of the CRA performance records of the insured depository institutions involved in the proposal. 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.[25]

Branch Bank received an overall "Satisfactory" rating at its most recent CRA performance evaluation by the FDIC, as of January 22, 2008. The Public Evaluation ("PE") for that examination gave Branch Bank ratings of "High Satisfactory" for the Lending Test and "Outstanding" for the Investment and Service Tests. Substantive violations of the Equal Credit Opportunity Act and the Fair Housing Act were noted and resulted in Branch Bank's overall CRA rating being lowered from "Outstanding" to "Satisfactory." The Board consulted with the FDIC on BB&T's fair lending record regarding the progress made by Branch Bank's management to address these matters and to correct its fair lending policies and procedures and fee structure to help ensure compliance with the fair lending laws.[26]

FSB is headquartered in Columbus, Georgia, with operations concentrated in the credit card and merchant services division in Wilson, North Carolina.[27] Rather than operate traditional brick and mortar branches, the bank operates on a branchless platform, distributing its products through the Internet, direct mail, and telemarketing calls. FSB's business model includes various business lines and operating subsidiaries that offer a variety of products and services.[28] FSB received a "Satisfactory" rating at its most recent CRA examination conducted by the Office of Thrift Supervision ("OTS), as of January 3, 2011. The bank was rated "Satisfactory" overall, with ratings of "Low Satisfactory" for the

[23] 12 U.S.C. § 2903.

[24] 12 U.S.C. §2801 *et seq*.

[25] *See Interagency Questions and Answers Regarding Community Reinvestment*, 66 *Federal Register* 11,642 at 11,665 (2010).

[26] One commenter requested that the BB&T acquisition be conditionally approved, asserting that a "Satisfactory" rating for a bank as large as BB&T was unacceptable and that the largest retail banks should all have "Outstanding" ratings for CRA performance. This commenter also criticized Branch Bank for its failure to maintain a consistent "Outstanding" CRA rating. The commenter cited the fair lending violations that were reported in the PE for BB&T's 2008 examination, noted above, and BankAtlantic's CRA performance as reasons why a conditional approval would be appropriate.

[27] The bank was chartered on April 1, 2008, when BB&T Bankcards Corporation converted from a special-purpose state bank to an FDIC-insured federal savings bank.

[28] At the time of the CRA evaluation, the business lines and operating subsidiaries that contributed to the thrift's CRA performance were BB&T Bankcards ("Bankcards"), Sheffield Financial ("Sheffield"), and Liberty Mortgage Corporation ("LMC"). Bankcards issued credit card products to consumer, corporate, and small business clients and was the FSB's largest business line. Sheffield, a nationwide specialty installment lender, financed consumer and small business purchases of small-ticket outdoor equipment. LMC offered a variety of

Lending Test, “Outstanding” for the Investment Test, and “High Satisfactory” for the Service Test.[29]

BankAtlantic received a “Needs to Improve” CRA rating at its most recent CRA examination conducted by the OTS, as of May 24, 2010. The OTS examination noted violations of the Federal Trade Commission Act discovered during the thrift’s consumer compliance examination that involved an automated overdraft protection program.

BB&T reported that it has reviewed BankAtlantic’s policies and procedures, monitoring reports, training delivery and frequency, and compliance reports. BB&T has directed its compliance staff to work with both Branch Bank and BankAtlantic employees to ensure that BankAtlantic’s overdraft practices comply with the FDIC’s guidance on overdraft protection programs.[30] BB&T has committed that after consummation of the proposed merger, it will address any deficiencies in BankAtlantic’s CRA performance by implementing BB&T’s existing policies and procedures at the combined organization. Those policies and procedures are considered satisfactory. To that end, BB&T plans to build on BankAtlantic’s existing CRA efforts and programs, including identifying the housing, small business, and community development needs of each assessment area; reviewing community action plans; and interviewing local community-based organization leaders to discuss the needs of the communities.

B. HMDA Analysis

In its evaluation, the Board has considered the records of BB&T and BankAtlantic in complying with fair lending and other consumer protection laws. The Board has reviewed HMDA data reported by Branch Bank and BankAtlantic. A commenter opposed the proposal by alleging, based on 2010 HMDA data reported by Branch Bank and BankAtlantic, that both institutions engaged in discriminatory treatment of minority individuals in their home mortgage lending. The commenter also alleged that Branch Bank and BankAtlantic denied the home mortgage loan applications of minority borrowers more frequently than those of nonminority applicants in certain metropolitan statistical areas (“MSAs”).[31]

The HMDA data indicate that in 2010 Branch Bank somewhat lagged the aggregate in the percentage of applications received from African Americans and Hispanics and from minority census tracts but was consistent with the aggregate with respect to the percentage of applications it received from LMI census tracts and LMI individuals. The percentage of Branch Bank’s loan originations was largely consistent with the aggregate with respect to its loans in LMI census tracts and to LMI individuals, but the bank lagged the aggregate with respect to its loans to African Americans and Hispanics and in minority census tracts.

In the Port St. Lucie MSA, an area cited by the commenter, Branch Bank received and originated very few applications from African Americans and Hispanics in 2010. The Board notes that Branch Bank currently has four branches in the Port St. Lucie MSA and

home purchase and refinance products, including FHA and VA loans, that were originated nationwide through a network of mortgage originators. Residential mortgage loans accounted for less than 1 percent of FSB’s loan portfolio. Due to a change in FSB’s business model, LMC ceased operations on July 31, 2010.

[29] These ratings represented FSB’s first CRA examination, and the review period was April 1, 2008, the date the bank commenced operations, through December 31, 2009.

[30] Branch Bank, which will survive the merger with BankAtlantic, is a state nonmember bank supervised by the FDIC.

[31] The Board reviewed 2008, 2009, 2010, and preliminary 2011 HMDA data for Branch Bank in its combined assessment areas; in Florida, Georgia, North Carolina, and Virginia (the states with the majority of the bank’s branching network); and in all areas identified by the commenter. The Board also reviewed BankAtlantic’s 2008, 2009, 2010, and preliminary 2011 HMDA data in the MSAs cited in the comments, as well as BankAtlantic’s HMDA lending throughout its combined assessment areas.

entered the market only recently, in August 2009, when BB&T acquired Colonial Bank, Montgomery, Alabama, in a failed-bank transaction with the FDIC.

In 2011, HMDA loan applications from African Americans and Hispanics in Branch Bank's combined assessment areas increased slightly from 2010. The Board notes that, although the percentage of Branch Bank's originations to African Americans in 2011 remained the same as in 2010, the percentage of its loan originations to Hispanics increased slightly. In addition, Branch Bank's HMDA loan originations in minority census tracts, in LMI census tracts, and to LMI individuals remained steady or increased in 2011.

The Board's review of Branch Bank's denial disparity rates to African American or Hispanic applicants relative to white applicants (denial disparity ratios or "DDRs") in its combined assessment areas, the State of North Carolina (the bank's home state), the Winston-Salem MSA (the bank's headquarters), the State of Florida, and the MSAs identified by the commenter, indicates that the DDRs were largely consistent with, or more favorable than, those of the aggregate in 2010.

Regarding BankAtlantic, in 2010 the thrift's lending significantly exceeded the aggregate's lending with respect to the percentage of its loans to African Americans and Hispanics, in minority and LMI census tracts, and to LMI individuals. In 2010, BankAtlantic's DDRs for African Americans were more favorable than those of the aggregate in all of the thrift's combined assessment areas, as well as in the areas of interest to the commenter. For Hispanics, the thrift's DDRs were consistent with the aggregate in all of the thrift's combined assessment areas, as well as in the two MSAs cited by the commenter. In 2011, the DDRs for African American and Hispanic borrowers largely mirrored the thrift's performance in 2010.

The Board is concerned when HMDA data for an institution indicate disparities in lending and believes that all lending institutions are obligated to ensure that their lending practices are based on criteria that ensure not only safe and sound lending but also equal access to credit by creditworthy applicants regardless of their race or ethnicity. Although the HMDA data might 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 Branch Bank or BankAtlantic has excluded or imposed higher costs on any group on a prohibited basis. The Board recognizes that HMDA data alone, even with the recent addition of pricing information, provide only limited information about the covered loans.[32] HMDA data, therefore, have limitations that make them an inadequate basis, absent other information, for concluding that an institution has engaged in illegal lending discrimination.

Because of the limitations of HMDA data, the Board's consideration of those data has taken into account other information, including examination reports that provide on-site evaluations of compliance with fair lending and other consumer protection laws and regulations by BB&T and its lending affiliates. The Board has also considered information provided by BB&T about its compliance risk-management systems and has consulted with the FDIC, the primary federal supervisor of Branch Bank, and the OCC, the primary federal supervisor of BB&T's subsidiary federal savings bank and BankAtlantic.

[32] 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 whether an applicant who was denied credit was, in fact, creditworthy. In addition, 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) are not available from HMDA data.

Although the HMDA data suggest that there may be opportunities for Branch Bank to improve its outreach and mortgage lending to African Americans and Hispanics and in minority communities, the HMDA data, absent other information, are not evidence of discrimination. Branch Bank is subject to continuous supervision by its supervisory agencies, and it has undergone a number of reviews for compliance with consumer protection and fair lending laws, regulations, and statutes since its 2008 CRA evaluation. Such reviews incorporate additional data beyond the HMDA data reported annually and include reviews of loan files, the articulated policies and procedures of the institution, and assessments of the bank's actual practices. The fair lending reviews include assessments of Branch Bank's underwriting, pricing, and advertising and marketing programs, and examiners have found no evidence of discouragement or discrimination on any prohibited basis. Further, the Board has reviewed Branch Bank's compliance programs and conferred with the FDIC. The Board concludes that Branch Bank's mortgage lending operations and compliance programs are sufficient to ensure compliance with fair lending and other consumer protection laws. In addition, the Board notes that this proposal is designed to round out Branch Bank's presence in certain markets and finds that the bank is well positioned to take advantage of the opportunities presented to enhance its mortgage lending efforts with respect to traditionally underserved racial and ethnic market segments.

The Board has considered all the facts of record, including the CRA performance records of the institutions involved, information provided by BB&T, comments received on the proposal and responses to those comments, and confidential supervisory information. Based on a review of the entire record, and for the reasons discussed above, the Board concludes that convenience and needs considerations, including the CRA performance records of the relevant insured depository institutions, are consistent with approval of the proposal. Moreover, the adoption of BB&T's policies and procedures into BankAtlantic's operations is likely to help improve overall CRA compliance.

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.[33]

Financial Stability Standard

In reviewing proposals under section 4 of the BHC Act, the Board expects that it will generally find a significant adverse effect if the failure of the resulting firm, or its inability to conduct regular-course-of-business transactions, would likely impair financial intermediation or financial market functioning so as to inflict material damage on the broader economy. That kind of damage could occur in a number of ways, including seriously compromising the ability of other financial institutions to conduct regular-course-of-business transactions or seriously disrupting the provision of credit or other financial services.

To assess the likelihood that failure of the resulting firm may inflict material damage on the broader economy, the Board will consider a variety of metrics that capture the systemic "footprint" of the merged firm and will also consider the incremental effect of the transaction on the systemic footprint of the acquiring firm. These metrics would include measures of the size of the resulting firm; availability of substitute providers for any critical products

[33] Dodd-Frank Act, § 604(e), codified at 12 U.S.C. § 1843(j)(2)(A). 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) and (f) of the Dodd-Frank Act.

and services offered by the resulting firm; interconnectedness of the resulting firm with the banking or financial system; the extent to which the resulting firm contributes to the complexity of the financial system; and the extent of the cross-border activities of the resulting firm.[34] These categories are not exhaustive, and additional categories could inform the Board's decision.[35] In addition to these quantitative measures, the Board will consider 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.[36]

Analysis of the Financial Stability Impact of this Proposal

In this case, the Board has evaluated the foregoing metrics to determine whether the proposal presents a significant risk to the stability of the U.S. banking or financial system. The Board also has considered the relative degree of difficulty of resolving the resulting firm. The Board reviewed publicly available data, data compiled through the supervisory process, and data obtained through information requests to the institutions involved in the proposal, as well as qualitative information.

This transaction would increase BB&T's systemic footprint by only a negligible amount and, therefore, would not raise financial stability concerns. BB&T would control 1.4 percent of the total U.S. deposits after the transaction, placing it well within the 10 percent limitation on total U.S. deposits. The proposed transaction would increase the firm's size and degree of interconnectedness with other financial institutions, and contribute to complexity of the financial system, by an insignificant amount. Furthermore, neither BB&T nor BankAtlantic has market shares that are sufficiently large to suggest they are major providers of any critical financial services. Consequently, the acquisition does not raise concerns about a potential lack of substitute providers for such services.

In addition, the structure and operation of the combined organization would be centered on a conventional commercial banking business. In the event of distress, the resolution process would be handled in a predictable manner by relevant authorities. The combined firm would not exhibit a high degree of organizational or legal complexity and would have limited engagement in cross-border activities, further suggesting that resolution of the combined organization in the event of its failure would not involve a level of cost, time, or difficulty that would jeopardize the stability of the USFS.

Based on these and all the other facts of record, the Board has determined that considerations relating to financial stability are consistent with approval.

[34] A large value of a metric for any one category may suggest that distress at the resulting firm is likely to result in material damage to the broader economy. Many of the metrics considered by the Board measure an institution's activities relative to the U.S. financial system ("USFS"). For example, the pro forma asset size of the resulting firm is expressed in terms of the resulting firm's pro forma assets as a share of total assets of the USFS. For this purpose, the USFS comprises all U.S. financial institutions used in computing total liabilities for the purposes of calculating the limitation on liabilities of a financial company required under section 622 of the Dodd-Frank Act and includes U.S.-based bank and nonbank affiliates of foreign banking organizations. In connection with its supervision of nonbank financial institutions that the Financial Stability Oversight Council determines could pose a threat to the financial stability of the United States, the Board may require financial and other reporting by these institutions, which would increase the pool of available data for financial stability analyses. *See* sections 113 and 151 of the Dodd-Frank Act, codified at 12 U.S.C. §§ 5323 and 5341, respectively.

[35] The metrics for the resulting entity are not, by themselves, determinative. The Board will take into account all factors that are relevant to a transaction, some of which may not be captured by the metrics.

[36] For further discussion of the financial stability standard, *see Capital One Financial Corporation,* FRB Order No. 2012-2 (Feb. 14, 2012).

Public Benefits

As noted, the Board is required to consider whether the proposed acquisition of BankAtlantic "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."[37]

The Board has reviewed the above criteria in light of the record in this case. Overall, the record indicates that consummation of the proposal would result in additional benefits to consumers currently served by BankAtlantic. The proposal would allow BB&T to expand the range of financial products and services available to existing customers of BankAtlantic. After the acquisition, BankAtlantic customers would benefit from Branch Bank's higher legal lending limit, an expanded range of commercial and consumer loan products, a full range of cash management services, a wider variety of mortgage loan products, and access to Branch Bank's corporate, personal, and employee benefit trust services, insurance, and investment services. In addition, BankAtlantic customers would have access to Branch Bank's branch locations and ATM network throughout Florida and the Southeastern United States. BB&T has committed to correct BankAtlantic's deficiencies with respect to overdrafts in customer accounts and to improve BankAtlantic's processes, procedures, and practices for compliance with the CRA. The proposal would provide the opportunity for significant operational efficiencies for the combined organization, and BB&T expects to realize significant cost savings from consolidating systems, platforms, and corporate staff functions.

Based on all the facts of record, including the commitments and conditions noted in this case, the Board has concluded that consummation of the proposal can reasonably be expected to produce public benefits that would outweigh any likely adverse effects. 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.

Conclusion

Based on the foregoing and all the facts of record, the Board has determined that the proposal should be, and hereby is, approved.[38] In reaching its conclusion, the Board has considered all the facts of record in light of the factors that it is required to consider under the BHC Act. The Board's approval is specifically conditioned on compliance by BB&T with the conditions imposed in this order and the commitments made to the Board in connection with the notice. The Board's approval also is subject to all the conditions set forth in

[37] 12 U.S.C. § 1843(j)(2)(A).

[38] A commenter requested that the Board hold a public hearing on the proposal. 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 commenter's request in light of all the facts of record. In the Board's view, commenters have had ample opportunity to submit comments on the proposal and, in fact, submitted written comments that the Board has considered in acting on the proposal. The commenter's request does not identify disputed issues of fact that are material to the Board's decision and that would be clarified by a public hearing. In addition, the request does not demonstrate why the written comments do not present the commenter's 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 request for a public hearing on the proposal is denied.

Regulation Y, including those in sections 225.7 and 225.25(c),[39] and to the Board's authority to require such modification or termination of the activities of a bank holding company or any of its subsidiaries as the Board finds necessary to ensure compliance with, and to prevent evasion of, the provisions of the BHC Act and the Board's regulations and orders issued thereunder. For purposes of this action, these conditions and commitments are deemed to be conditions imposed in writing by the Board in connection with its findings and decision herein and, as such, may be enforced in proceedings under applicable law.

The acquisition shall not be consummated 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 Richmond, acting pursuant to delegated authority.

By order of the Board of Governors, effective July 31, 2012.

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

Robert deV. Frierson
Deputy Secretary of the Board

Order Issued Under Bank Merger Act

Five Star Bank
Warsaw, New York

Order Approving the Acquisition of Branches
FRB Order No. 2012–7 (July 27, 2012)

Five Star Bank ("Five Star"), Warsaw, New York,[1] a state member bank, has applied under section 18(c) of the Federal Deposit Insurance Act[2] ("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 Act[4] ("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.

[39] 12 CFR 225.7 and 225.25(c).

[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 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.

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[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, 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

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.

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.

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.

[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.

[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 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.

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 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]

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.

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[18] 12 U.S.C. § 2901 *et seq*.

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

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 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, effective July 27, 2012.

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

Robert deV. Frierson
Deputy Secretary of the Board

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

[21] *See* 12 U.S.C. §322; 12 CFR 208.6.

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