U.S. Department of Justice

Antitrust Division

Office of the Assistant Attorney General

Washington, D.C. 20530

JUN - 7 1994

William E. Kirk, Esquire
Townshend & Kirk
700 Melvin Avenue
Annapolis, Maryland 21401

Dear Mr. Kirk:

This letter responds to your request for a statement by the Department of Justice, pursuant to the Business Review Procedure, 28 C.F.R. § 50.6, of its enforcement intentions with respect to a proposal by four Annapolis, Maryland banks to act jointly in making home equity loans available to middle and lower income families.

The four banks who seek to act jointly in this matter are the Annapolis Bank and Trust Co., the Annapolis National Bank, the Bank of Annapolis and the Farmers National Bank of Maryland. According to your representations, these banks, like many others, are subject to both regulatory and community pressures to increase their local lending, particularly to middle and lower income households. The proposal that is the subject of this business review request represents an attempt by the four banks to respond to those community desires in a manner that both expands their lending to such borrowers and reduces the risks and costs of such lending.

Under the proposal the four banks initially would commit a total of $2 million that would be loaned to poor and middle income households that seek to improve their homes.[1] Loans under this program would only be available to households whose gross household income does not exceed the median income for the Baltimore SMA, and would range in amounts from $5,000 to $35,000.

Applications for loans under this program would be reviewed by a loan committee consisting of one representative from each bank. The application will be accepted or rejected based on

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[1]Farmers National Bank would commit $1 million to the program. Annapolis Bank and Trust would commit $500,000. Annapolis National Bank and Bank of Annapolis would each commit $250,000. If the program is successful, the parties may increase their participation in the future.

credit-worthiness criteria agreed on by the four banks. Approved applications would be assigned, on a rotating basis, to one of the banks. Each bank would administrator its "own" loans and collect and keep the interest paid thereon. Any losses that result from approved loans will be shared equally by the four banks. The rates and other terms for these loans will be based on a schedule of maximum rates agreed on by the four banks, and the rate schedule will be modified periodically to reflect market changes. You assert that the purpose of the joint proposal is to provide these loans at below-market rates and that the "common rates and terms [will] represent a more flexible and lenient structure to the borrower than the traditional bank products in the market place."

After careful consideration of the information and assurances that you have provided, the Department of Justice has concluded that it has no present intention of challenging under the antitrust laws the proposed joint lending program outlined in this letter.

You assert that the parties' agreement as to rates and terms is an integral part of a joint venture designed to reduce loan rates for, and thereby increase output to, a segment of the populace. Additionally, you have assured us that the joint venture will not reduce the rivalry between the four banks for any other type of business. Under the present circumstances, we have no reason to disagree with your assertions. There is no indication that the proposed joint venture is designed to cloak anticompetitive activity. Moreover, based on the information that you have provided, the potential consumer benefits of the proposal would appear to outweigh any potential competitive risks.

To the extent that money is lent at below-market rates on relaxed credit standards to a given group of borrowers,[2] the resulting loans are riskier than those made at market rates and standards. Since it would be difficult, if not impossible, to predict which of these riskier loans would be defaulted, the sharing of losses may be viewed by each of the four banks as a means of reducing the risk of a large loss. To the extent that risk is reduced, all other things being equal, output should increase and more credit should be made available to persons of modest means than would be the case if the banks acted individually.

In this case the agreement on maximum rates appears clearly ancillary to the sharing of losses. The higher the loan rate, all other things being equal, the higher the risk of default. If

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[2]In this letter, we use the term below-market rates to encompass both the lending of money at lower rates to creditworthy borrowers and the lending of money to those who would not be extended such credit under traditional standards.

an individual bank could raise the interest rates on "its" loans and keep the higher interest earned while sharing the resulting greater loan losses with its co-venturers, it could impose greater risks on the other banks. In such a setting, the utilization of a maximum rate schedule is a not unreasonable means by the joint venturers of reducing the moral hazard under which one could gain by imposing greater risk on the others.

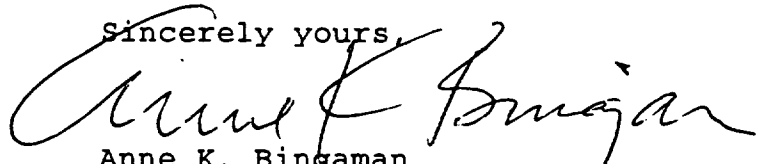
According to the information that you have provided, the four banks have approximately 11.26 percent, 4.97 percent, 1.03 percent and 0.97 percent of IPC deposits in the country, for a cumulative share of 18.2 percent. Moreover, there are some 50 lending institutions doing business in Anne Arundel County. Under these circumstances, your assertion that the proposed joint venture is not a sham designed to cloak a collective exercise of market power with respect to any class of borrower seems credible on its face.[3]

The proposed joint venture could have procompetitive effects. If, as a result of risk reduction or other forms of cost savings dependent on joint action, more loans are made than would occur through individual bank lending both the consumer and production goals of the antitrust laws would be well served.

This letter only expresses the Department's current enforcement intention. In accordance with our normal practices, the Department remains free to bring whatever action or proceeding it subsequently comes to believe is required by the public interest if actual operation of any aspect of the proposed joint action proves anticompetitive in purpose or effect.

This statement of the Department's enforcement intentions is made in accordance with the Department's Business Review Procedure, 28 C.F.R. § 50.6. Pursuant to its terms, your business review request and this letter will be made available to the public within 30 days of the date of this letter unless you request that part of the material be withheld in accordance with Paragraph 10(c) of the Business Review Procedure.

Sincerely yours,



Anne K. Bingaman
Assistant Attorney General

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[3]An agreement to charge less than market rates does not necessarily mean that the rates charged will be at a competitive level or below. A cartel agreement to reduce rates below the existing monopoly or oligopoly level could still yield supra-competitive pricing. There is no evidence, however, that such a situation exists here.