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TARP Capital Purchase Program Update

On October 14th, the U.S. Treasury announced a Capital Purchase Program to purchase up to \$250 billion of senior preferred shares from U.S. banks, savings associations, and their holding companies. An election to participate in the Program must be made by November 14, 2008. The Treasury Department's initial announcement, and the accompanying term sheet, raised many questions about the Program for which answers are beginning to emerge. Summarized below are the terms of the Program as announced and some of the clarifying statements which have been issued in recent days.

Program Terms

Eligible Institutions. Eligible institutions include any U.S. bank or U.S. savings association not controlled by a Bank Holding Company ("BHC") or Savings and Loan Holding Company ("SLHC") and any U.S. BHC, or any U.S. SLHC which engages only in activities permitted for financial holdings companies under Section 4(k) of the Bank Holding Company Act.

Purchase Amount. The minimum subscription amount is 1% of an institution's risk-weighted assets. The maximum subscription amount is the lesser of \$25 billion or 3% of its risk-weighted assets. Funding will occur by year-end 2008.

Rank and Voting Rights. The Senior Preferred shares to be issued will be perpetual, will qualify as Tier 1 capital, and will rank senior to common stock and pari passu (at an equal level in the capital structure) with existing preferred shares, other than preferred shares which by their terms rank junior to other preferred shares. The Senior Preferred shares will be non-voting, other than class voting rights on matters that could adversely affect the shares.

Dividends. The senior preferred shares will pay cumulative dividends at a rate of 5% per annum for the first five years and 9% per annum thereafter. For Senior Preferred issued by banks which are not subsidiaries of holding companies, the Senior Preferred will pay non-cumulative dividends at a rate of 5% per annum for the first five years and thereafter at a rate of 9% per annum. If dividends on the Senior Preferred are not paid in full for 6 dividend periods, whether or not consecutive, the Senior Preferred will have the right to elect 2 directors. The right to elect directors will end when full dividends have been paid for four consecutive dividend periods. As long as an institution is current on its dividends on the Senior Preferred shares, it may declare and pay dividends on preferred shares ranking pari passu with the Senior Preferred, junior preferred shares and common shares. During the first 3 years after issuance, Treasury's consent will be required for any increase in an institution's common dividends unless the Senior Preferred has been redeemed or Treasury has transferred all of the Senior Preferred to third parties.

Share Repurchases. Treasury's consent will be required for any share repurchases by an institution within the first 3 years (other than repurchases of the Senior

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Preferred and repurchases of shares in connection with any benefit plan in the ordinary course of business consistent with past practice) unless, prior to the repurchase, the Senior Preferred has been redeemed or Treasury has transferred all of the Senior Preferred to third parties.

Redemptions and Transfer. The Senior Preferred shares will be callable at par after 3 years. Prior to the end of this 3-year period, the Senior Preferred may be redeemed with the proceeds from certain qualifying equity offerings of Tier 1 perpetual preferred or common stock. The Senior Preferred shares may be transferred by Treasury to a third party at any time.

Warrants. Treasury will receive warrants to purchase common stock of the institution with an aggregate market price equal to 15% of the Senior Preferred investment. The warrants will have a 10-year term and be exercisable immediately. The exercise price on the warrants will be the market price of the institution's common stock at the time of issuance, calculated on a 20-trading day trailing average.

Executive Compensation. For the period during which Treasury holds equity issued under the Program, institutions must adopt the Treasury Department's standards for executive compensation and corporate governance. These standards, which generally apply to the chief executive officer, chief financial officer, plus the next three most highly compensated executive officers, include:

(1) ensuring that incentive compensation for senior executives does not encourage unnecessary and excessive risks that threaten the value of the institution;

(2) required clawback of any bonus or incentive compensation paid to a senior executive based on statements of earnings, gains or other criteria that later are proven to be materially inaccurate;

(3) prohibiting the institution from making any golden parachute payment to a senior executive based on Internal Revenue Code Section 280G; and

(4) agreeing not to deduct for tax purposes executive compensation in excess of \$500,000 for each senior executive.

Additional Clarifications

Since the announcement of the Program, various statements and releases have been issued to clarify certain uncertainties following the initial release.

Capital Treatment of Senior Preferred. The Federal Reserve Board issued an interim final rule on October 16 indicating that the Senior Preferred could be included as Tier 1 capital for bank holding companies. A similar clarification is expected shortly from the banking regulators.

Accounting Treatment of Warrants. *The American Banker* reported on October 19 that a letter was sent from the SEC's Deputy Chief Accountant and a technical advisor to the Financial Accounting Standards Board to the Treasury Department's Assistant Secretary for Financial Institutions indicated that they would not object "if the warrants...were to be classified as permanent equity." A resolution of this issue would respond to concerns which have been raised that the warrants might be treated as liabilities and not equity under generally accepted accounting principles.

FDIC FAQs: On October 20, the FDIC issued a process-related FAQs for the Program. Certain of the questions and answers in that release are summarized below.

Q: How does an institution apply to participate in the Program?

A: An institution must submit an application to its appropriate Federal banking agency. If the applicant is a bank holding company, the application should be submitted to both the applicant's holding company supervisor and the supervisor of the largest insured depository institution controlled by the applicant. Each Federal banking agency has information on its Web site regarding where an application for participation in the Program should be directed.

Q: Is there an application form?

A: Yes. The Federal banking agencies have developed a common application form that should be used to participate in the Program. The application form is available on the web site of each Federal banking agency.

Q: What information must be provided in the application?

A: The application requires an institution to submit basic information about the institution, the amount of the perpetual preferred stock investment that the financial institution is requesting from Treasury, as well as information regarding the amount of authorized but unissued preferred stock and common stock that the institution currently has available for purchase.

Q: What happens if an institution is unable to issue the Preferred Shares by the application deadline due to the need for a shareholder vote, Board authorization, or other constraint?

A: Institutions do not need to complete all of the required authorizations by the submission of the application. If an institution receives preliminary approval, it will have 30 days in which to submit final documentation and fulfill any outstanding requirements. An institution must explain any limitations to executing the final documentation or meeting the required conditions on its application form.

Q. Will applications filed by institutions or the names of institutions be released publicly?

A. No. All applications are confidential proposals submitted for review by an institution's appropriate Federal banking agency. Applications which are denied or withdrawn will not be disclosed. Treasury will provide electronic reports detailing any completed transactions, as required by the Emergency Economic Stabilization Act of 2008, within 48 hours.

Q: Who should an institution contact with questions regarding how to file an application or the status of a submitted application?

A: An institution should contact its appropriate Federal banking agency using the contact information provided on the agency's Web site.

Q: How long will it take for an application to be processed?

A: Treasury, working in consultation with the Federal banking agencies, will process and preliminarily accept applications as expeditiously as possible. Because of the diversity of institutions that are expected to apply, response times may vary.

Q: When must an institution submit the final documentation to complete the Preferred Share purchase?

A: Final documentation must be submitted no later than 30 days after an institution has been notified that it has received preliminary acceptance into the Program.

Bar Admissions:

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