

What's Under the TARP?

Treasury's Capital Purchase Plan
and the
FDIC's Temporary Liquidity Guarantee Program

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Capital Purchase Plan

- What would we be issuing?
- Are we eligible?
- Should we participate?
- How do we apply?
- Any "gating issues?"
- How does this affect executive comp?

What would we be issuing?

Senior Preferred Stock

(Full term sheet is available at www.treas.gov)

- Capital Treatment: Tier 1 eligible
- Amount: 1%-3% of risk-weighted assets
- Voting: generally non-voting
- Dividend--5% initial, 9% after 5 years

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Senior Preferred Stock (cont.)

- Redemption: Redeemable within 1st 3 years with proceeds from a common stock or a Tier 1 perpetual preferred offering equal to at least 25% of the issue price of the Senior Preferred
- Transferability: no contractual restrictions
- Registration:
 - Must file a shelf registration statement with the SEC covering the Senior Preferred
 - Must provide “piggyback” registration rights

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Senior Preferred Stock (cont.)

- Dividends: can't increase common dividends without Treasury approval until the 3rd anniversary of issuance unless the Senior Preferred has been redeemed or transferred. Must be current in Senior Preferred dividends before paying on junior securities.
- Repurchase restrictions: Treasury consent required for most common/junior share repurchases until the 3rd anniversary of the investment unless Senior Preferred has been redeemed or transferred. Must be current on Senior Preferred dividends before repurchasing common/junior securities.

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Warrants

- Amount: 15% of the Senior Preferred dollar amount
- Exercise Price: the 20-trading day trailing average market price of the common stock on the date of the investment
- Voting: warrant shares issued to Treasury upon exercise are non-voting
- Term: 10 years
- Accounting: equity (not liability) treatment. Capital treatment still to be determined.

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Warrants (cont.)

- Registration: must apply to list the underlying warrant shares on a national exchange and provide “piggyback” registration rights
- Exercise/Transfer Limitations: Treasury can transfer or exercise only 50% of the warrants before the earlier of:
 - Dec. 31, 2009 or
 - Company’s receipt of gross proceeds of 100% of the issue price of the Senior Preferred from offering(s) of common or Tier 1 perpetual preferred stock

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Warrants (cont.)

- Reduction: if the Company raises common or perpetual preferred equal to at least 100% of the issue price of the Senior Preferred by Dec. 31, 2009, the number of warrants will be reduced by 50%.
- Substitution: If the Company is no longer exchange listed or can’t obtain shareholder approval to issue warrant shares (if required) within 18 months after issuance, Treasury has option to exchange the warrants for senior term debt or other instrument(s)

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Are We Eligible?

- “Healthy”—yes; “Troubled”—no. But what does this mean?
- Evaluation most likely based on CAMELS ratings, ratios (current and projected) and regulatory recommendations.
- Other possible factors: projected CRE concentration (less than 300%), use of proceeds (lending, acquisitions, replenish loan loss reserve, etc.)

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Are We Eligible? (cont.)

- Telephone discussions re eligibility with primary federal regulator are encouraged; in-person meetings aren't
- Currently structured for public companies; participation by others is contemplated, but terms are as yet unknown.

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Should We Participate?

- Financial Considerations
 - Need for capital in current economy
 - Effect on EPS, cash flow, book value.
 - Generally, the lower your P/E ratio, the more attractive it is
 - Restrictions on common dividend increases and repurchases of common and other junior securities (note: trust preferred is senior to Senior Preferred)

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Should We Participate? (cont.)

Financial Considerations

- Deployment of proceeds
- Accounting treatment
- Compare to other capital alternatives
- Executive comp limitations
 - Employment contracts, SERPs, etc.
 - Loss of deductibility of over \$500,000 of comp

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Should We Participate? (cont.)

Financial Considerations

- Holding company cash flow from bank(s)
- Exit strategy
 - New capital by the end of 2009 to reduce warrants
 - 3-year call date
 - 5-year dividend increase
- Rule of Thumb--take it if you can get it

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Should we Participate?

- Non-Financial Considerations
 - Perception factor— “in vs. out”
 - Competitive effects—don’t get left behind
 - Uncle Sam is now a significant investor...but increased industry regulation will come, regardless of whether you participate
 - Probably a one-time offer, so request as much as you think you’ll need

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How Do We Apply?

- Application and instructions are available on Fed, FDIC, OCC and OTS websites (joint press release issued Oct. 20, 2008)
- Current version of application may change to include projections (with requested capital vs. without) and interest in acquiring failed/failing institutions
- BHCs submit to Fed and the Bank's primary federal regulator
- Banks w/o holding companies submit to primary federal regulator

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How Do We Apply? (cont.)

- Review investment agreement and related documents (to be posted to Treasury's website soon) before submitting application
- Determine ability to comply with reps, warranties and closing conditions—especially registration and authorization of shares
- "Robustly explain" in the application any limitations in ability to execute the required documents or meet closing conditions—important for private/Sub S companies that apply

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How Do We Apply? (cont.)

- Submit application to federal banking regulator(s) by 5:00 p.m. eastern time Nov. 14, 2008
- Treasury will issue preliminary approval “promptly”--will not be “first come, first served”
- No publication of rejection; Treasury will publish acceptances within 48 hours
- Must submit final documentation and fulfill any outstanding requirements within 30 days after preliminary acceptance

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How Do We Apply? (cont.)

- Contacts: If regulated by the:
 - Federal Reserve: contact your local Reserve Bank about the program.
 - FDIC: contact the appropriate regional office for your institution.
 - OCC: contact Fred Finke (fred.finke@occ.treas.gov) for more information and send applications to HQ.Licensing@occ.treas.gov or OCC Director of Licensing, 250 E St. SW, Mail Stop 7-13, Washington DC, 20219-0001.
 - OTS: contact the appropriate regional office for your institution.

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“Gating issues”

- Charter amendment: articles of incorporation may need to be amended to provide:
 - Authority to issue preferred stock
 - Sufficient number of authorized shares of common stock to cover warrants upon exercise

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“Gating Issues” (cont.)

- If amendment is needed:
 - Call shareholders' meeting to approve amendment
 - If SEC registered, file preliminary proxy materials with SEC for potential review
 - Must have shareholder approval before Senior Preferred can be issued
 - Authorization of additional warrant shares can wait, but exercise price goes down by 15% every 6 months until shareholder approval is obtained, with substitution of other instrument(s) after 18 months

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“Gating Issues” (cont.)

- Shelf Registration
 - As currently structured, the program requires the issuer to register the Senior Preferred, warrants and warrant shares with the SEC
 - Must also apply to list the warrant shares on the same exchange on which your common stock is traded
 - Warrants will be exchangeable, at Treasury’s option, for other securities/instruments that reflect equivalent value if exchange listing is lost or shareholder approval of warrant shares is not received within 18 months

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“Gating issues” (cont.)

- Open questions:
 - What provisions will apply to private companies, S corps and mutuals?
 - Should they apply now? Current informal guidance is yes, with an explanation of issues affecting ability to participate in the program as currently structured.
 - What about public companies that aren’t listed on an exchange?
 - State securities law (“blue sky”) implications
 - Interplay between SEC review and regulatory issuance time frames

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Executive Comp Restrictions

- Full guidelines available at www.treas.gov.
- Restrictions apply to the “Top 5”:
 - Principal executive officer
 - Principal financial officer
 - 3 other most highly compensated executive officers
- Requires recovery of incentive comp paid based on materially inaccurate statements of earnings or other criteria
- Cannot deduct more than \$500,000 of executive comp for each of the Top 5

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Executive Comp Restrictions (cont.)

- “Golden Parachute” prohibition
 - Applies to Top 5
 - Same as 280G limitation--present value of severance payments must be less than 3 times the 5-year average of the executive’s annual W-2 compensation
 - Before closing the capital purchase, must terminate/revise employment agreements, bonus plans, etc. that violate the Fed’s restrictions
 - Consult with counsel to avoid potential 409A traps when revising comp arrangements

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Temporary Liquidity Guarantee Program

- Guarantee of Newly Issued Debt
 - FDIC-insured institutions and holding companies are eligible
 - Will not be extended to “troubled institutions”
 - Guarantee (to applicable limit) of all newly issued senior unsecured debt issued before June 30, 2009
 - Limited to 125% of senior unsecured debt:
 - Outstanding as of Sept. 30, 2008 and
 - Scheduled to mature before June 30, 2009

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Temporary Liquidity Guarantee Program

- Guarantee of Newly Issued Debt (cont.)
 - Extends 3 years (to June 30, 2012), regardless of whether liability has matured by that date
 - 75 basis point fee
 - Automatic coverage with fee waiver until opt-out deadline of Nov. 14, 2008
 - FDIC will issue specific guidelines, including Fed Funds application and prohibition of prepayment and replacement of existing debt with guaranteed debt

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Temporary Liquidity Guarantee Program

- Non-interest-bearing Deposit Transaction Accounts
 - Full FDIC insurance coverage, regardless of dollar amount, until Dec. 31, 2009
 - Primarily payroll and other business accounts--will be extended to all non-interest-bearing accounts
 - Effective automatically as of Oct. 14, 2008; may opt out thereafter (but can't opt back)
 - 10 basis point fee applied to accounts not otherwise covered by existing \$250,000 limit
 - FDIC will issue further guidance (customer notification, etc.)

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Intra-TARP Interplay

- Can participate in all of these programs, some or none
- Executive comp restrictions apply only to the Capital Purchase Program. Similar restrictions will apply to the troubled asset auction and "systemically significant failing institutions" programs
- Participants in the FDIC programs will be subject to enhanced regulatory oversight to prevent rapid growth/excessive risk-taking

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Long-term Questions

- Hoard or lend?
 - Treasury wants banks to lend proceeds, but there's no requirement to do so
 - Tough times ahead justify significant capital reserves; asset quality is still an issue
- Politics--will foreclosure mitigation efforts be required?
- Competitive landscape—will this prolong life for irrational competitors?

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Long-term Questions (cont.)

- Funding for increased M&A?
 - Cheap capital for potential acquirors...
 - But M&A volume may not increase if banks that might otherwise sell may get new leases on life
- Treasury has a broad array of powers—how aggressively will it use them?

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