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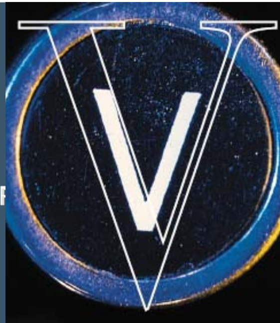

economic crisis team

A PUBLICATION OF VENABLE'S CORPORATE AND FINANCIAL SERVICES GROUPS

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Please contact any of the Venable lawyers named below if you have any questions about the new Capital Purchase Program or Liquidity Guarantee Program.

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FEDERAL GOVERNMENT TAKES HISTORIC ACTIONS IN SUPPORT OF U.S. FINANCIAL INSTITUTIONS

On October 14, 2008, both the United States Department of Treasury and the Federal Deposit Insurance Corporation (the "FDIC") announced historic and unprecedented actions designed to encourage U.S. financial institutions to build capital and to strengthen confidence and encourage liquidity in the banking system. These actions demand the immediate attention of financial institutions and will require swift and decisive action by directors of financial institutions within the next 30 days. As detailed below, Treasury announced a voluntary Capital Purchase Program (the "Capital Purchase Program"), pursuant to which it will purchase up to $250 billion of senior preferred securities from eligible U.S. financial institutions on standardized terms. In turn, the FDIC announced a Temporary Liquidity Guarantee Program (the "Liquidity Guarantee Program"), pursuant to which the FDIC will guarantee certain newly-issued senior unsecured debt issued by eligible institutions on or before June 30, 2009, as well as funds in non-interest bearing transaction deposit accounts held by FDIC-insured banks until December 31, 2009. Summaries of both of these Programs are set forth below.

Treasury Department Details Capital Purchase Program

An eligible institution that desires to participate in the Capital Purchase Program must notify Treasury of its election to participate before **5:00 p.m. (EDT) on November 14, 2008**. Participation in the Capital Purchase Program will require negotiating and preparing the appropriate documentation with Treasury and taking necessary corporate actions to issue the preferred securities to Treasury. Also, because participation in the Program will trigger certain restrictions on compensation of senior executives, in order to avoid questions regarding conflicts of interests, institutions may want to have the determination as to whether to participate in the Program made or reviewed by the institution's independent directors or a special committee of independent directors.

Under the Capital Purchase Program, Treasury has developed standardized terms for its purchase of up to $250 billion of senior preferred shares (the "Senior Preferred") of Qualifying Financial Institutions ("QFI") electing to participate in the Program. Funding under the Capital Purchase Program will occur by year-end 2008. As of October 14, 2008, nine large financial institutions have agreed to participate in the Capital Purchase Program.

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Eligibility and Allocation

To be deemed a QFI, the issuer must be:

- a U.S. bank or U.S. savings association not controlled by a bank holding company or savings and loan holding company;

- a U.S. bank holding company or U.S. savings and loan holding company that engages only in activities permitted for financial holding companies under Section 4(k) of the Bank Holding Company Act and any U.S. bank or U.S. savings association controlled by such a U.S. bank holding company or U.S. savings and loan holding company; or

- a U.S. bank holding company or U.S. savings and loan holding company whose U.S. depository institution subsidiaries are the subject of an application under 4(c)(8) of the Bank Holding Company Act (any company the activities of which have been determined to be so closely related to banking as to be a proper incident thereto).

Banks, savings associations, bank holding companies, and savings and loan holding companies that are controlled by a foreign bank or company are not eligible to participate nor, apparently, are grandfathered unitary thrift holding companies or industrial loan holding companies that engage in non-financial activities.

Once Treasury, in consultation with the applicable federal banking agency, confirms eligibility, a QFI may issue to Treasury an amount of Senior Preferred equal to not less than 1% of the QFI's risk-weighted assets, but not more than the lesser of (i) $25 billion or (ii) 3% of the QFI's risk-weighted assets.

The Senior Preferred will have a liquidation preference of at least $1,000/share, rank senior to common stock and equal with existing senior preferred shares, qualify for Tier 1 status and have a perpetual life.

Dividends

Cumulative dividends will be paid quarterly on the Senior Preferred at a rate of 5% per year for the first five years and 9% per year thereafter. If dividends on Senior Preferred are not paid in full for six dividend periods, whether or not consecutive, the Senior Preferred will have the right to elect two directors of the QFI, which right will continue until dividends have been paid in full for four consecutive dividend periods. No dividends may be declared or paid on other preferred or common shares as long as the Senior Preferred is outstanding. Consent of Treasury is required for any increase in common dividends or share repurchases until the third anniversary of its investment.

Redemption and Repurchases

During the first three years of the investment, the Senior Preferred may only be redeemed with proceeds from the QFI's sale of Tier 1 qualifying perpetual preferred stock or common stock for cash which results in gross proceeds of not less than 25% of the Senior Preferred issue price. After the third anniversary, the Senior Preferred may be redeemed at any time for 100% of the issue price plus accrued and unpaid dividends, subject to the approval of the QFI's primary federal bank regulator.

Until the third anniversary of the investment, the consent of Treasury shall be required for any share repurchases by the QFI (other than repurchases of Senior

Preferred and repurchases of junior preferred shares and common shares in connection with any benefit plan in the ordinary course of business consistent with past practice), unless prior to the third anniversary the Senior Preferred is redeemed in whole or Treasury has transferred all of the Senior Preferred to third parties. Additionally, the QFI may not repurchase or redeem any other preferred or common shares unless full dividends have been paid on the Senior Preferred.

Transferability

Treasury may transfer the Senior Preferred to a third party at any time. The QFI is bound to promptly file a shelf registration statement and to grant Treasury piggyback registration rights for the Senior Preferred.

Voting rights

Voting rights of the Senior Preferred are limited to class voting rights on:

- the authorization or issuance of shares ranking senior to the Senior Preferred;
- any amendment to the rights of the Senior Preferred; or
- any merger, exchange or other transaction that would adversely affect the rights of the Senior Preferred.

Executive compensation

A QFI participating in the Capital Purchase Program must adopt Treasury's standards for corporate governance and executive compensation and must comply with these standards for so long as Treasury holds the Senior Preferred. These standards generally apply to the CEO, the CFO and the next three most highly compensated executive officers and include:

- ensuring compensation does not encourage unnecessary and excessive risk;
- requiring the clawback of compensation paid based on materially inaccurate criteria;
- prohibiting golden parachute payments; and
- agreeing not to deduct for tax purposes compensation in excess of $500,000 for each senior executive.

Warrants

On the date of investment, Treasury will also receive immediately exercisable warrants from the QFI to purchase common stock having an aggregate market price equal to 15% of the Senior Preferred investment. The initial exercise price for the warrants will be the market price for the QFI common stock on the date of the Senior Preferred investment, calculated on a 20-trading day trailing average. Accordingly, an institution that is not publicly traded may be ineligible to participate in the program.

FDIC Temporary Liquidity Guarantee Program to Guarantee Bank Debt and Insure Non-Interest Bearing Deposit Transaction Accounts

Under the Liquidity Guarantee Program, the FDIC will guarantee newly-issued senior unsecured debt and non-interest bearing deposit transaction accounts at FDIC-

insured depository institutions, subject to the terms outlined below.

Guaranteed Liabilities

The FDIC's guarantee will apply to the following liabilities:

- All newly-issued senior unsecured debt issued by an eligible institution on or before June 30, 2009, including promissory notes, commercial paper, inter-bank funding, and any unsecured portion of secured debt. Eligible debt will be 100% guaranteed by the FDIC through June 30, 2012 (regardless of the actual date of maturity of the liability). The amount of debt covered by the guarantee may not exceed 125% of debt outstanding as of September 30, 2008 that was scheduled to mature before June 30, 2009. Eligible institutions include FDIC-insured depository institutions, U.S. bank holding companies, U.S. financial holding companies, and certain U.S. savings and loan holding companies.

- All funds in non-interest bearing deposit transaction accounts held by FDIC-insured banks until December 31, 2009.

Fees and Duration

Eligible institutions will be covered under the Liquidity Guarantee Program for a period of 30 days, and fees for coverage will be waived during that time. Prior to the expiration of the 30 day period, however, eligible institutions must inform the FDIC whether they intend to opt out of the Program. Coverage of guaranteed liabilities at eligible institutions that opt out of the Liquidity Guarantee Program will expire at the end of the 30 day period, regardless of the term of the instrument. After the first 30 days, eligible institutions that do not opt out of the Liquidity Guarantee Program will be charged a fee as follows:

- for all newly-issued senior unsecured debt, an annualized fee equal to 75 basis points multiplied by the amount of debt issued under the Liquidity Guarantee Program; and

- for non-interest bearing transaction deposit accounts, a 10 basis point surcharge that will be applied to non-interest bearing transaction accounts not otherwise covered by the existing deposit insurance limit of $250,000. This surcharge will be added to the participating institution's current risk-based deposit insurance premium.

The ability of participating eligible institutions to issue guaranteed debt under the Liquidity Guarantee Program will expire on June 30, 2009. Participating institutions will be subject to enhanced supervisory oversight to prevent rapid growth or excessive risk-taking.

How We Can Help

The clock is ticking for financial institutions wishing to participate in Treasury's Capital Purchase Program or the FDIC's Liquidity Guarantee Program. If you are involved with a financial institution that meets the criteria for participating in either Program and would like some guidance about the criteria that you should evaluate in determining whether, and to what extent, you should participate; what steps need to be taken to implement your participation in these Programs; or the extent to which any employment or executive compensation programs must be restructured to facilitate your participation in these programs, Venable is here to help you. Please feel free to contact Ron Glancz in Venable's Financial Services practice group at (202) 344-4947 or rglancz@venable.com or Tom France in Venable's Corporate practice group at (703) 760-1657 or tfrance@venable.com.

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