

TARP Capital Purchase Program – Application FAQs

October 25, 2008

On October 20, 2008, the Treasury, in conjunction with the FDIC, FRB, OCC and OTS (collectively, the “Federal Banking Agencies”), released application guidelines for financial institutions interested in participating in the TARP Capital Purchase Program (the “Program”). For a detailed discussion regarding the Program and its executive compensation restrictions, please see the presentations on our website entitled “[TARP Capital Purchase Program](#)” and “[Executive Compensation Restrictions under TARP Capital Purchase Program](#).”

Additionally, we anticipate that the Treasury will publish the form of the investment and related legal documents for participation in the Program within days. We continue to be closely tracking government responses to the turmoil effecting many of our clients, including development regarding the Program as well as any guidance the Treasury and the Federal Banking Agencies may issue.

Based upon a review of the material the Federal Banking Agencies have made available and on our conversations with our clients and the Federal Banking Agencies, below are frequently asked questions we hope are helpful in assisting you determine whether to participate in the Program.

FAQs regarding TARP Capital Purchase Program Application Process

1. Can all banks participate?

Generally speaking, the Program is available to (a) any U.S. banking holding company or savings and loan holding company which engages solely or predominately in activities that are permitted for financial holding companies and (b) any U.S. bank or savings association not controlled by a holding company.

The Federal Banking Agencies have been clear that eligible institutions include mutual and sub-chapter S organizations. Financial institutions controlled by a foreign entity will not be eligible. All eligible institutions have been encouraged to participate.

2. What are some of the pros and cons of participating in the Treasury’s Capital Purchase Program?

Pros:

- The standardized terms of the Program have been designed in an attempt to attract not only weaker institutions, but healthier ones as well, in an effort to address the possible stigma of participation.
- Based upon the state of the private market and the terms of the perpetual senior preferred shares and warrants to be issued pursuant to the Program, the investment is fairly inexpensive “bridge” financing and below current market terms, and the preferred stock issued to the Treasury will be treated as Tier 1 capital by the Federal Banking Agencies.
- An institution could use the preferred stock investment to build capital to cushion future losses or provide the capital to support growth in earning assets or to implement strategic initiatives, including mergers and acquisitions. In order to ensure broad-based participation, the Federal Banking Agencies have not issued many restrictions on the use of these proceeds.
- The 10-year warrants that will be issued will be equal to 15% of the Treasury’s preferred stock investment, with a fair market value exercise price (calculated on a 20-trading day trailing average on the date of the investment).

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Cons:

- Some institutions who are well-capitalized have solid asset quality and find it challenging to use the preferred capital to support the generation of earning assets and may not be able to deploy the capital fast enough to generate attractive returns.
- The “strings attached” to the investment, including restrictions on executive compensation, the impact of potential percentage ownership and other dilution resulting from the exercise of warrants or redeeming the preferred stock by issuing common stock, as well as subjecting increased common stock dividends and buyback programs to the consent of the Treasury for three years, may make the investment unattractive to some institutions.
- There are those that believe that there will be a stigma attached to an institution which participates in the Program (which participation will be publicly announced within 48 hours of completion) because this would somehow indicate that such institution was troubled and needed governmental assistance. There are others that believe that there will be a stigma attached to an institution which does not participate because this would indicate that the Federal Banking Agencies believe the institution is too troubled to qualify and submitted an application which was rejected. Treasury and the Federal Banking Agencies have been sensitive to these concerns.

3. What is the application process?

Qualifying institutions should review the Program information on the Treasury website and consult with their respective Federal Banking Agency. After this consultation, the institution should submit an application to that same regulator, which will be treated as confidential. If the applicant is a 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. In the application, the qualifying institution will indicate the amount of perpetual senior preferred stock investment it is requesting (which must be between 1% and 3% of risk weighted assets) which generally will be based upon information contained in the latest quarterly supervisory report filed by the applicant with its appropriate Federal Banking Agency. If an application is submitted before the Treasury publishes the investment agreement and the required ancillary documents, an applicant will have to submit an amended application providing updated responses to items that were based upon the prior review of these documents.

The application must be received by the appropriate Federal Banking Agency **no later than 5:00 p.m. (EST) on November 14, 2008**. Treasury has made clear that sufficient capital has been allocated so that all qualifying banks can participate. Therefore, the Program will not be implemented on a first-come-first-served basis. Additionally, all Federal Banking Agencies are using a standardized process to review all applications to ensure consistency.

Once an application has been reviewed, it will be sent to the Treasury along with a recommendation from the applicable Federal Banking Agency. The Treasury will give significant weight to these recommendations when deciding to make the capital purchase investment. If an applicant receives preliminary approval to participate in the Program from the Treasury, the institution will have 30 days from the date of notification to submit the investment agreements and related documentation and obtain any necessary board or shareholder approvals or resolve any other constraints. All completed transactions will be publicly announced within 48 hours of execution. However, the Treasury will not announce any applications that are withdrawn or denied.

4. How can institutions that are not publicly held participate?

The Treasury has indicated that the same application process described above will apply. However, the Treasury is still working on finalizing and publishing the required legal documents so private institutions and mutual and sub-chapter S organizations can participate as well on substantially similar economic terms as public institutions.

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5. What if an institution does not have sufficient preferred stock or common stock authorized to participate?

Assuming a class of “blank check” preferred stock has been authorized but is not sufficient, the Treasury has indicated that it will adjust the liquidation preference per share in order to complete the investment. However, if an institution does not have (i) a sufficient number of unissued shares of common stock to reserve for issuance upon the exercise of any warrants and/or (ii) a class of authorized preferred stock to issue the Treasury under the Program, please consult your legal counsel. Applicants may have to seek shareholder approval in order to adjust their capitalization in order to complete the investment. For example, while an institution will have 30 days following preliminary approval from the Treasury to obtain any required shareholder approval to authorize a class of preferred stock, this 30 day period may not be enough time. Additionally, if shareholder approval is necessary to increase the number of shares of common stock authorized or to issue the warrants under applicable stock exchange rules and the institution fails to obtain such approval, the exercise price for the warrant will be reduced by 15% of the original exercise price on each 6-month anniversary of the issue date of the warrants until shareholder approval is obtained (the maximum reduction would be 45% of the original exercise price). Qualifying institutions may want to consider beginning the shareholder approval process before submitting an application.

6. What is the purpose of the “shelf” registration statement and how does an institution file it?

The “shelf” registration statement is intended to register under the Securities Act the shares of senior preferred stock and the warrants that will be issued to the Treasury and the shares of common stock issuable upon any exercise of the warrants so that they are freely transferable. If you are a public institution and you file quarterly and annual reports with the SEC, you can probably use Form S-3 for your shelf registration statement. For institutions that are not publicly held, it is unclear what the requirements will be. Holding companies that are not publicly held may have to use Form S-1, which is much more detailed and involved. Under the federal securities laws, banks and savings institutions would not have to file a shelf registration statement for any securities it issues to the Treasury as such securities would be exempt from registration under the Securities Act. Please consult your securities counsel for more information.

7. When will an institution need to file a shelf registration statement?

The term sheet published by the Treasury describing the Program states that the shelf registration statement must be filed with the SEC as soon as practicable after the investment is made by the Treasury. Therefore, if you are a publicly held holding company, you can probably wait until you are sure that you will participate in the Program before beginning to prepare the registration statement. For holding companies that are not publicly held, it is unclear what the requirements will be. In either case, you should discuss this with your securities counsel and your accountants in order to determine how long it will take to prepare the registration statement and how much it will cost.

Please feel free to contact us with any questions you may have. We are available to meet with you and your management or your board to step through the Program and the application process.

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