

# CORPORATE AND SECURITIES LAW

## *Alert*

NEWS FOR THE CLIENTS AND FRIENDS OF BASS, BERRY & SIMS PLC

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## Treasury Announces TARP Capital Purchase Program

October 16, 2008

On October 14, 2008, the United States Treasury announced its voluntary capital purchase program pursuant to which Treasury will purchase up to \$250 billion of senior preferred shares from qualified financial institutions on standardized terms. A copy of the Treasury press release related to this program and the standardized terms detailed in the initial term sheet can be found on [Treasury's Web site](#). While many of the details of the program have yet to be released, the summary below highlights the key terms.

Under the program, qualified financial institutions (which include virtually all United States banks and bank holding companies) that are chosen by Treasury may sell preferred securities to Treasury in an amount equal to not less than 1% of the institution's risk-weighted assets and not more than the lesser of \$25 billion and 3% of its risk-weighted assets. To participate in the program, institutions must notify Treasury by 5:00 p.m. on November 14, 2008. Treasury will then determine which institutions will be allowed to participate after consultation with the appropriate federal banking agency.

The preferred shares, which will qualify as Tier 1 capital without restriction and be transferable by Treasury at any time, will rank senior to an issuer's common stock and pay a cumulative, quarterly dividend at a rate of 5% per annum until the fifth anniversary of the date of issue, and will reset to 9% per annum thereafter. If the preferred securities are issued by a bank which is not a subsidiary of a holding company, the dividend will be non-cumulative. The preferred shares will rank pari passu with existing preferred shares issued by the issuing financial institution, other than preferred shares which by their terms rank junior to any other existing preferred shares, and will rank senior to common stock.

The preferred shares will be non-voting, except for class voting rights on the issuance of shares that are senior; any amendment to the rights of the holders of the preferred shares; and any merger, exchange or similar transaction which would adversely affect the rights of the holders of the preferred shares. The shares may be redeemed after three years at par. Prior to that time, the shares can only be redeemed with the proceeds of an offering of Tier 1 qualifying perpetual preferred stock or common stock which results in aggregate gross proceeds to the issuer of not less than 25% of the issue price of the preferred shares. All redemptions, whether before or after the initial three year period, will be subject to approval of the issuer's primary federal banking regulator.

For as long as the preferred shares are outstanding, the issuer is prohibited from paying or declaring dividends on any junior preferred shares, preferred shares with equal ranking, or common shares unless all accrued and unpaid dividends for all past dividend periods (or in the case of non-cumulative preferred shares the latest completed dividend period) have been declared and paid in full. An issuer is also prohibited from repurchasing or redeeming any junior or pari passu preferred shares or common shares during periods dividends on the preferred shares are unpaid. During the initial three-year term, any increase in common dividends or repurchase of common shares or junior or pari passu preferred shares, must be approved by Treasury unless Treasury has transferred all of the preferred shares to third parties.

Issuers of the preferred shares will be required to promptly file a registration statement covering the preferred shares and take such other steps as Treasury may reasonably request to list the preferred shares on a national securities exchange.

Issuers participating in the program must comply with the executive compensation and corporate governance provisions of the Emergency Economic Stabilization Act of 2008 for the period during which Treasury holds equity or debt securities of the issuer. Compliance with these provisions includes: (1) certification by the issuer that the contracts of the chief executive officer, chief financial officer and three next highest paid executive officers do not encourage or reward unnecessary and excessive risk taking that threatens the value of the financial institution; (2) recovering or clawing back any bonus or incentive compensation paid to these top five executives based on statements of earnings, gains, or other criteria that later prove to be materially inaccurate; (3) amending existing compensation arrangements to eliminate excess parachute payments (as long as the preferred shares, warrants or common shares are held by Treasury) to these top five executives in the event of involuntary termination, bankruptcy, liquidation or receivership; and (4) agreeing not to deduct for tax purposes executive compensation in excess of \$500,000 for these top five executives. In addition, the issuer and the affected executive officers must grant Treasury a waiver from any claims that they have as a result of modifying or terminating these plans. For more information regarding Treasury's proposed guidelines and regulations on the executive compensation limitations visit [Treasury's Web site](#).

In addition to the preferred shares, issuers will be required to issue Treasury 10-year warrants to purchase shares of common stock having an aggregate market price equal to 15% of the preferred shares. The initial exercise price of these warrants, which will be subject to anti-dilution protection and will be immediately exercisable, will be the market price (based on a trailing 20-day trading average) of the common shares on the date that the preferred shares are issued. The exercise price is subject to downward adjustment in 15% increments every six months if shareholder approval is required to issue the warrants and underlying common shares and such approval is not received. Shareholder approval should only be required if the issuer does not have enough authorized but unissued shares of common stock or if the number of common shares to be issued exceeds 20% of the issuer's outstanding common shares at the time of issuance. The downward adjustment to the exercise price is capped at 45%.

The warrants are freely transferable; provided that, until the earlier of December 31, 2009 or completion by the issuer of a qualified public offering resulting in aggregate gross proceeds to the issuer in excess of the issue price for the preferred shares, Treasury will not transfer or exercise in excess of an aggregate of 50% of the warrants. Issuers are also required to promptly file a registration statement covering the warrants and the underlying shares of common stock and take such other steps as may be reasonably requested by Treasury to facilitate the transfer of the warrants

and underlying common shares, including applying for the listing of the common shares on a national securities exchange. Treasury has indicated that it will not exercise voting power with respect to the common shares.

In the event that the financial institution is no longer listed on a national securities exchange, or the consent of its shareholders to issue the common shares is not received if required within 18 months after the issuance date of the warrants, the warrants will be exchangeable, at the option of Treasury, for senior term debt or another economic instrument or security of the institution such that Treasury is appropriately compensated for the value of the warrant, as determined by Treasury.

As is evident in a review of the term sheet, there are many questions that must be answered with respect to the program and many details that need to be fleshed out. We expect that Treasury will be issuing guidelines on the program soon and we believe that many of these questions and details will be addressed in the guidelines.

Should you have any questions regarding this program, please feel free to contact Bob Thompson or Scott Holley with Bass, Berry & Sims PLC at (615) 742-6200.

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