

## Troubled Asset Relief Program & Temporary Liquidity Guarantee Program

Updated: April 15, 2009

On October 3, 2008, President Bush signed into law the Emergency Economic Stabilization Act (the "Act"). One of the most significant pieces of this legislation was the creation of the Troubled Asset Relief Program (TARP). The Act authorizes the Secretary of the Treasury to purchase up to \$700 billion of troubled assets from financial institutions.

On October 14, 2008, Treasury Secretary Paulson and President Bush announced the Capital Purchase Program (CPP), in which the first \$250 billion of the TARP would be used to purchase equity stakes in financial institutions. Approximately half of the CPP funds were used to purchase equity interests in eight of America's largest banks.

Also on October 14, 2008, the Federal Deposit Insurance Corporation (FDIC) announced the Temporary Liquidity Guarantee Program (TLGP). This new program is intended to strengthen confidence in the banking system by guaranteeing newly issued senior unsecured debt of financial institutions and by providing full deposit insurance coverage for non-interest-bearing transaction accounts of FDIC-insured institutions.

These programs have raised many questions for those working in the financial institution industry. In this communication, we hope to highlight the terms of each program and address many of the questions being asked.

This Accounting Insight discusses only key terms of each program. Each institution should obtain a complete understanding of each program's terms and conditions. Please see Appendix A for a list of helpful website links, or contact your relationship executive at Wipfli for more information.

### Capital Purchase Program Application Deadlines

<i>Public Institutions<sup>1</sup></i>	<i>Nonpublic C-Corp Institutions</i>	<i>S-Corp Institutions</i>	<i>Mutual Holding Companies and Subsidiaries</i>	<i>Mutual Institutions</i>
November 14, 2008	December 8, 2008	February 13, 2009	May 7, 2009	May 14, 2009

<sup>1</sup> Public institutions are defined as those (1) whose securities are traded on a national securities exchange and (2) required to file periodic SEC reports, such as the annual (Form 10-K) and quarterly (Form 10-Q) reports.

## Capital Purchase Program

Qualifying Financial Institutions (as defined in the CPP) are eligible to participate in the CPP. Generally, these financial institutions include U.S. banks and savings institutions and U.S. bank and savings and loan holding companies. Treasury Secretary Paulson has communicated that the CPP is available to healthy institutions that may have “plenty of capital to get through [the current market turmoil], but are not positioned to lend as widely as is necessary to support our economy.”<sup>2</sup> The U.S. Treasury will ultimately determine whether a financial institution is eligible to participate and how much will be allocated to each institution using the recommendation of that institution’s primary regulator.

### Key Updates:

- On October 31, 2008, the U.S. Treasury clarified the original CPP was available only to publicly traded institutions, which are defined as institutions (1) whose securities are traded on a national securities exchange and (2) required to file periodic reports, such as the annual (Form 10-K) and quarterly (Form 10-Q) reports, with the Securities and Exchange Commission.
- On November 17, 2008, the U.S. Treasury published a term sheet and deadline for public institutions that did not meet the definition above and other nonpublic institutions (collectively “nonpublic institutions”) who wish to participate in the CPP. These terms are discussed further below. Since the terms required the institution to issue preferred stock, institutions that have elected to be taxed under Subchapter S of Chapter 1 of the U.S. Internal Revenue Code (“S-Corp institutions”) could not participate under these terms.
- On January 14, 2009, the U.S. Treasury published a term sheet and deadline for S-Corp institutions who wish to participate in the CPP. These terms are discussed below.
- On April 7, 2009, the U.S. Treasury published three term sheets and a deadline for mutual holding companies and public and nonpublic mid-tier holding company subsidiaries of mutual holding companies who wish to participate in the CPP. The terms for public and nonpublic subsidiaries of mutual holding companies are consistent with the terms previously issued for other public and nonpublic institutions. The terms for mutual holding companies are consistent with the terms previously issued for S-Corp institutions. The various sections of this Accounting Insight have been updated to include discussion of the few significant differences applicable to mutual holding companies and their subsidiaries.
- On April 14, 2009, the U.S. Treasury published a term sheet and a deadline for mutual banks and savings associations (“mutual institutions”) who wish to participate in the CPP. These terms are consistent with the terms previously issued for S-Corp institutions and are included in the section on Subordinated Debentures.

<sup>2</sup> Statement by Secretary Henry M. Paulson, Jr. on Capital Purchase Program, October 20, 2008.

**Troubled Asset Relief Program & Temporary Liquidity Guarantee Program****Capital Purchase Program (Continued)**

All institutions that participate in the CPP must comply with the U.S. Treasury's rules and regulations regarding executive compensation and benefits. Generally, these conditions include the following<sup>3</sup>:

- The institution is not allowed to offer incentives to senior executives that would encourage unnecessary and excessive risks.
- The institution is prohibited from making golden parachute payments to senior executives.
- The institution is given a clawback provision whereby senior executive bonuses and other incentives based on earnings must be paid back to the institution if the reported earnings or other data used to calculate the bonuses prove to be inaccurate.
- The institution may not make bonus payments, with certain exceptions, to the most highly compensated employee or employees depending on the size of the institution.

***Preferred Stock (Public and Nonpublic Institutions)***

Those public and nonpublic institutions that wish to participate in the program may sell senior preferred stock (the "Stock") to the U.S. Treasury, which will be classified as Tier I capital for regulatory capital purposes. The total amount of the Stock must be at least 1% but not more than 3% of the institution's risk-weighted assets. This Stock, which is fully transferable, must be senior to common stock and not subordinate to any existing preferred stock.

- Institutions that do not have the necessary preferred stock authorized will likely have to hold a shareholder meeting to obtain appropriate authorization to issue this Stock.

Institutions that are not subsidiaries of a mutual holding company cannot redeem this Stock for the first three years except in certain cases where the institution has raised proceeds from a Qualifying Equity Offering (as defined in the CPP). After three years, the Stock may be redeemed by the institution in part or in whole at any time.

The Stock will pay cumulative quarterly dividends at a rate of 5% for the first five years and 9% thereafter. (Note: If the Stock is issued by a bank that is not a subsidiary of a holding company, the dividend will be noncumulative.) Dividend payments on and any repurchase of common and other preferred stock by the institution will be restricted unless all accrued and unpaid dividends are fully paid on the Stock. The owner of the Stock (that is, the U.S. Treasury) will have the right to elect two directors if dividends on the Stock have not been paid in full for six dividend periods (does not have to be consecutive periods).

- Since this is preferred stock rather than a debt instrument, the dividend payments will not be deductible for tax purposes.

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<sup>3</sup> For more information on the executive compensation limits, please visit the executive compensation page on the U.S. Treasury website (see Appendix A).

## Capital Purchase Program (Continued)

### *Preferred Stock (Public and Nonpublic Institutions)* (Continued)

For the first three years after the Stock is issued, the U.S. Treasury must consent to any increase in the dividend rate on the institution's common stock. For nonpublic institutions, after the third anniversary, the U.S. Treasury must consent to any increase in common dividends greater than 3% per year, and no dividends may be paid in common shares (for example, stock dividends and stock splits).

The U.S. Treasury must consent to any repurchase of common and other preferred stock before the third anniversary for public institutions and before the tenth anniversary for nonpublic institutions.

For nonpublic institutions, after the tenth anniversary, the institution will be prohibited from paying any common dividends or repurchasing any equity securities (including trust preferred securities) until all Stock held by the U.S. Treasury is redeemed or has been transferred to third parties. Nonpublic institutions also have certain restrictions on related-party transactions.

### *Common Stock Warrants (Public Institutions Only)*

In connection with the issuance of the Stock, public institutions must also issue to the U.S. Treasury common stock warrants that have a total market value equal to 15% of the Stock. These warrants are transferable, immediately exercisable, and will have an exercise term of ten years. The U.S. Treasury will agree not to exercise voting power with respect to common stock purchased through exercise of these warrants. If the institution is no longer traded or listed on a national exchange or the institution does not have the necessary common stock authorized to issue the warrants, the U.S. Treasury has the option to exchange the warrants for a senior debt instrument or another financial instrument with a fair value similar to the value of the warrants.

- Institutions that do not have adequate common stock authorized to cover these warrants will likely have to hold a shareholder meeting to obtain appropriate authorization for the additional shares.

### *Preferred Stock Warrants (Nonpublic Institutions Only)*

In connection with the issuance of the Stock, nonpublic institutions must also issue to the U.S. Treasury preferred stock warrants that have a total market value equal to 5% of the Stock. These warrants are transferable, immediately exercisable, and will have an exercise term of ten years (although the U.S. Treasury expects to exercise them immediately). The warrants will have an exercise price of \$.01 per share but must be redeemed at par value.

The preferred stock obtained through exercise of these warrants will pay dividends at 9% and cannot be redeemed until all of the Stock is redeemed. All other terms are similar to the terms of the Stock.

**Troubled Asset Relief Program & Temporary Liquidity Guarantee Program****Capital Purchase Program** (Continued)***Subordinated Debentures (S-Corp and Mutual Institutions)***

Those S-Corp and mutual institutions that wish to participate in the program may issue subordinated debentures (the “Debentures”) to the U.S. Treasury, which, for regulatory capital purposes, will be classified as Tier I capital if issued by a holding company and as Tier II capital if issued by a bank or savings association. The total amount of the Debentures must be at least 1% but not more than 3% of the institution’s risk-weighted assets. These Debentures, which are fully transferable, must be senior to common stock and any other class of equity. Debentures issued by a bank or savings association must be expressly subordinated to claims of depositors and to other debt obligations, with certain limited exceptions. Debentures issued by a holding company must be subordinated to senior indebtedness of the company, with certain limited exceptions.

S-Corp institutions cannot redeem these Debentures for the first three years except in certain cases where the institution has raised proceeds from a Qualifying Equity Offering (as defined in the CPP). After three years (and at any time for mutual institutions), the Debentures may be redeemed by the institution in part or in whole.

The Debentures will pay interest at a rate of 7.7% for the first five years and 13.8% thereafter. If the Debentures are issued by a holding company, interest payments may be deferred for up to 20 quarters; however, any unpaid interest shall cumulate and compound at the applicable interest rate in effect. Dividend payments on and any repurchase of common stock and other equity securities, including trust preferred securities, by the institution will be restricted unless all accrued and unpaid interest for past interest periods is fully paid on the Debentures. The owner of the Debentures (that is, the U.S. Treasury) will have the right to elect two directors if interest on the Debentures has not been paid in full for six interest periods (does not have to be consecutive periods).

- Since these are debentures rather than equity instruments, the interest payments will be deductible for tax purposes.

For the first three years after the Debentures are issued, the U.S. Treasury must consent to any increase in the dividend rate on the institution’s common stock or other capital instruments. After the third anniversary, the U.S. Treasury must consent to any increase in common dividends greater than 3% per year and any extraordinary dividends paid on deposit accounts (mutual institutions). No dividends may be paid in common shares (for example, stock dividends and stock splits). Notwithstanding these restrictions, U.S. Treasury consent will not be required for an increase in common dividends for S-Corp institutions proportionate to an increase in taxable income if the dividends are tax distributions to shareholders used to fund their individual tax payments.

The U.S. Treasury must consent to any repurchase of common and other equity securities before the tenth anniversary.

## Troubled Asset Relief Program &amp; Temporary Liquidity Guarantee Program

## Capital Purchase Program (Continued)

*Subordinated Debentures (S-Corp and Mutual Institutions)* (Continued)

After the tenth anniversary, the institution will be prohibited from paying any common dividends or repurchasing any equity securities (including trust preferred securities) until all Debentures are redeemed. Institutions also have certain restrictions on related-party transactions.

In connection with the issuance of the Debentures, institutions must also issue to the U.S. Treasury warrants to purchase additional subordinated debentures equal to 5% of the Debentures. These warrants are transferable, immediately exercisable, and will have an exercise term of ten years (although the U.S. Treasury expects to exercise them immediately). The warrants will have an exercise price of \$.01 per note but must be redeemed at par value.

The subordinated debentures obtained through exercise of these warrants will pay interest at 13.8% and cannot be redeemed until all of the Debentures are redeemed. All other terms are similar to the terms of the Debentures.

**Action Point:** While the deadlines for other institutions have already passed, mutual holding companies and subsidiaries of mutual holding companies must submit an application to the applicable regulatory agency by May 7, 2009. Mutual institutions must submit an application to the applicable regulatory agency by May 14, 2009. The application and other information on the CPP, including where to send the application, can be found on the U.S. Treasury website (see Appendix A).

**Action Point:** If your institution is a mutual holding company, a subsidiary of a mutual holding company, or a mutual institution and you believe there is even a remote possibility your institution would like to participate in the program, we recommend completing the application and sending it to the applicable regulatory agency. Applications may be withdrawn if an institution subsequently decides it does not wish to participate, but institutions will not be able to participate at all if they do not submit an application by the due date.

**Action Point:** Before participating in the CPP, we recommend carefully analyzing the effect the Stock or Debentures will have on the institution. This analysis should include the impact of the Stock or Debentures on current and future regulatory capital, shareholder equity, and earnings by considering factors such as how the capital will be leveraged; the tax impact of the dividend or interest payments; the effect the preferred stock or subordinated debenture warrants will have; and how the Stock or Debentures will be repurchased. For more information or help completing such an analysis, please contact your Wipfli relationship executive.

**Troubled Asset Relief Program & Temporary Liquidity Guarantee Program****Temporary Liquidity Guarantee Program**

The TLGP includes two separate programs of the FDIC: the Transaction Account Guarantee Program and the Debt Guarantee Program. See Appendix A for a link to the FDIC final rule and other helpful information included on the FDIC website regarding the TLGP.

***Transaction Account Guarantee Program***

Under the Transaction Account Guarantee Program, funds in non-interest-bearing transaction accounts at participating institutions are 100% guaranteed by the FDIC up to any amount until December 31, 2009. Non-interest-bearing transaction accounts are defined to also include Interest on Lawyers Trust Accounts (IOLTA) and negotiable order of withdrawal (NOW) accounts that carry an interest rate of 0.50% or less during calendar year 2009. All FDIC-insured institutions and most U.S. bank and savings and loan holding companies are eligible to participate and are automatically covered for the first 30 days.

An institution that did not wish to participate must have notified the FDIC by the extended deadline of December 5, 2008, that it elected to opt out of the program, in which case the unlimited insurance expired and the institution will not have to pay any fees.

If an institution did not opt out of this program, the institution will pay a 10-basis-point fee on balances in non-interest-bearing transaction accounts exceeding the existing \$250,000 deposit insurance limit effective as of November 13, 2008. This fee will be collected through the normal FDIC assessment process.

- If account balances from non-interest-bearing transaction accounts are swept into an interest-bearing or nondeposit account overnight, they will not be covered under this program. An exception to this rule applies to sweeps from non-interest-bearing transaction accounts into non-interest-bearing savings accounts (example, for Regulation D purposes)—such transfers will be guaranteed under the program.
- If an institution wanted to include NOW accounts with interest rates exceeding 0.50% in the Transaction Account Guarantee Program, the institution must have reduced the interest rate to 0.50% or less by December 31, 2008, and committed to maintain the interest rate at 0.50% or less through December 31, 2009.
- The FDIC has published a list of institutions that opted out of this program on its website.

## Troubled Asset Relief Program &amp; Temporary Liquidity Guarantee Program

## Temporary Liquidity Guarantee Program (Continued)

*Debt Guarantee Program*

All FDIC-insured institutions and most U.S. bank and savings and loan holding companies were eligible to participate in the Debt Guarantee Program and were automatically covered for the first 30 days. Under this program, the FDIC will guarantee all senior unsecured debt issued on or after October 14, 2008, through June 30, 2009, that has a stated maturity of more than 30 days or 1 month. Senior unsecured debt includes, but is not limited to:

- Promissory notes
- Commercial paper
- Unsubordinated unsecured notes
- U.S. dollar denominated certificates of deposit owed to an insured depository institution, an insured credit union, or a foreign bank
- U.S. dollar denominated bank deposits in an international banking facility of an insured depository institution or a foreign bank

The FDIC's final rules specifically exclude the following (see final rule for complete list):

- Convertible debt
- Unsecured portion of otherwise secured debt
- Certificates of deposit (not owed to another insured institution – see above)
- Deposits denominated in a foreign currency
- Revolving credit agreements
- Funds swept from other accounts
- Loans from affiliates

The guarantee will extend to the maturity date of the debt or June 30, 2012, whichever comes earlier. The guarantee is limited to 125% of the face value of senior unsecured debt that was outstanding as of September 30, 2008, and that was scheduled to mature before June 30, 2009. If, as of September 30, 2008, an institution did not have any unsecured debt outstanding or only had federal funds purchased outstanding, the guarantee is limited to 2% of consolidated liabilities as of September 30, 2008. The FDIC is also able to make exceptions to this limitation on a case-by-case basis. The calculated amount of senior unsecured debt must have been reported to the FDIC (even if the amount is \$0) via *FDICconnect* no later than December 5, 2008.

An institution that did not wish to participate must have notified the FDIC by the extended deadline of December 5, 2008, that it elected to opt out of the program, in which case the guarantee of senior unsecured debt expired and no fees will be assessed.

## Troubled Asset Relief Program & Temporary Liquidity Guarantee Program

### Temporary Liquidity Guarantee Program (Continued)

#### *Debt Guarantee Program* (Continued)

If an institution did not opt out of this program, the institution will pay an annual fee effective as of November 13, 2008, based on the face value of any guaranteed debt and the time to maturity (see table below). The entire amount of the assessment is calculated when the debt is issued and will be collected even if the debt is repaid prior to its scheduled maturity.

Debt with a maturity of:	Annualized assessment rate (basis points)
180 days or less	50
181 to 364 days	75
365 days or more	100

If an institution wished to issue nonguaranteed debt that would otherwise qualify for this guarantee, the institution must have made this election by December 5, 2008, and must pay a fee equal to 0.375% of the institution's debt guarantee limit. This fee may be used to offset assessments for future guaranteed debt issued prior to June 30, 2009.

- There are many rules and reporting requirements related to the Debt Guarantee Program. Each institution participating in the program should become familiar with these rules and other requirements by reading the final rule published by the FDIC. Please see Appendix A for a link to this rule and a link to the frequently asked questions (FAQ) which can help answer some of these questions.
- The FDIC has published a list of institutions that opted out of this program on its website.

## Concluding Thoughts

Although the deadlines have passed for other institutions, management of mutual holding companies and subsidiaries and mutual banks and savings associations should take some time to understand the Capital Purchase Program's terms and conditions to determine what, if any, action the institution should take. Wipfli will continue to monitor any developments that occur with all of these programs, and we will update this communication on our website as necessary. (See Appendix B for significant updates to this Accounting Insight.) If you have questions about any of the programs or subsequent updates to them, please contact your relationship executive at Wipfli.

## Contact Information

For more information, please contact:

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Or e-mail us at [WipfliFinancialInstitutionsPractice@wipfli.com](mailto:WipfliFinancialInstitutionsPractice@wipfli.com).

## Related Website Links

U.S. Department of the Treasury – Emergency Economic Stabilization Act page:

<http://www.financialstability.gov/>

Capital Purchase Program Term Sheets, Applications, and Other Information:

<http://www.financialstability.gov/roadtostability/CPAppdocs.html>

Executive Compensation Limitation Information:

<http://www.financialstability.gov/about/executivecompensation.html>

(NOTE: As of April 15, 2009, the U.S. Treasury posted the following statement on its website: “Treasury is in the process of drafting new and appropriate restrictions on executive compensation for financial institutions that are receiving assistance under the EESA.”)

FDIC – Temporary Liquidity Guarantee Program page:

<http://www.fdic.gov/regulations/resources/TLGP/index.html>

Temporary Liquidity Guarantee Program Final Rule:

<http://www.fdic.gov/news/board/08BODtlgp.pdf>

Temporary Liquidity Guarantee Program Frequently Asked Questions

<http://www.fdic.gov/regulations/resources/TLGP/faq.html>

## Significant Updates to This Accounting Insight

### *October 31, 2008*

- The U.S. Treasury clarifies in its press release HP-1247 that the Capital Purchase Program is only available to publicly traded institutions in its current form. Additional guidelines, terms, and deadlines will be provided for privately held institutions at a later date.

### *November 3, 2008*

- The FDIC announces in Financial Institution Letter (FIL) 125-2008 the deadline for opting out of either the Transaction Account Guarantee Program or the Debt Guarantee Program has been extended from November 12, 2008, to December 5, 2008. The FDIC also announces the form to opt out will be available on FDIC*connect* beginning November 12, 2008. In addition, the FIL notes the deadline for compliance with certain disclosure requirements is extended from December 1, 2008, to December 19, 2008.

### *November 14, 2008*

- Deadline for public companies to submit a CPP application to applicable regulatory agency.

### *November 17, 2008*

- The U.S. Treasury publishes a CPP term sheet and deadline for nonpublic institutions not covered under the original CPP term sheet. Nonpublic institutions have until December 8, 2008, to submit an application for CPP funds. The U.S. Treasury is still considering how the CPP will apply to S-corporation and mutual institutions since the updated term sheet does not apply to such institutions.

### *November 21, 2008*

- The FDIC publishes its final rule on the Temporary Liquidity Guarantee Program. Key changes from its interim rule include the following:
  - Senior unsecured debt does not include debt with a maturity of 30 days or less (for example, federal funds purchased).
  - An institution that did not have senior unsecured debt outstanding as of September 30, 2008, will use 2% of its liabilities outstanding to determine its debt guarantee limit.
  - IOLTAs and NOW accounts with an interest rate of 0.50% or less are covered under the Transaction Account Guarantee Program.
  - The fee assessed for debt guaranteed under the Debt Guarantee Program will range from 0.50% to 1.00% of the debt's face value depending on the time to maturity.

## Significant Updates to This Accounting Insight (Continued)

### *December 5, 2008*

- Deadline for financial institutions to opt out of the FDIC's Transaction Account Guarantee Program and/or Debt Guarantee Program.

### *December 8, 2008*

- Deadline for nonpublic companies to submit a CPP application to applicable regulatory agency.

### *January 14, 2009*

- The U.S. Treasury publishes a CPP term sheet and deadline for S-Corp institutions not covered under previous CPP term sheets. S-Corp institutions have until February 13, 2009, to submit an application for CPP funds if they have not already done so. The U.S. Treasury is still considering how the CPP will apply to mutual institutions.

### *February 13, 2009*

- Deadline for S-Corp institutions to submit a CPP application to applicable regulatory agency.

### *April 7, 2009*

- The U.S. Treasury publishes CPP term sheets and deadline for mutual holding companies and public and nonpublic mid-tier holding company subsidiaries of mutual holding companies. These institutions have until May 7, 2009, to submit an application for CPP funds if they have not already done so.

### *April 14, 2009*

- The U.S. Treasury publishes a CPP term sheet and deadline for mutual banks and savings associations not covered under previous CPP term sheets. Mutual institutions have until May 14, 2009, to submit an application for CPP funds if they have not already done so.