

UPDATE

News of Developments in the Financial Sector and Related Areas

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Banking Industry Continues to Consolidate

The banking industry continues to consolidate throughout the United States and in the State of Arkansas. The consolidation in banking occurs from a number of factors, with banks experiencing loan portfolio problems resulting in inadequate capital on one hand and the pricing of banks in acquisition transactions on the other hand. Recent published reports reveal that the averages for the top 123 transactions in the United States completed in the first half of this year had a price/earnings ratio of 28.67, with a price/book multiple of 2.17. On a national level, the FDIC reports that the number of insured institutions declined in the period from September 2001 through June 2004 from 9,702 insured institutions to 9,079 insured institutions or a decline of approximately 6.5%. During this same time frame, the FDIC reports that there were 343 new institutions created. Had the new institutions not been created, the decline in the number of insured institutions on a national level during this period would have been approximately 10%. The Arkansas State Bank Department reports that for the

period from June 30, 2000, through the period ending June 30, 2004, the number of state chartered banks declined from 148 to 120, or a decline of 19%. It is interesting to note that during this time frame, only 3 new state chartered banks were formed, which occurred in the year 2000, with no new denovo banks created since that time. Recent research published under the FDIC Future of Banking Study reflects that while the number of commercial banks declined by 29% from 1994 through 2003, the number of bank branches increased by 15% over the same period to almost 67,000. The study showed that despite consolidation, branches remained a valuable resource in helping banks generate fee income and possibly better manage their overhead expenses. Recent data published by the FDIC shows that the expansion of bank branching continues in place. The FDIC analysis of the mid-year 2004 data reflects that bank branch networks are generally associated with lower expenses, higher fee income and higher profitability. At the same time, the FDIC 2004 data shows that charter consolidation and out-of-state branching are leading to more highly concentrated deposit markets in a number of states and metropolitan areas which may restrict the ability of large institutions to acquire more branches given existing state and federal caps for deposit market share. Based on FDIC data, branching by large institutions is clearly exceeding the growth rate by smaller institutions. Arkansas remains among the highest states on a national level in the opening of new branches by insured institutions (both state and national banks), with a 12% increase for the three-year period beginning in 2001 and ending in 2004. In 2003 alone, there were 86 new branches by insured institutions, for an 8.4% increase.

Regulation of National banks by States

Earlier this year, the Office of the Comptroller of the Currency ("OCC") issued two final regulations relating to the preemption of state laws by federal law over national banks. The first regulation clarifies to the extent the operations of a national bank are subject to state laws and identifies the type of state laws that are preempted by federal law under the National Bank Act. The second regulation is directed toward the exclusive authority of the OCC under the National Bank Act to examine, supervise and regulate the affairs of a national bank. Because of the controversial nature of these two final regulations as to state versus federal regulation of national banks, a number of lawsuits are now pending by state regulatory authorities regarding the position taken by the OCC as reflected in these two final regulations, particularly in the area of preemption of corporate subsidiaries of national banks and the applicability of preemption of state laws relating to these corporate subsidiaries. The OCC has recently issued Interpretative Letter No. 1005 confirming that the OCC regulations concerning preemption of state laws do not preempt the provisions of the Uniform Commercial Code. The OCC has also issued Interpretative Letter No. 1006 confirming that state unclaimed property or escheat laws are not preempted. A bill has been introduced in the United States House of Representatives which would allow states to enforce consumer protection statutes such as fraud and unfair and deceptive practices laws and would not allow the OCC to apply the preemption to subsidiaries of national banks, such as mortgage loan companies.

Securities Activities of Banks

The Securities and Exchange Commission ("SEC") has delayed action until March 31, 2005 (and possibly later) on proposed Regulation B that delineates the securities activities banks may engage in without

registering as brokers. Information on proposed Regulation B is on the *Update* website at www.GWBinns.com by clicking on *Update Archives* in the August 2004 issue under the heading entitled *Securities Activities of Banks*. In a recent letter to the SEC, the Federal Reserve Board, Federal Deposit Insurance Corporation and the Office of the Comptroller of the Currency expressed their disagreement to the proposal by the SEC. Quoting directly from their letter: "*After carefully reviewing the Proposed Rules, we believe that the Proposed Rules reflect a profound misinterpretation of the language and purposes of the 'broker' exceptions in the GLB Act.*"

Cases, Releases and Rulings

President Bush recently signed into law the American Jobs Creation Act (the "Jobs Act") which increases the maximum number of shareholders for Subchapter S corporations from 75 to 100, and allows up to six generations of a family to be counted as one shareholder. The Jobs Act also lifts the current rules that prohibit banks from converting to Subchapter S corporations if any of their shares are held in individual retirement accounts.

The Federal Trade Commission and the Justice Department have announced their support in a letter urging the Massachusetts House of Representatives to adopt a bill that would enable nonlawyers to compete with lawyers in performing certain real estate closing services, taking the position that competition would lower prices and enable consumers to receive more convenient and better services. The bill, HB180, would amend the laws of Massachusetts to authorize nonlawyers to perform real estate closing services, such as drafting deeds, mortgages, leases and agreements, examining titles, issuing title certification of policies of title insurance and representing lenders as their closing agent.