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U P D A T E

News of Developments in the Financial Sector and Related Areas

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Noncumulative Perpetual Preferred Stock

A number of bank holding companies have issued trust preferred securities and continue to utilize trust preferred securities for a number of reasons. Bank holding companies may include trust preferred securities in tier 1 capital in an amount equal to 25 percent of all core capital elements (including trust preferred securities). Noncumulative perpetual preferred stock ("Perpetual Preferred") is an excellent alternative to bank holding companies that need tier 1 capital but are beyond the 25 percent trust preferred limitation. Although common stock should generally be the dominate form of tier 1 capital for a bank holding company, Perpetual Preferred qualifies as tier 1 capital. The issuance of Perpetual Preferred also increases the amount of trust preferred qualifying as tier 1 capital, in that for each $1 million of Perpetual Preferred issued, $333,333 of trust preferred securities in tier 2 become eligible for tier 1 capital. Perpetual Preferred may be issued at both the bank holding company level and the bank level in order to increase tier 1 capital. Because Perpetual Preferred is considered a separate class of stock, Subchapter S corporations are not eligible since they can only have one class of stock. A coupon payment on Perpetual Preferred is similar to trust preferred, and the issuer has the option to call the securities after five (5) years. Any redemption of Perpetual Preferred is subject to regulatory approval. Perpetual Preferred has no voting rights and is perpetual, meaning that it has no final maturity date. Quarterly dividends are subject to board approval and are noncumulative if not paid. Unlike dividends paid on trust preferred securities, dividends paid on Perpetual Preferred are not a tax deductible interest expense. Perpetual Preferred is an excellent vehicle for increasing tier 1 capital, maintaining shareholder ownership, funding acquisitions, stock repurchases and providing funds for internal growth. Our firm is available to answer questions on the benefits of issuing Perpetual Preferred and the placement of these securities with third parties.

Arkansas Usury Law

On January 9, 2003, the Federal Reserve Board ceased using the phrase "Federal Reserve Discount Rate" and began using the phrase "primary credit rate." At that time, the Attorney General of Arkansas issued Opinion No. 2002-334 concluding that the Federal Reserve Board's primary credit rate was equivalent to the Federal Reserve Discount Rate. In addition, in a Release dated January 9, 2003, by the

Federal Reserve Board regarding the term "Discount Rate," the release stated that because primary credit is the Federal Reserve's main discount window program, the Federal Reserve at times uses the term "Discount Rate" to mean the "primary credit rate". In *Pakay v. Davis*, WL 2884473 (2006), the Arkansas Supreme Court concluded that the Federal Reserve's primary credit rate would be applied in place of the Federal Reserve Discount Rate for purposes of construing the maximum legal rate of interest under the Arkansas Constitution. The facts reflect that Parkay entered into a contract for land providing for an 8% interest rate and contended that the contract was usurious since it exceeded the maximum interest rate permissible under Arkansas law of 7% (no more than 5% per annum above the primary credit rate of 2%). Davis, on the other hand, argued that there was no way to calculate what constitutes usury under the Arkansas Constitution since the Federal Reserve Board abolished the Federal Reserve Discount Rate on January 9, 2003. The Court had little trouble in holding that the primary credit rate should be applied in the place of the Federal Reserve Discount Rate in determining the maximum rate of interest under the Arkansas Constitution. A summary of cases regarding the Arkansas usury law is available on the ***Update*** web site at www.GWBinns.com under the heading entitled "Cases and Rulings."

Quarterly Banking Profile

The Federal Deposit Insurance Corporation ("FDIC") has issued its *Quarterly Banking Profile* reflecting the financial results for the third quarter of this year. The report reflects that past due loans and leases increased 6.9 percent during the third quarter. This is the second consecutive quarter that noncurrent loans have increased, and it is the largest quarterly increase since the third quarter of 2001. Noncurrent loans have increased in four of the last five quarters. The growth in past due loans occurred across a number of loan categories. Past due residential mortgage loans increased 5.3 percent, past due construction and development loans increased 33 percent and past due commercial and industrial loans increased 6.7 percent during the quarter. For the first time in three years, core deposits decreased during the quarter. At the same time, non-core deposits, which include deposits in foreign offices and time deposits in denominations of $100,000 or more, increased 3.2 percent during the quarter. Overall deposit growth failed to keep pace with the growth in industry assets reflecting a growing share of insured institutions' liabilities becoming more sensitive to changes in interest rates. The report is available on the website of the FDIC at *www.fdic.gov.*

Payday Lenders

In a report on payday lenders entitled *Financial Quicksand* by the Center for Responsible Lending findings were as follows:

- Ninety percent of payday lending revenue is based on fees from borrowers trapped in debt.
- The typical payday borrower pays back $793 for a $325 loan.
- Predatory payday lending now costs American families $4.2 billion per year in excessive fees.
- States that ban payday lending save their citizens an estimated $1.4 billion in predatory payday lending fees every year.
- States should consider capping annual interest rates on small consumer loans at thirty-six percent.

The report is available online at www.responsiblelending.org.