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U P D A T E

News of Developments in the Financial Sector and Related Areas

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Interstate De Novo Branching

On July 21, 2010 President Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act"). Section 613 of the Dodd-Frank Act amends the National Bank Act and the Federal Deposit Insurance Act to eliminate state law provisions that may bar de novo branching for non-domestic banks.

Prior to passage of the Dodd-Frank Act, de novo interstate branching across state lines was only permitted by those states which opted-in under the provisions of the Riegle-Neal Interstate Banking and Branching Efficiency Act (the "Riegle-Neal Act"). A majority of the states did not opt-in under the Riegle-Neal Act that permitted de novo interstate branching. In those states that did not opt-in, a bank could only enter those states through the acquisition of an existing bank which in most cases required the payment of a premium for the charter of the acquired bank.

The intent of Section 613 was to level the playing field in that thrift associations regulated by the Office of Thrift Supervision have had the authority to branch nationwide since 1992. Under the Dodd-Frank Act, the Office of Thrift Supervision will cease as a functioning regulator on July 21, 2011 and the responsibility for federal thrift associations will be assumed by the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation will assume the responsibilities over state savings associations. Another reason for the passage of Section 613 is based on the theory that federal banking regulators desired to have more competition in the various states in order to cut down on the excessive number of community banks that currently exist.

Section 613, by eliminating the opt-in requirement of the Riegle-Neal Act, will open the doors of more than twenty states that currently prohibit de novo interstate branching. Section 613 does limit the branching within a particular state to the laws of that specific state. However, in most cases banks can branch throughout their own state.

Section 613 will do away with the various legal devices utilized in the past by banks to enter states without acquiring a whole bank and paying a large premium. Some of those devices included the sale of assets and the assumption of deposits by one of two banks within the same bank holding company and then the sale of the naked bank charter stripped of its assets and its liabilities to the out of state bank. Another device was the sale and acquisition of a naked charter resulting from the merger of

two merging banks. Premiums for naked charters have exceed one million dollars in states such as Florida and the average price for a naked charter in Arkansas has generally been in the range of $250,000.

Section 613 will become effective on July 22, 2010. As a result of Section 613 there will likely be an increase in branches in border towns of contiguous states.

Consolidation in Banking

The banking industry continues to consolidate throughout the United States, but at a much slower pace than in the past two decades. Consolidation occurs from a number of factors with banks experiencing loan and securities portfolio problems resulting in inadequate capital on one hand and the pricing of banks in acquisition transactions on the other hand. The Federal Deposit Insurance Corporation ("FDIC") reports that the number of insured institutions has declined over 40% since 1992.

In some cases, depressed stock prices for publically traded financial institutions is a factor in the decline in merger and acquisition activity because there is less buying power by an acquirer with the result that a healthy institution is unwilling to accept a lower price. Probably the most significant factor in the decline is the closure of banks by the FDIC resulting in acquirers for banks purchasing the assets of the closed bank at a modest premium of the deposits, and the FDIC entering into a loss-sharing agreement with the acquirer on potential loan and asset losses. Because of FDIC closure of banks and the utilization of loss-sharing agreements, acquirers have in some cases either excluded or escrowed problem assets in making an acquisition of a healthy bank thereby leaving the risk of collection of the problem assets with the shareholders of the acquired institution.

Since 2007, merger and acquisition activity has continued to decline. Although there are still acquirers for banks, they are much more selective in the acquisitions that are being made. The FDIC reports that the number of institutions on FDIC's problem list has risen to 860, the highest since March 31, 1993, when there were 928. Problem institutions are characterized as those institutions having a risk of failing and being closed by the FDIC.

Prior to 2007 there had not been a bank failure since the second quarter of 2004. During 2007 there were three bank failures with the largest being NetBank located in Georgia with approximately $2.5 billion in assets and $2.3 billion in total deposits.

During 2008 there were twenty-six bank failures with the largest being Washington Mutual Bank located in Washington with approximately $307 billion in assets and $188 billion in deposits. During 2009, there were one-hundred forty bank failures with the largest being Colonial Bank located in Alabama with approximately $25 billion in assets and $20 billion in deposits. For the first eleven months of this year, there were one-hundred forty-nine bank failures with the largest being Western Bank Puerto Rico located in Mayaguez, Puerto Rico with approximately $11.9 billion in assets and $8.6 in deposits.

Probably the biggest issue facing banks during the coming year will be the ability to raise capital, not only for acquisitions but for credit quality issues relating to loan portfolios and securities portfolios. Banks will need to look for alternatives for capital, one of which would be the private placement of its equity, debt or hybrid (trust preferred and noncumulative perpetual preferred) securities with local investors, existing shareholders and major customers.

Our firm is available to answer questions regarding the benefits of issuing securities in a private placement.