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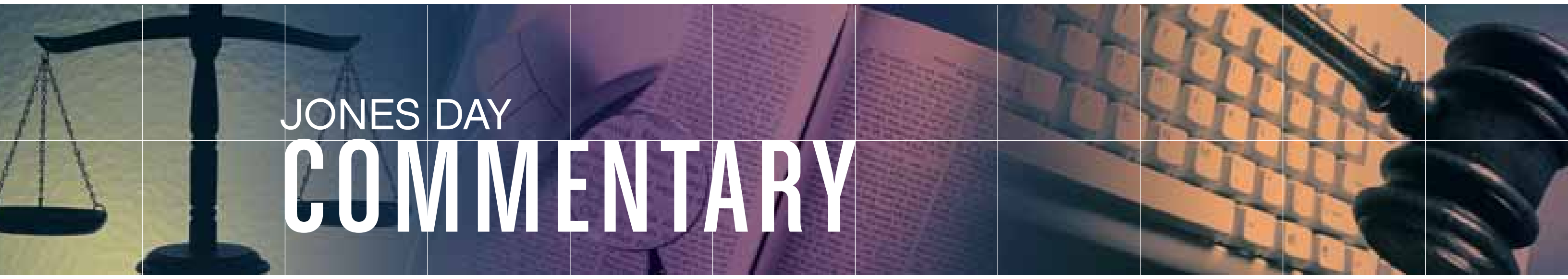

REVISED EXECUTIVE COMPENSATION REQUIREMENTS FOR PARTICIPANTS UNDER THE TROUBLED ASSETS RELIEF PROGRAM

On February 17, 2009, President Obama signed into law the American Recovery and Reinvestment Act of 2009 ("ARRA"), widely described as the Stimulus Bill.[1] ARRA significantly expands the executive compensation requirements previously imposed under the Emergency Economic Stabilization Act of 2008 ("EESA"), which established the Troubled Assets Relief Program ("TARP"), and by subsequent guidance issued by the U.S. Department of the Treasury. ARRA's executive compensation restrictions apply to any entity that has received or will receive financial assistance under TARP (a "TARP Recipient") and generally will continue to apply for as long as any obligation arising from financial assistance provided under TARP remains outstanding, other than government-held warrants (the "TARP Assistance Period"). The ARRA restrictions are not limited to recipients of the TARP Capital Purchase Program, and they have potentially broad application to anyone participating in any TARP program or the Financial Stability Plan announced on February 10, 2009, other than where participation is solely in connection with loan modification programs under Section 109 of EESA.

EESA Section 111 created different executive compensation restrictions depending on the nature of the assistance received by a TARP Recipient and provided broad, general rules that were fleshed out in subsequent guidance issued by the Treasury Department. As amended by ARRA, Section 111 provides a more comprehensive set of rules for all TARP Recipients. EESA's revised executive compensation requirements represent an amalgamation of some of EESA's prior

1. This is an updated version of our Commentary first published on February 15, 2009.

executive compensation requirements, prior Treasury guidance, and a number of the proposed executive compensation guidelines announced by the Treasury Department on February 4, 2009 (the "Treasury Guidelines"). ARRA left in place EESA's tax deductibility and excise tax provisions.

It remains to be seen what role or impact the Treasury Guidelines and prior guidance will have now that ARRA has become law. For example, the $500,000 annual compensation limit under the Treasury Guidelines for certain TARP Recipients was not included in ARRA. The Treasury Department could seek to impose that limit, or other limits, on future TARP Recipients as a condition to the receipt of further TARP assistance using the ARRA restrictions as a baseline. As a result, the next round of general guidance from the Treasury Department will be very important.

The revised executive compensation requirements are summarized as follows:

GENERAL STANDARDS

TARP Recipients must implement and comply with the following executive compensation and corporate governance standards during the TARP Assistance Period:

- Limits on compensation that exclude incentives for senior executive officers to take unnecessary and excessive risks that threaten the value of the TARP Recipient.
- A provision for the recovery by the TARP Recipient of any bonus, retention award, or incentive compensation paid to a senior executive officer and any of its next 20 most highly compensated employees based on statements of earnings, revenues, gains, or other criteria that are later found to be materially inaccurate. A TARP Recipient's "senior executive officers" are its five most highly paid executives whose compensation is required to be disclosed pursuant to the Securities Exchange Act of 1934 (the "Exchange Act") and its regulations (or, for nonpublic companies, comparable employees).
- A prohibition on the TARP Recipient making any golden parachute payment to a senior executive officer or any of its next five most highly compensated employees. A "golden parachute payment" is any payment for departure from a company for any reason, except for payments for services performed or benefits accrued.
- A prohibition on any compensation plan that would encourage manipulation of the reported earnings of the TARP Recipient to enhance the compensation of any of its employees.

BONUS, RETENTION AWARD, AND INCENTIVE COMPENSATION PROHIBITION

During the TARP Assistance Period, TARP Recipients are prohibited from paying or accruing any bonus, retention award, or incentive compensation (the "Bonus/Incentive Prohibition"). This Bonus/Incentive Prohibition does not apply to the payment or accrual of long-term restricted stock that:

- does not fully vest during the TARP Assistance Period;
- has a value not greater than one-third of the total amount of annual compensation of the employee receiving the stock; and
- is subject to such other terms and conditions as the Treasury Secretary may determine are in the public interest.

The Bonus/Incentive Prohibition applies to different employees of TARP Recipients based on the amount of financial assistance they receive under TARP:

- **Tier One**: Only the most highly compensated employee of a financial institution that received less than $25 million in financial assistance.
- **Tier Two**: *At least* the five most highly compensated employees of a financial institution that received at least $25 million but less than $250 million in financial assistance.
- **Tier Three**: The senior executive officers and *at least* the next 10 most highly compensated employees of a financial institution that received at least $250 million but less than $500 million in financial assistance.
- **Tier Four**: The senior executive officers and *at least* the next 20 most highly compensated employees of a financial institution that received $500 million or more in financial assistance.

If the Treasury Department determines it is in the public interest with respect to a TARP Recipient, the Bonus/Incentive Prohibition for Tiers Two, Three, and Four may apply to a greater number of employees. In the case of all TARP Recipients, the Bonus/Incentive Prohibition does not prohibit any bonus payment required to be paid pursuant to a written employment contract executed on or before February 11, 2009.

BOARD COMPENSATION COMMITTEE

TARP Recipients must establish a Board Compensation Committee that:

- is composed entirely of independent directors; and
- meets at least semiannually to discuss and evaluate employee compensation plans in light of an assessment of any risk posed to the TARP Recipient from such plans.

If the TARP Recipient's common or preferred stock is not registered under the Exchange Act and the TARP Recipient has received $25 million or less in financial assistance under TARP, these responsibilities are to be carried out by the TARP Recipient's board of directors.

LUXURY EXPENDITURES LIMITATION POLICY

Each TARP Recipient's board of directors must have in place a company-wide policy regarding excessive or luxury expenditures, as identified by the Treasury Department. The expenditures may relate to:

- entertainment or events;
- office and facility renovations;
- aviation or other transportation services; or
- other activities or events that are not reasonable expenditures for staff development, reasonable performance incentives, or other similar measures conducted in the TARP Recipient's normal course of business operations.

NONBINDING SHAREHOLDER VOTES ON EXECUTIVE COMPENSATION

Each TARP Recipient must permit a separate shareholder vote to approve the TARP Recipient's executive compensation, as disclosed in the TARP Recipient's Compensation Discussion and Analysis, related compensation tables, and other related material under the compensation disclosure rules of the Securities and Exchange Commission (the "SEC"), in any proxy or consent or authorization for an annual or other meeting of its shareholders during the TARP Assistance Period (a "Say on Pay Vote"). The Say on Pay Vote will not be binding on or overrule any decisions by the TARP Recipient's board of directors, will not create or imply any additional fiduciary duty on the part of the board, and will not restrict or limit the ability of the TARP Recipient's shareholders to make proposals for inclusion in proxy materials related to executive compensation. The SEC is to issue any required final rules and regulations related to the Say on Pay Vote requirement not later than one year after the date of enactment of ARRA.

REVIEW OF PRIOR PAYMENTS TO EXECUTIVES

The Treasury Department is to review bonuses, retention awards, and other compensation paid to the senior executive officers and the next 20 most highly compensated employees of each entity receiving TARP assistance before the date of enactment of ARRA to determine whether any such payments were inconsistent with the purposes of the revised executive compensation requirements or TARP, or were otherwise contrary to the public interest. If the Treasury Department makes such a determination, it is directed to seek to negotiate with the TARP Recipient and the subject employee for appropriate reimbursements to the federal government with respect to compensation or bonuses.

CERTIFICATION OF COMPLIANCE WITH REVISED EXECUTIVE COMPENSATION REQUIREMENTS

Each TARP Recipient's chief executive officer and chief financial officer (or their equivalents) must provide a written certification of the TARP Recipient's compliance with the requirements of revised Section 111 of EESA to the SEC in its annual filings required under the securities laws (or, in the case of a nonpublicly traded company, to the Treasury Secretary).

SECTION 162(M)

Each TARP Recipient is subject to the $500,000 compensation deduction limitation of Internal Revenue Code Section 162(m)(5). Because this Code provision is premised on government acquisitions of assets rather than government stock purchases, it is not clear how it will apply, if at all, to TARP Recipients.

OTHER PROVISIONS

TARP Recipients can repay any assistance they have previously received under TARP without any requirement that repayments be made from cash offerings of Tier I capital instruments, which are generally limited to common or preferred stock. Bank holding companies and FDIC-insured institutions will require prior approval from their bank regulators before redeeming any securities issued under TARP and will need to meet all regulatory capital requirements following any such redemption.

EFFECTIVENESS

There is no stated effective date for ARRA's executive compensation requirements. However, the Treasury Secretary is directed to promulgate regulations to implement the revised executive compensation requirements and the SEC is to issue final rules and regulations related to the Say on Pay Vote requirement.

LAWYER CONTACTS

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