Agency # 210.00

ARKANSAS STATE BANK DEPARTMENT

Rules and Regulations

Updated: January 25, 2017

ARKANSAS STATE BANKING BOARD

Position Number	Classification of Position	Entitled to Nominate	Incumbent	Term Expires
1	Bank Dept. Member	Bank Commissioner	Zach McClendon	12-31-2019
2	Arkansas Bankers Association Member	Bankers Association	Randy Scott	12-31-2020
3	Arkansas Bankers Association Member	Bankers Association	Gary Hudson	12-31-2018
4	Public Member	Governor	Gary Smith	12-31-2018
5	Public Member	Governor	David Leech	12-31-2021
6	Public Member	Governor	Lana Hampton	12-31-2018

LEGAL HOLIDAYS

The following are legal holidays for all purposes:

New Year's Day--January 1;

Robert E. Lee's Birthday--Third Monday in January;

Martin Luther King's Birthday--Third Monday in January;

George Washington's Birthday--Third Monday in February;

Memorial Day--the last Monday in May;

Independence Day--July 4;

Labor Day--First Monday in September;

Veteran's Day--November 11;

Thanksgiving Day--Fourth Thursday in November;

Christmas Eve--December 24;

Christmas Day--December 25.

Pursuant to A.C.A. § 1-5-101 it is provided that holidays falling on Saturday will be observed on the preceding Friday and holidays falling on a Sunday will be observed the succeeding Monday.

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The Arkansas Code of 1987, as amended
(including the Arkansas Banking Code
A.C.A. § 23-45-101 through A.C.A. § 23-50-110)
is accessed
Online
at
www.arkleg.state.ar.us

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www.banking.arkansas.gov

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ARKANSAS STATE BANK DEPARTMENT RULES AND REGULATIONS

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SECTION 1

STATE BANK DEPARTMENT - GENERAL PROVISIONS

46-101.1 - REQUESTS FOR DOCUMENTS (Reference A.C.A. § 23-46-101)

Requests for non-confidential documents may be made by filling out a request form provided by the department. Telephone requests may be accepted.

46-101.2 - FEES FOR COPIES PROVIDED PURSUANT TO REQUEST (Reference A.C.A. § 23-46.101)

Copies of documents provided pursuant to request from the public or in the case of subpoena (if the copies are of confidential records) will be provided based upon the following fee schedule:

- regular copies - $ .50 per page;
- certified copies - $1.00 per page;
- microfilm copies - $1.00 per page;
- faxed copies - $ .50 per page extra.

46-101.3 - CONFIDENTIAL OR NON-CONFIDENTIAL STATUS OF BANK DEPARTMENT RECORDS (Reference A.C.A. § 23-46-101)

A. The names of **stockholders of a bank or bank holding company** will not be regarded as confidential. The stockholder's list of a bank or bank holding company will not be regarded as confidential.

B. **Articles of Agreement and Incorporation** and all amendments are not confidential.

C. **Stock Transfers**. A one-page request form submitted to the Commissioner requesting a transfer of bank stock from one stockholder to another. **However, any information submitted to the** Commissioner, including any personal financial statements, along with the request will be regarded as confidential and is not subject to disclosure.

D. **Applications**. All applications submitted to the Commissioner may be disclosed to anyone with the exception that personal financial statements submitted in support of such applications shall be regarded as confidential and are not subject to disclosure.

E. **Examination Reports**. Examination reports are highly confidential and are not subject to public disclosure. Such examination reports are regularly submitted to the federal regulatory authorities and/or other state financial institution regulatory authorities, as well as to the examined bank as a matter of regulatory process. However, the examination reports remain the property of the Department and, as such, the report, as well as all correspondence between regulatory authorities and the examined bank in respect to the examination report, is confidential, A.C.A. § 23-46-101.

F. **Investigation Reports**. An investigation made by a bank examiner assigned to investigate the merits of an application, or other bank matter, is generally considered as confidential. The exception being that the Commissioner, in his/her discretion, reserves the right to permit an investigation on the merits of an application to be reviewed by the applicant and an official protestant to an application and permit introduction into evidence, by a party to the proceeding, those portions of the investigation which may be necessary and relevant to that proceeding.

G. **Corporate "File"**. A bank's corporate file contains the following: Articles of Incorporation, Amendments to Articles of Incorporation, Oaths of Directors, list of stockholders. The file is subject to disclosure with the exception of any information in support of a petition for a stock transfer since such supportive information is confidential.

H. **Financial Statements**. Personal financial statements shall not be exhibited to the public.

LEGAL HOLIDAY (BANK)

48-103.1. - LEGAL HOLIDAY; APPLICABLE LAW (Reference A.C.A. § 23-48-103)

The legal holidays applicable to state banks shall be those holidays set forth in A.C.A. § 1-5-101 and such other holidays as shall be established from time to time by the Board of Governors of the Federal Reserve System. A state bank is not required to close on any legal holiday. A bank may close one business day of each week in which event the day of such closing is deemed a legal holiday and not a business day. Business transacted on a holiday is binding and shall have the same effect as if transacted on the next succeeding business day. All items payable on a legal holiday shall be deemed to be payable on the day next succeeding the holiday.

46-203 - CERTIFIED COPIES AND CERTIFICATES OF GOOD STANDING FEES (Reference A.C.A. § 23-46-203)

Certified copies of records and papers furnished to an individual by the State Bank Department will be charged at a rate of $1.00 per page.

Certificates of Good Standing provided by the State Bank Department will be charged at $50.00 per certificate.

46-207.1 - INTEREST IN STATE BANKS; PARTICIPATION IN (Reference A.C.A. § 23-46-207)

State Bank Department employees, subject to A.C.A. § 23-46-207, may be a depositor in any financial institution the Department regulates and may participate in overdraft programs associated with such deposit relationships so long as participation in such programs are regularly offered as a customer service of the institution.

PROCEEDINGS BEFORE THE BOARD AND COMMISSIONER

46-304.1 – APPLICATIONS (Reference A.C.A. § 23-46-304)

The Commissioner and the State Banking Board rule that applications forms provided by the State Bank Department for various applications will request information required for submission of an application to the Board or the Commissioner. The Board and the Commissioner reserve the right to request additional information as necessary to consider an application.

46-305.1 – APPLICATIONS/DOCUMENTS (Reference A.C.A. § 23-46-305)

The Commissioner and the State Banking Board may permit applications and supporting documentation, or any other documents to be submitted to the State Bank Department in original paper document format, photographic format, or electronic format, which has been determined as acceptable by the Commissioner.

46-402.1 - MEETINGS OF THE BOARD; REGULAR MEETING DATES (Reference A.C.A. § 23-46-402)

Meetings of the State Banking Board will be held in offices of the State Bank Department, except in the case of meetings at which a large attendance is anticipated. In such a situation, the Commissioner will arrange for a meeting in outside quarters where a larger space is available.

Regular meetings of the Board may be scheduled four (4) times a year. These meetings will be held at 10:00 a.m. on the third Thursday of January, April, July, and October, but if, in the opinion of either the Commissioner or chairman of the State Banking Board, any necessitous reason exists for changing the date of a regular meeting, either said Commissioner or chairman may reset the meeting for a different date after giving notice as required in these regulations for the call of a special meeting. All meetings are public except when the members meet in executive session as permitted under the Arkansas Freedom of Information Act.

46.403.1. - PUBLICATION REQUIREMENTS. APPLICATIONS BEFORE THE STATE BANKING BOARD (Reference A.C.A. § 23-46-403)

Sponsors of the following applications must publish notice of the proposed application three (3) times at equal intervals in a newspaper of statewide circulation. Publication shall be as close as practicable to the date the application is filed with the State Bank Department, but no more than ten (10) calendar days prior to or after the filing date. Publications must provide for a fifteen (15) day comment period beginning with the actual filing of the application. These applications are:

(1) New state bank charters;

(2) Merger or consolidation applications between one or more banks, or saving and loan associations into a state bank;

(3) Purchase or assumption application (over 50% of the assets or liabilities) of another depository institution; and

(4) Change of a state bank's main banking office from one municipality to another (Simple or Complex Application).

46-404.1 - APPLICATION FILING FEES. APPLICATIONS TO BE PRESENTED TO THE STATE BANKING BOARD (Reference A.C.A. § 23-46-404)

Following is a list of application filing fees:

a)	New bank charter	$8,000
b)	Merger applications (per institution)	$5,000
c)	Conversion (national bank to state bank)	$8,000
d)	Conversion (stock savings and loan or federal savings bank to state bank)	$8,000
e)	Charter amendments	$ 200
f)	Charter amendments for trust powers	$ 500
g)	Purchase or assumption (over fifty percent (50%) of assets or liabilities of another depository institution)	$5,000
h)	Relocation of main office (from one municipality to another)(Application does not include any reorganization or change of bank business plans – must be simple relocation of address only)	$2,500
i)	Reorganization and Relocation of Bank Charter (Complex Application)	$6,500

46-404.2 - APPLICATION FILING FEES. APPLICATIONS WHICH ARE NOT FILED WITH THE STATE BANKING BOARD (Reference A.C.A. 23-46-404)

a)	New branch banking office (Expedited branch application) A.C.A. § 23-48-703	$ 300
b)	New branch banking office (Standard branch application) A.C.A. § 23-48-703	$ 500
c)	New branch banking office (Mobile branch application) A.C.A. § 23-48-703	$ 300
d)	Plan of exchange (plus expenses of Commissioner; does not include costs associated with appraisals of bank stock)	$ 500
e)	Filing of fictitious name	$ 25
f)	Filing of out-of-state bank/bank holding company	$ 300

g)	Change in Control	$5,000
h)	Purchase or Assumption (less than fifty percent (50%) of assets or liabilities)	$ 300
i)	Registered Agent for Service of Process A.C.A. § 23-48-327	$ 25

46-406.1 - HEARINGS. FILING FEES FOR WRITTEN/OFFICIAL PROTESTS (Reference A.C.A. § 23-46-406)

a) A filing fee of $2,500 will be required to file an official protest for the following applications:

1) New bank charter;
2) Merger application;
3) Purchase or assumption (over fifty percent (50%) of assets or liabilities);
4) Conversion (national to state bank);
5) Conversion (stock savings and loan or federal savings bank to state bank);
6) Relocation of main office (from one municipality to another)(Simple Application); and
7) Reorganization and Relocation of Bank Charter (Complex Application).

b) A filing fee of $500 will be required to file an official protest for a new branch banking office application (standard branch application) (A.C.A. § 23-48-703).

c) A filing fee of $300 will be required to file an official protest for the following applications:

1) Purchase or Assumption (less than fifty percent (50%) of assets or liabilities;
2) New branch banking office application (expedited branch application) A.C.A. § 23-48-703; and
3) New branch banking office application (mobile branch application) A.C.A. § 23-48-703.

46-406.2 ADJUDICATIVE HEARINGS BEFORE THE STATE BANKING BOARD AND/OR THE COMMISSIONER (Reference A.C.A. § 23-46-406)

The following rules shall apply to adjudicative hearings before the State Banking Board and/or the Commissioner:

(a) Public Hearing at Commissioner's Discretion. The Commissioner at his/her discretion, regardless of whether any formal protest or letters of opposition were filed, may hold a hearing on an application.

(b) Decision Maker.

1) Matters Before the State Banking Board. When an adjudicative hearing is conducted before the State Banking Board, the Board Chairman will conduct the hearing. The State Banking Board, collectively, will act as the decision maker.
2) Matters Before the Commissioner. When an adjudicative hearing does not involve the State Banking Board, the Commissioner reserves the right to act as decision maker or have a decision maker appointed. In the event the Commissioner decides to act as the decision maker, but is unable to conduct the hearing, a Deputy Commissioner will conduct the hearing. In the event the Commissioner decides to have a decision maker appointed, a list of five (5) potential decision makers will accompany the notice of the hearing sent to the parties entitled to notice by mail. This list will be compiled by the Commissioner. All parties will receive the same list of five (5) potential decision makers. Two (2) potential decision makers are to be chosen from the list and communicated by facsimile or hand delivery to the Commissioner within two (2) business days of receipt. The Commissioner may authorize an employee of the Arkansas State Bank Department to be served in the event of hand delivery. The Commissioner will then choose a decision maker to conduct the hearing from those potential decision makers submitted by the parties receiving notice by mail. The Commissioner will choose a decision maker from those submitted, even if not all parties submit decision makers. If no parties submit potential decision makers to the Commissioner, the Commissioner will choose a decision maker from the original list sent with the notice.

(c) Hearing Procedures. For the purpose of the actual hearing, the following rules will govern:

1) The decision maker may rule on motions, require briefs, and issue such orders as will ensure the orderly conduct of the proceedings;
2) All objections must be made in a timely manner and stated on the record;
3) Subject to terms and conditions prescribed by the Administrative Procedure Act, parties have the right to introduce evidence on issues of material fact, cross-examine witnesses as necessary for a full and true disclosure of the facts, present evidence in rebuttal, and, upon request of the decision maker, may submit briefs and engage in oral argument;
4) The decision maker is charged with maintaining the decorum of the hearing and may refuse to admit, or may expel, anyone whose conduct is disorderly; and
5) The hearing will be held in accordance with the Administrative Procedure Act.

(d) Order of Proceedings. The decision maker will conduct the hearing in the following manner:

1) The decision maker will give an opening statement, briefly describing the nature of the proceedings;
2) The parties are to be given the opportunity to present opening statements;
3) The parties will be allowed to present their case in the sequence determined by the decision maker;
4) Each witness must be sworn or affirmed by the decision maker, or the court reporter, and be subject to examination and cross-examination as well as questioning by the decision maker. The decision maker may limit questioning in a manner consistent with the law; and
5) When all parties and witnesses have been heard, parties may be given the opportunity to present final arguments.

(e) Court Reporter. In the event of a hearing before the State Banking Board and/or the Commissioner, the Arkansas State Bank Department will arrange for a court reporter to be present for the hearing. The applicant will be responsible for paying the costs of the court reporter appearing at the hearing and for copies of the transcript. The applicant will provide a copy of the transcript, free of charge, to the Arkansas State Bank Department.

(f) Order of Decision Maker. The decision maker will issue an oral ruling at the conclusion of the hearing or a letter opinion within a reasonable time after the conclusion of the hearing. The prevailing party will then have ten (10) days from the date of the oral ruling or letter opinion to prepare and submit a written order to the Commissioner and the opposing party(s). Upon receipt of the written order by the Commission, the opposing party(s) will then have ten (10) days to object to the form or precedent.

(g) Expiration of Approval. The decision maker's Order approving and application shall expire eighteen (18) months from the date of the approval. Upon written request, the Commissioner may approve an extension of the eighteen (18) months.

46-407.1 - REHEARING MODIFICATIONS (Reference A.C.A. § 23-46-406)

The State Banking Board and the Commissioner take the position that until the Findings of Fact, Conclusions of Law, and written decision have been served on the parties, the Board has the power to reverse, modify, or rehear a decision formerly reached.

46-509.1 – ASSESSMENT FEES (Reference A.C.A. § 23-46-509)

The State Banking Board and the Bank Commissioner require that assessment fees payable on a semi-annual basis to the State Bank Department be remitted by automated processing as established by the Bank Commissioner. Exceptions for payment of assessment fees by any other method than the automated method established by the Department must be upon prior request and approval by the Bank Commissioner. Exception requests will only be approved on an extraordinary basis.

46-511.1 - BANK RETENTION OF RECORDS (Reference A.C.A. § 23-46-511)

Arkansas state banks are required to maintain the following records permanently:

a) Minute books of meeting of stockholders and directors; and

b) Capital stock ledger and capital stock certificate ledger or stocks.

All records, other than those described in part a) and b) shall be retained as follows:

Examination reports	permanent
Call reports	permanent
General ledger	permanent
Accounts payable	7 years

GENERAL

Customer relationship contract, after closing	
Signature cards	10 years
Loan applications - Consumer	25 months
Loan applications – Business	12 months
Overdraft loan agreement	6 years
Safe deposit agreement	10 years
Night depository agreement	1 year
Financial activity records	
Deposit tickets	10 years
Buy/sell orders for securities (after maturity)	3 years
Withdrawal receipts	10 years
Cash letters	1 year
Stop payment orders	6 years
Safekeeping receipts	7 years
Wire transfer receipts	6 years
Safe deposit access records	7 years
Accounting records of financial activity	
Transaction journal	7 years
Note and discount register	10 years
Draft register	10 years
Dividend Checks	10 years
Reconciliation record of account activity	
Customer statements	6 years
Checks paid	7 years
Supporting and specialized documentation	
Collateral records or receipts	10 years
Amortization records	to maturity
Credit files	6 years
Account analysis records	3 years

Proof sheets .... 3 years
Overdrafts .... 4 years
Trial balance .... 4 years
Return or exception items .... 5 years
Transit letters .... 3 years
1099 forms .... 5 years

DEPOSITS

Evidence of compliance with Electronic Funds Transfer Act .... 2 years

Currency transactions over $10,000 reports .... 5 years

Exemption reports and written statements for currency
Transactions over $10,000, after removal from exemption list .... 5 years

Taxpayer identification records for certificates of deposit,
After redemption .... 6 years

Signature cards for deposit accounts verifying identity of signer .... 10 years

Statements or ledger cards for deposit accounts .... 6 years

Checks, drafts, and money orders over $100 except for accounts
Which average 100 checks per month and fall into one of these
Categories; payroll, dividend, employee benefit, insurance claims,
Medical benefits, government agency, brokers or dealers in
Securities, fiduciary accounts, pension or annuity checks, and
Checks drawn on other financial institutions .... 6 years

Certificates of deposit records, purchased .... 5 years

Certificates of deposit records, redeemed .... 10 years

Deposit slips or credit tickets for transactions over $100
that identify amount of currency transacted .... 10 years

LOANS

GENERAL
Credit extension records for transactions over $10,000,
excluding real estate required by the Bank Secrecy Act
(formerly $5,000) .... 5 years

COMMERCIAL
Standby letters of credit records (Regulation H) .... Not specified

INSTALLMENT/CONSUMER

Credit evaluations required by Equal Credit Opportunity Act and Regulation B, after notification or final disposition

- Consumer ....25 months
- Business..12 months

Evidence of Compliance with Consumer Credit Protection Act Title IX for EFTS services .... Until final disposition

Evidence of compliance with Truth in Lending requirements (Regulation Z), after disclosure.................................3 years

INVESTMENTS

Municipal securities deal transactions records. Forms MSD4 and Forms MSD5 (Regulation H), after disclosure ....3 years

Broker/deal transactions and commission records, customer account records and related correspondence.................................3 years

Credit information relating to public and investment securities ....3 years

Records of lost or stolen securities.................................3 years

Transaction records for brokers and dealers extending credit (Regulation T) ....3 years

TRUST

Fiduciary records, after termination of account or settlement of litigation................................. permanent

Investments of each trust account shall be kept separate from the assets of the bank ....10 years

OTHER RECORDS NOT SPECIFIED................................. 6 years

All records as noted in Act 89 of 1997 may be retained by photographic or other reproduction methods in lieu of retention of original records.

48-310.1 - APPEAL OF COMMISSIONER DECISION ON MINIMUM CAPITAL REQUIREMENTS TO STATE BANKING BOARD (Reference A.C.A. 23-48-310)

A state bank may appeal an order of the Commissioner to increase its capital stock to the Arkansas State Banking Board. Notice of the bank's request for appeal must be served upon the Commissioner and the members of the State Banking Board by personal service or certified mail within ten (10) days of the date the Commissioner's order was issued. A public hearing on the appeal will be held as soon as practicable by the State Banking Board. Notice of the hearing will be given twenty (20) days prior to the date of the hearing stating the time, date, and location of the hearing. Notice will be provided by United States mail to the parties to the appeal and published one time in a newspaper of statewide circulation. The bank requesting such an appeal will be required to provide a court reporter and transcript of the hearing to the Arkansas State Banking Board free of charge.

SECTION 2

GENERAL POWERS OF BANKS

47-101.1. - WAREHOUSING MORTGAGES AND OTHER LOANS (Reference A.C.A. § 23-47-101)

A.C.A. § 23-47-101(a)(14)permits state banks "to warehouse or act as agent in warehousing mortgages and other loans;". The aggregate of mortgages or other loans shall not be applied against the legal lending limit if the state bank is acting as agent in warehousing mortgages or other loans for a subsidiary.

47-101.2 - INCIDENTAL POWERS (Reference A.C.A. 23-47-101)

A.C.A. §23-47-101(b) reads: "In addition to the foregoing, a bank may exercise any other powers which are incidental to the business of banking." This statutory reference to incidental powers is very similar to the National Banking Act. The Commissioner and the Banking Board may give consideration to the interpretations of similar words in the National Bank Act by the Comptroller of the Currency, but shall not utilize this section to permit the exercise of any power or performance of any activity which is beyond the reasonable progression of the business of banking as authorized in the Arkansas Code.

47-101.2(a) GIFT CARD DISCLOSURES (Reference OCC Bulletin 2006-34).

The State Banking Board, pursuant to Act 304 of 2007, adopts the following guidance on disclosure and marketing issues for the sale of gift cards issued by the Office of the Comptroller of the Currency, August 14, 2006:

PURPOSE AND SCOPE

This bulletin is intended to provide guidance to national banks on a number of disclosure and marketing issues presented by gift cards, so that national banks that issue gift cards do so in a manner in which both purchasers and recipients of gift cards are fully informed of the terms and conditions of the product.[1]

BACKGROUND

A gift card is a type of prepaid or stored value card that is designed to be purchased by one consumer (purchaser) and presented as a gift to a second consumer (recipient).[2] The terms and

[1] This bulletin is limited to particular disclosure matters relating to bank-issued gift cards. It does not address other supervisory issues relating to these products or to other types of "prepaid" or "stored value" card products.
[2] In this regard, gift cards differ from payroll cards, travel expense cards, and other types of prepaid card products that are not designed to be marketed as a gift from one consumer to another.

conditions of different gift card products can vary significantly, but gift cards are generally divided into two main categories: retail gift cards and bank-issued gift cards. A retail gift card is typically offered by a major retail, entertainment, or food service company, to be used at establishments owned and operated by that company. A bank-issued gift card is typically issued by a financial institution, carries the logo of a payment card network such as VISA, MasterCard, or American Express, and can be used at the various locations that accept cards from that network.[3]

A bank-issued gift card is typically a bank product, and not merely an arrangement through which a third party can facilitate the use of its product in a payment card network. When a gift card is a bank product, the consumer's agreement is with the bank, and the gift card and the related disclosures, the cardholder agreement, and other documentation will specifically identify the bank as the issuer of the card. In addition, the bank generally will establish and impose the fees and other terms associated with the card and control the net proceeds of such fees; will be the party with the financial responsibility to merchants that honor the card; and will hold for its own account, or for the account of the consumer, the pool of funds used to pay merchants when consumers present gift cards to pay for goods or services.[4]

Industry studies and medial reports suggest that the gift card market is growing rapidly, and will continue to do so over the next several years. This rapid growth – together with the diversity of fees and other terms and conditions among different gift card products – shows that it is important for national banks that offer these products to adopt sound disclosure practices to help ensure that consumers understand the gift card products they are purchasing and using.

CONSUMER DISCLOSURES

Because the purchaser and the recipient of a gift card typically are not the same person, gift cards present unique disclosure challenges. In particular, providing disclosures to a gift card purchaser may not be sufficient to avoid compliance and reputation risks related to misunderstanding by a recipient about material costs, terms, and conditions of the gift card. In these circumstances, the OCC expects national bank gift card issuers to take appropriate actions to ensure that critical information is provided in a form that is likely to be readily available to recipients, as well as purchasers, of gift cards. Accordingly, with respect to gift cards that are bank products, the OCC would expect to see the following disclosures:

- <u>Disclosures on Gift Cards.</u> Basic information that is most essential to a gift card recipient's decisions about when and how to use the cars should be provided on the gift card itself, or on a sticker or tape affixed to the gift card. In light of the terms and provisions of most bank gift cards, this information generally will include disclosures relating to the following matters:

[3] As in the case of credit cards, bank-issued gift cards may be co-branded and offered through, or jointly with, a retailer or other company such as a retail shopping mall, but these cards generally have the same broad acceptability as other bank cards.

[4] In connection with the gift card, the bank would be subject to the prohibition against unfair or deceptive acts or practices in the Federal Trade Commission Act, 15 USC 45(a)(1), and to all other requirements applicable to bank products.

  - The expiration date of the card (which, consistent with existing practices for credit and debit cards, should be presented clearly on the front of the card);

  - The amount or the existence of any monthly maintenance, dormancy, usage, or similar fees; and

  - How consumers may obtain additional information about their cards or other customer service (for example, by providing a toll-free number or Web site address).

- <u>Disclosures Accompanying Gift Cards.</u> Other information that is important to a gift care recipient's decisions and actions should be provided in a form that is designed to be passed on with the card to the recipient, and issuers should encourage card purchasers to provide this information to gift card recipients. For example, the card could be carried in promotional packaging that contains this material information, or inserted into a sleeve that sets forth or is attached to these disclosures. Depending on the terms of the gift card product, this information may include:

  - The name of the bank that issued the card;

  - Any other fees that may apply to the card, including card replacement or reissuance fees, balance inquiry fees, foreign currency conversion fees, and cash redemption fees, and how they will be collected (for example, by debits to the card balance);

  - Whether and how consumers can receive a replacement card in the event that their card is lost or stolen, the information that consumers need to retain in order to do so, and responsibility for unauthorized transactions;

  - Where the card can be used, including, if applicable, suggestions for using the card as gas stations, hotels, restaurants, or other locations that may seek payment authorization in an amount greater than the consumer's actual purchase;

  - The issuer's obligation to authorize transactions through use of the card, and examples of the circumstances under which it may refuse to do so;

  - The importance of tracking the balance remaining on the card;[5]

  - Whether, and if so, how the card may be used in "split payment" transactions (when the card is used in conjunction with another form of payment) and the process for redeeming *de minimis* remaining balances:

  - How consumers can resolve problems and complaints and receive balance and other information about their cards; and

[5] Some gift card issuers provide a simple chard, similar to a checking account register, for gift card recipients to use to track their purchases and remaining balances.

- When applicable, the issuer's ability to revoke or change the terms of the gift card agreement.

PRACTICES TO AVOID

National bank gift card issuers should take appropriate steps to avoid engaging in marketing or promotional practices that could mislead a reasonable consumer about the terms, conditions, or limitations of the bank gift card product they are offering. For example, issuers should not advertise a gift card as having "no expiration date" if monthly service or maintenance fees, dormancy fees, or similar charges can consume the card balance and thereby have the same practical effect as an expiration date. Similarly, if such fees may consume the card balance before the stated expiration date for the card arrives, disclosures relating to that expiration date (other than the disclosure on the front of the card) should explain that possibility. Issuers also should generally avoid describing gift card products in terms suggesting that they are similar to gift certificates or other payment instruments with which consumers may be more familiar, or as products that carry federal deposit insurance when such insurance does not apply.

47-101.3. – WILD CARD STATUTE (Reference A.C.A. § 23-47-101)

Pursuant to the power granted to the Commissioner by A.C.A. §23-47-101(c), the Commissioner, by written order, may authorize state banks to engage in any banking activity then permitted to national banks. Such authority may be subject to such conditions and restrictions as the Commissioner may determine to be appropriate, whether or not any such conditions or restrictions are applicable to national banks.

47-101.4. - DISPOSITION OF INCOME FROM THE SALE OF CREDIT LIFE INSURANCE OR DEBT CANCELLATION CONTRACTS (Reference A.C.A. § 23-47-101)

(a) Individual employees, officers, directors, and principal shareholders of a state bank shall not personally profit by retaining commissions or other income (including experience rating credits and other rebates, but not including any portion of a premium required to cover the underwriting risk) from the sale of credit life, health and accident, and mortgage life insurance ("credit life insurance") or debt cancellation contracts to the institution's loan customers. However, employees and officers may participate in a bonus or incentive plan based in whole or in part on sales of credit life insurance or debt cancellation contracts under which payments the state bank in any year may not exceed 5% of the recipient's annual salary. Alternatively, bonuses paid to any individual during the year for sales of credit life insurance or debt cancellation contract may not exceed 5% of the average salary of all loan officers participating in the plan. Payments may not be made to employees and officers more frequently than quarterly.

(b) Income derived from the sales of credit life insurance or debt cancellation contracts to loan customers shall be credited to the income accounts of the state bank and not to the individual employees, officers, directors, or principal shareholders, their interests, or other affiliates. However, such income may be credited to an affiliate operating under the Bank

Holding Company Act or to a trust for the benefit of all shareholders, provided that the state bank receives reasonable compensation in recognition of the role played by its personnel, premises and goodwill in credit life insurance and debt cancellation sales. As a general rule, "reasonable compensation" means an amount equivalent to at least 20% of the affiliate's net income attributable to the state bank's credit life insurance or debt cancellation sales.

(c) Where other legal considerations preclude a bank from using a particular procedure for selling credit life insurance or debt cancellation contracts or from disposing of the income in a particular manner, a state bank that wishes to provide this service to its loan customers shall seek and utilize an alternative method that complies with (a) and (b) above.

(d) The distribution to shareholders of income derived from the sale of credit life insurance and debt cancellation contracts shall be accomplished through a declaration of dividends in conformity with law, rule, regulation and prudent financial practices.

(e) Nothing in this section shall be construed to prohibit a bank employee, officer, director, or principal shareholder who holds an insurance agent's license from agreeing to compensate the bank for the use of its premises, employees, and goodwill; provided, that all income directly received by such employee, officer, director, or principal shareholder from this activity is remitted to the bank as compensation.

RIGHT OF BANK TO EXECUTE GUARANTY

47-101.5. - GUARANTIES (Reference A.C.A. § 23-47-101)

A state bank is not authorized to be an accommodation guarantor. An accommodation guaranty by a state bank is void and ultra vires. A state bank can execute a valid guaranty agreement if such action is necessary or advisable to protect an economic interest of the bank. In Bank of Morrilton v. Skipper, Tucker & Co., 165 Ark. 49, the bank executed an agreement guaranteeing the payment of certain liabilities by one of its customers. The purpose of the guaranty was to enable the customer (who was indebted to the bank) to collect funds under an improvement district contract that would enable the customer to pay the debt to the bank. The case was remanded for a new trial; but the Supreme Court recognized that a guaranty executed for the purpose stated would be binding on the bank. In Wasson v. American Can Co., 189 Ark. 354, the bank guaranteed the payment of certain drafts by one of its customers that owed it about $3,000. The guaranty by the bank was intended to enable the customer to purchase cans for tomato canning purposes and the intention of the bank was that this guaranty would enable the customer to continue business operations and pay part or all of the indebtedness to the bank, held that this guaranty was to protect an economic interest of the bank and was binding on the bank. The same principle of law was recognized in Citizens Bank of Booneville v. Clements, 172 Ark. 1023. See also Merchants & Planters Bank & Trust Company v. Deaton, 200 Ark. 828; also Nakdimen v. First National Bank, 177 Ark. 303.

47-101.6 - COMPUTER SERVICES BY BANK OR OPERATING SUBSIDIARY (Reference A.C.A. § 23-47-101)

Any state bank, with the approval of the Commissioner, and so long as national banks are so authorized, may furnish computer, data processing, item processing, billing and posting services through its own organization or an operating subsidiary pursuant to A.C.A.§ 23-47-601 (and without the necessity of becoming a stockholder of a Bank Service Company) to other banks, and to non-banking customers who are its depositors.

MESSENGER SERVICE

47-101.8 - MESSENGER SERVICE (Reference A.C.A. § 23-47-101)

(a) To meet the requirements of its customers, a state bank may provide messenger services within the geographic limits of its operations by means of an armored car or otherwise, under which messenger service:

(1) funds may be picked up by the messenger and transmitted to the bank for deposit; and

(2) funds may be transmitted by the bank to its customer by messenger.

(b) The messenger service shall be pursuant to a written contract between the bank and the customer wherein it is agreed that in performing the functions under both (a)(1) and (a)(2) above, the messenger is the agent of the customer; that where funds (including currency, coin, checks or similar items) are transmitted to the bank by messenger for deposit, title to the funds shall remain with the customer until they are accepted by a teller of the bank at its banking house or any branch, and the depositor relationship shall not commence until such acceptance; that funds delivered by the bank to the messenger for transmission to a customer shall become the property of the customer when they are delivered to and accepted by the messenger, the customer's withdrawal to be deemed to have been affected as of that moment.

(c) Hazard insurance covering holdup, robbery, theft, messenger fidelity or misappropriation shall be carried for the protection of the customer for all funds transmitted by messenger to or from the bank. The premiums on such insurance may be paid by the bank.

47-101.8. - POWER TO BORROW (Reference A.C.A. § 23-47-101)

The Arkansas Banking Code impose no restriction upon a bank's borrowing power except the issuance of capital notes. Excessive borrowing by a bank can affect its capital adequacy and may subject the bank to administrative action by the Commissioner. Except in the case of capital notes, borrowing by a bank does not require prior approval by the Commissioner.

48-307.1 - CHARTER AMENDMENT APPLICATION FOR CHANGE OF BANK CORPORATE NAME (Reference A.C.A. § 23-48-307)

Prior to filing an application with the State Bank Department for a charter amendment to change the corporate name of a state bank, the bank must complete the following procedures:

A) Publish legal notice of intention to change the corporate name of the bank one (1) time in a newspaper of statewide circulation. Such notice shall include both the current corporate name of the bank and the proposed new name. A copy of the legal notice must accompany the application; and

B) Request a current check of both state and federal trademark or servicemark filings on the proposed new name. Evidence must accompany the application for charter amendment verifying the applicant has made a trademark or servicemark search and no trademark or servicemark exists for the proposed name.

Once the charter amendment is received by the State Bank Department, notice of the filing of the application will be sent to all state-chartered banks by electronic transmission. Any protestants will have seven (7) days from the date the Department notice was sent to file an official protest to the application. An official protest must be provided to the Department in written form delineating the reasons for the protest and must be accompanied by a filing fee of two hundred dollars ($200).

48-309.1. - RESERVATION OF BANK CORPORATE NAME (Reference A.C.A § 23-48-309)

The State Bank Department will accept a reservation for a bank corporate name only prior to and for the purpose of formation of a new state bank or prior to the consummation of an interstate merger transaction. The reservation will be for a nonrenewable two hundred seventy day period. A name not used permanently prior to the expiration of this period will be cancelled.
Prior to filing a reservation of corporate name an applicant must:

> Request a current check of both state and federal trademark or servicemark filings on the proposed name. Evidence must accompany the application for reservation of corporate name verifying the applicant has made a trademark or servicemark search and no trademark or servicemark exists for the proposed name.

48-315.1. - CAPITAL NOTES (Reference A.C.A. § 23-48-315)

(a) A state bank, with the prior approval of the Commissioner, may issue subordinated capital notes. These notes may be authorized by the bank's directors; no stockholder's action being required. The notes must be sold at not less than par. The aggregate par value of the outstanding capital notes of a bank shall not exceed one-half (½) of the capital base of the issuing bank. Such notes shall be retired at such time and in such manner as may be fixed by the Board of Directors of the issuing bank, but not later than twenty (20) years after the date of issuance, subject to extension of the term as set forth in A.C.A. §23-48-315.

(b) It is strongly suggested that the terms of the capital notes clearly state that the subordination to deposit liabilities shall be effective only while the bank is in a state of impaired capital, insolvency, liquidation, etc. Otherwise, the bank, though entirely solvent, might find it impossible (without violating the provisions of the notes) to pay the capital notes until it had retired all of the senior indebtedness.

(c) A bank issuing capital notes must procure from the State Securities Commissioner an exemption certificate under A.C.A. § 23-42-503 (Supp. 1987).

48-315.2. - FEDERAL REGULATIONS (Reference A.C.A. § 23-48-315)

Pursuant to both the Federal Reserve and FDIC Regulations, the capital notes must have an original average weighted maturity of five (5) years or more. The five (5) year term begins, not from the date written on the note, but from the date the note is actually issued and placed in circulation.

SECTION 3

DEPOSITS

47-204.1 IDENTIFICATION REQUIREMENTS FOR THE TRANSFER OR CLOSURE OF PAY ON DEATH DEPOSIT ACCOUNTS (Reference A.C.A. §23-47-204)

A.C.A. § 23-47-204 (e)(4) states: "The State Bank Department shall promulgate rules that set out procedures a bank may take before transferring ownership of a deposit account, closing a deposit account and distributing the proceeds to a person designated by the account documents as a beneficiary."

(a) Before ownership of a deposit account is transferred, or a pay on death account is closed and the funds disbursed, a bank may require:
   (1) For pay on death accounts: Legal evidence of the death of all other account holder(s)
   (2) Identification from each designated beneficiary.
(b) If a designated beneficiary is a non-natural person, the bank may require:
   (1) The non-natural person to provide proof of legal existence and/or good standing as an entity; and
   (2) Individuals representing the non-natural person to provide identification, and evidence demonstrating their authority to collect the account on the non-natural person's behalf.

SECTION 4

INVESTMENTS

47-401.1 - INVESTMENT, CORPORATE DEBT OBLIGATIONS (Reference A.C.A. § 23-47-401)

A bank may invest in debt securities, not in the purchase of stock, with certain exceptions. As to convertible debentures:

a) If the securities are convertible into common stock at the option of the issuer, the bank may not purchase them.

b) If convertible at the option of the holder, the bank may purchase them but must write down the cost to an amount which equals the investment value of the security determined without assigning any value to the conversion feature.

PERMISSIBLE EXCEPTIONS. COMMON STOCK. TRUST PREFERRED SECURITIES.

Common stock is not generally determined to be an investment security. The State Banking Board and Commissioner rule that in some instances the purchase by a bank of common stock may facilitate the exercise of a true banking function and be "incidental to the business of banking." A bank could not purchase and hold common stock solely for the purpose of collecting dividends thereon; but if the acquisition of the common stock is merely incidental to the exercise of some valid banking power, it is permitted. Banks that are active in student loan operations may purchase and hold common stock of the Student Loan Marketing Association ("Sallie Mae"). Banks that participate in the secondary market for agricultural and rural housing real estate mortgages under the direction of the Federal Agricultural Mortgage Corporation ("Farmer Mac") may purchase and hold stock in the Corporation (adopted by the State Banking Board April 19, 1988).

Trust preferred securities are investments also called "trust preferred stock" which possess characteristics similar to debt obligations. Trust preferred securities are authorized investments for a state bank provided the preferred stock meets the investment quality and marketability requirements applicable to investment securities in accordance with the Federal Deposit Insurance Corporation, Financial Institution Letter, FIL-16-99, February 9, 1999, and any amendments thereof. Investments in trust preferred securities will be subject to the bank's legal loan limitation.

47-401.2 - INVESTMENT - CONSUMER PAPER (Reference A.C.A. § 23-47-401)

A bank may purchase consumer paper without recourse, warranty, or repurchase agreement. If, however, the bank purchases dealer paper under an arrangement whereby the dealer endorsed the paper or guaranteed its payment or repurchase, then under A.C.A. § 23-47-501, the loan limit (so far as the dealer in concerned), would be exceeded if the dealer's liability as endorser plus his/her primary liability, if any, to the bank exceeds twenty percent (20%) of the capital base.

1. **EFFECT OF RESERVE.** When consumer paper is purchased by the bank under guaranty or repurchase agreement, if the contract provides for the creation of a reserve by withholding from disbursements or otherwise out of which the bank is entitled to remedy defaults, for loan limit purposes the amount of this reserve may be deducted from the total advances to the dealer.

2. **EFFECT OF DEFAULT.** If two consecutive installments under an item of pledged consumer paper which the dealer has transferred with recourse or under a guaranty should at any time be in default, the entire amount remaining as owed under the defaulted item will be charged against the dealer's loan limit.

47-401.3 - REVENUE OBLIGATIONS – A.C.A § 23-47-401

Any single revenue bond issue of a governmental unit or political subdivision shall be subject to the twenty percent (20%) limitation of the capital base of the bank. A political subdivision will be defined to include an improvement district.

> **NOTE: REVENUE OBLIGATIONS; NOT TO BE COMBINED. For municipal bond obligations payable solely from pledged revenues, the twenty percent (20%) limitation should be applied to each business corporation whose obligation (for rent or otherwise) if being assigned to secure the bonds, and to each bond or note issue payable solely out of revenues; but these revenue bonds should not be combined in determining whether the loan limit of the municipality has been exceeded.**

47-401.4 - TRADING ACCOUNT (Reference A.C.A. § 23-47-401)

Any state chartered bank, or bank holding company owning a state chartered bank, which establishes a "Trading Account" (a "Trading Account" is a segregated account in which assets are held for resale by a bank that regularly engages in trading activities), should be aware that such trading account activity is a high risk activity. Due to the inherent risk, any state chartered bank establishing such an account is required to maintain a written policy setting forth guidelines by which the purchase and sales may be conducted. Such policy must receive the approval of the bank's board of directors and notices of such approval, with a copy of the policy, forwarded to the Commissioner.

> **NOTICE: ENGAGING IN TRADING ACCOUNT ACTIVITY IS A HIGH RISK ACTIVITY!** Banks that engage in the purchase and sale of investments in anticipation of interest rate changes, price changes, and changes in the market or economic condition or for other speculative purposes are engaging in "Trading Account" type activities. Such transactions must be conducted through the appropriate establishment of a "Trading Account." Failure to conduct such "Trading Account" type activities in a duly authorized "Trading Account" will result in the state or federal bank examiners declaring a bank's entire investment account a "Trading Account" and will require all investments to be marked to the lower of market value or acquisition cost. In establishing a "Trading Account" bank directors are reminded of the high risk and speculative nature of this type of banking activity.

STATE BANKING BOARD REQUIREMENTS.

If, after considering the risk of loss, and the possibility of gain, a bank wishes to establish a "Trading Account," it must consider and adopt a policy addressing the following:

A. The bank's board of directors shall adopt written objectives of the "Trading Account."

B. The bank's board of directors shall designate the officer(s) authorized to negotiate such trading transactions.

C. The bank's board of directors shall establish the maximum dollar amount of exposure acceptable to its bank.

D. The bank's board of directors shall identify the type of trading instruments to be traded (treasury bills, government bonds, government agencies securities, tax exempt securities, commercial paper, certificates of deposit, banker's acceptances, put options, call options, other bonds, notes and debentures, gold and silver bullion).

E. The bank's board of directors shall require all transactions to be recorded at the time a contractual obligation to purchase or to sell in an appropriate record at the bank reflecting the bank's "obligation to purchase" or the bank's "obligation to sell". At the time a transaction is consummated, the transaction shall be fully documented requiring invoicing, settlement sheets, etc.

F. The bank's board of directors shall establish, prior to trading activities, the dollar amount of profit or loss it is willing for the bank to incur.

G. The bank's board of directors shall approve a list of security dealers who are eligible for the designated officer(s) of the bank to enter into trade transactions. In approving the list of the dealers, the bank's board of directors must obtain reasonable background information, current financial data, and such other information necessary to establish the character, integrity and financial stability of the dealers which the bank's board of directors proposed to transact business.

H. The bank's board of directors shall require monthly written reports to be submitted by the officer(s) responsible for "Trading Account" activities for review by individual directors.

I. The bank's board of directors shall review the activities in the "Trading Account", including the number of transactions, the bank's exposure, the profit or loss, and the "Trading Account" policy, regarding the adequacy of the policy and the bank's strict adherence to the policy, no less frequently than quarterly with such review being noted in the minutes of the board of directors' meetings.

J. All transactions shall comply with, and meet all requirements of Arkansas' banking laws, rules and regulations, and applicable federal banking laws.

All assets held in "Trading Accounts" are to be reported consistently at lower of the market value or acquisition cost. It is <u>recommended</u> this reporting be made to the bank's board of directors no less frequently than monthly. It is <u>required</u> that this reporting at the lower of market or acquisition cost be done no less frequently than quarterly and reported in accordance with the instructions for the preparation of the Reports of Condition and Income.

Transfers to and from a "Trading Account", or any other account of the bank shall be recorded at market value at the time of the transfer and gains and losses recognized accordingly.

All accounting of gains or losses resulting from "Trading Account" activities shall be consistent with reporting guidelines contained in the instructions for the Report of Condition and Income.

The bank's board of directors shall require written reports to the board which shall include, at a minimum, the following:

1. Total dollar amount held in the "Trading Account."

2. Inventory list by issue with purchase price and current market value.

3. The number of trades which were engaged in during the previous month and the total dollar volume traded.

4. The dollar amount and the number of trades engaged in with each securities dealer.

5. The monthly profit or loss and the year-to-date profit or loss from the "Trading Account" activities, including unrealized losses.

6. Any pending transaction(s) (purchase and/or sale).

BANK SERVICE COMPANIES

47-603.1 - BANK SERVICE COMPANIES (Reference A.C.A. § 23-47-603)

State banks may establish, create or invest in bank service companies which may be corporations or limited liability companies to perform the bank services defined in the statute, including computer and data processing services and such other services as the Commissioner may from time to time by order permit. The stock, in the case of a corporation, or the membership interest, in the case of a limited liability company, of a bank service company may also be owned by persons other than state banks. The operation of bank service companies shall be subject to regulation and examination by the Commissioner so long as any state bank utilizes the services thereof and owns any equity interest in such organization or has any loans outstanding to such organization.

47-603.2- LIMITATION ON INVESTMENT (Reference A.C.A. § 23-47-603)

The aggregate of the loans to and investment in a bank service company cannot exceed twenty percent (20%) of the capital base of a state bank.

SECTION 5

LOAN LIMITS

47-501.1 - CERTIFICATES OF RELIANCE - ENDORSED OR GUARANTEED OBLIGATIONS (Reference A.C.A. § 23-47-501)

The use of Certificates of Reliance was repealed by Act 427 of 2005. State Banks are no longer authorized to use Certificates of Reliance.

47-501.2 - COMBINING LOANS TO PARENT CORPORATION AND SUBSIDIARY, AND LOANS TO SEPARATE SUBSIDIARIES (Reference A.C.A. § 23-47-501)

The Commissioner and State Banking Board rule that separate loans to a parent corporation and its subsidiary must be combined, for the assets of the parent may be represented wholly or in part by the stock of the subsidiary. If separate loans are made to two or more subsidiaries which operate separately and entirely independent of each other, then so far as the loan limit law is concerned, each could borrow up to the full loan limit; but if a subsidiary is dependent is its operations upon another subsidiary of the same parent for some vital service or commodity, the loans should be combined. If the parent corporation is not borrowing, obligations of subsidiary corporations are generally not combined except in the following situations:

A. the bank is looking to a single source for repayment of the loan;

B. one or more loans are for the accommodation of the parent corporation or other subsidiary; or

C. the borrowing corporations are not separate concerns in reality but merely departments or divisions of a single enterprise.

Obligations of a corporations must be combined with any other extension of credit the proceeds of which are used for the benefit of the corporation.

47-501.3 – TOTAL INDEBTEDNESS (Reference A.C.A. §23-47-501)

"Total indebtedness" shall also include any credit exposure to a person arising from a derivative transaction, repurchase agreement, reverse repurchase agreement, securities lending transaction, or securities borrowing transaction between the bank and the person. For the purposes of this paragraph the term derivative transaction shall include any transaction that is a contract, agreement, swap, warrant, note, or option that is based in whole or in part, on the value of, any interest in, or any quantitative measure or the occurrence of any event relating to, one or more commodities, securities, currencies, interest or other rates, indices, or other assets.

47-502.1 - DRAFTS OR BILLS OF EXCHANGE (Reference A.C.A. § 23-47-502)

The Commissioner and the State Banking Board rule that this exception applies to negotiable drafts and to bills of exchange drawn by the seller of commodities upon the purchaser and bearing the acceptance of the latter, or drawn by the purchaser of commodities upon his bank and endorsed by the seller. In order to qualify under this exception, drafts or bills of exchange must be two name paper. Thus, unaccepted drafts are not eligible, nor are bills of exchange endorsed without recourse or not endorsed.

47-502.2 - OBLIGATIONS DRAWN AGAINST EXISTING VALUES (Reference A.C.A. § 23-47-502)

The Commissioner and the State Banking Board rule that this exception applies to obligations secured by pledge of bill of lading covering goods or commodities in process of shipment. It is immaterial whether the obligation is negotiable and whether it is one-name or two-name paper; but the exception applies only to paper in connection with a sale transaction.

47-502.3 - OBLIGATIONS SECURED BY CERTAIN TRANSFERABLE DOCUMENTS OF TITLE (Reference A.C.A. § 23-47-502)

The Commissioner and the State Banking Board rule that one hundred fifteen percent (115%) collateral margin applies both to livestock and readily marketable and nonperishable commodities, etc., covered by transferable documents. “Transferable documents” will be construed to include merely title documents, such as bills of lading or warehouse receipts, and not to include a lien instrument such as a chattel mortgage.

If one hundred fifteen percent (115%) collateral margin should be impaired by depreciation, the failure to restore the margin may result in a loan limit violation.

Even though the bank has previously loaned a borrower up to the statutory loan limit of twenty percent (20%), it may, without committing a loan limit violation, lend the same borrower additional funds against collateral properly margined as provided in the last preceding paragraph.

47-502.4 - OBLIGATIONS GUARANTEED BY FARM SERVICE AGENCY (Reference A.C.A. § 23-47-502)

Obligations, which the Farm Service Agency or United States Department of Agriculture (formerly Farmers Home Administration), guarantees against any <u>loss</u> sustained by the bank are, to the extent of such guarantee, free from loan limitations.

47-502.5 - LOANS SECURED BY CERTIFICATE OF DEPOSIT (Reference A.C.A. § 23-47-502)

The portion of a loan properly secured by a commercial bank certificate of deposit, whether it is an "own" bank certificate of deposit or a certificate of deposit issued by another commercial bank will not be subject to that bank's legal loan limit.

47-502.6 - LOAN COMMITMENTS AND STANDBY LETTERS OF CREDIT (Reference A.C.A. § 23-47-502)

Loan commitments and standby letters of credit will be subject to a banks legal loan limit in the entire amount on the date the loan commitment or letter of credit is issued in written form whether or not any, a portion of, or all of the loan has been funded.

SECTION 6

SUBSIDIARIES

(RESERVED)

SECTION 7

TRUST POWERS

47-701.1 - ACTIVITIES NOT REQUIRING TRUST POWERS (Reference A.C.A. § 23-47-701)

A bank acting as escrow holder under an ordinary escrow contract, where the bank has no power to invest the escrowed funds, does not require trust powers. A state bank without trust powers may act as paying agent under a bond or note issue but it may not act as trustee thereunder.

47-701.2 - FEDERAL DEPOSIT INSURANCE CORPORATION AND FEDERAL RESERVE APPROVAL (Reference A.C.A. § 23-47-701)

A non-member insured bank may not adopt trust powers without Federal Deposit Insurance Corporation approval. A state member bank must obtain Federal Reserve approval.

47-701.3 - TITLE TO TRUST SECURITIES IN NAME OF A NOMINEE (Reference A.C.A. § 23-47-701)

A bank or trust company in the administration of a trust may place title to trust securities in the name of a nominee. If there is a co-trustee, consent must be obtained. But a bank or trust company in such a situation, will be absolutely responsible for any loss occasioned by the act of the nominee.

47-701.4 - COMMON TRUST FUND (Reference A.C.A. § 23-47-701)

(a) This concept permits the consolidation of the assets of the various trusts being administered by the bank into a common fund for investment purposes and to allocate to each trust a specific interest in this fund based on the amount of its contribution. An insured state chartered non-member bank or trust establishing a common trust fund should consult the Federal Deposit Insurance Corporation regarding its rules and regulations on such common trust funds.

(b) The Internal Revenue Code and the regulations and rulings promulgated thereunder contain certain provisions which exempt common trust funds from income taxation and instead impose the tax on each trust, whether or not the income is distributed. If there is a co-fiduciary, the bank establishing the common trust fund must secure the permission of the co-fiduciary prior to the investment of trust assets into the fund. If the bank merely acts as an investment agent in respect to the investments of one of its customers, such funds may not be placed in the common trust fund. Any state bank establishing a common trust fund shall obtain approval of the Commissioner in advance of implementation. Such approval shall not be unreasonably withheld.

47-701.5 - INDIVIDUAL RETIREMENT ACCOUNT (Reference A.C.A. § 23-47-701)

Section 26 U.S.C. 408 et seq. establishes Individual Retirement Accounts. A bank that has trust powers may accept deposits into Individual Retirement Accounts and may, depending on the arrangement between the depositor and the bank, exercise discretion in the investment of such account. If a bank does not have trust powers, it may accept such deposits on a "custodial" arrangement only. However, reference should be made to the above cited federal law and the regulations and rulings promulgated thereunder for the administration of such accounts.

47-701.6 - KEOGH PLAN (Reference A.C.A. § 23-47-701)

A bank's activities as trustee or custodian under a Keogh Plan is governed by Section 26. U.S.C. 404(e).

47-705.1 - TRUST DEPOSITS AWAITING INVESTMENT OR DISTRIBUTION (Reference A.C.A. § 23-47-705)

All Trust Deposits awaiting investment or distribution which are determined to be eligible under A.C.A. § 28-69-206 for pledging of government securities to the deposit, may be secured by a blanket pledging of eligible securities to those eligible trust deposits subject to the following requirements:

(a) The total of the pledged securities must always exceed the total of the eligible trust deposits by ten percent (10%). Such trust deposits shall have a prior and preferred claim on said pledged securities.

(b) Any bank using blanket securities as collateral for eligible trust deposits must identify the securities being used and perfect a security interest in such securities for the benefit of the owners of the accounts for which the pledge is made.

(c) Trust deposits that are being collateralized must be designated in the trust department's records. The actual amount of collateralization need not be given. These records should be maintained current at all times within the bank's trust department.

(d) Funds held by a state bank as trustee which are awaiting investment or distribution shall not be held uninvested or undistributed any longer than is reasonable for the proper management of the account. Each state bank exercising fiduciary powers shall adopt and follow written policies and procedures intended to ensure that the maximum rate of return available for trust-quality, short-term investments is obtained upon funds so held, consistent with the requirements of the governing instrument and local law. Such policies and procedures shall take into consideration all relevant factors, including but not limited to the anticipated return that could be obtained while the cash remains uninvested or undistributed, the cost of investing such funds, and the anticipated need for the funds.

(e) Funds held in trust by a state bank as trustee awaiting investment or distribution may, unless prohibited by the instrument creating the trust or by local law, be deposited in the commercial or savings or other department of the bank, provided that it shall first set aside under control of the trust department as collateral security (i) direct obligations of the United States, (ii) other obligations fully guaranteed by the United States as to principal and interest, or (iii) general obligations of the State of Arkansas.

(f) The securities so deposited or securities substituted therefore as collateral shall at all times exceed the total of the eligible trust deposits by ten percent (10%), but such security shall not be required to the extent that the funds so deposited are insured by the Federal Deposit Insurance Corporation. The requirements of this section are met when qualifying assets of the bank are pledged to secure a deposit in compliance with local law, and no duplicate pledge shall be required in such case.

47-701.7 - BANK AS TRUSTEE; VOTING OF OWN SHARES (Reference A.C.A. § 23-47-701)

The trust department of a state bank is theoretically subject to the dominion of the board of directors; and the trust department conceivably might in some situations be called upon to vote the bank's own shares for proposals more calculated to benefit the individual directors than the bank. Under the National Banking Act (Section 12 U.S.C. 61) a national bank cannot vote its own shares in the election of directors of the bank unless under the terms of the trust the manner in which the shares shall be voted may be determined by a donor or beneficiary of the trust and unless such donor or beneficiary actually directs how such shares shall be voted. Moreover, if the national bank has a co-trustee, the shares may be voted by the co-trustee. The above stated national bank rule shall be applicable with respect to voting any shares of the bank held by the trust department in the election of the bank's directors. On all other proposals, the trust department is urged to weigh carefully the issues presented and any conflicts of interest which are present before deciding whether to vote or how to vote the shares.

47-701.8 - TRUST POLICIES (Reference A.C.A. § 23-47-701)

All state banks exercising trust powers shall adopt a trust policy setting forth, at a minimum, trust department investment practices, including investments in the obligations of the bank and its affiliates, voting practices and procedures concerning the banks stock and the stock of any affiliates of the bank, and trust account administration policies and procedures.

FIDUCIARY POWERS OF STATE BANKS

47-701.9 - FIDUCIARY POWERS OF STATE BANKS (Reference A.C.A. § 23-47-701)

(a) Definitions. For the purposes of this regulation, the term:

"**Account**" means the trust, estate or other fiduciary relationship which has been established with a bank;

"**Custodian under a Uniform Gifts to Minors Act**" means an account established pursuant to a state law which is substantially similar to the Uniform Gifts to Minors Act as published by the America Law Institute and with respect to which the bank operating such account has established to the satisfaction of the Secretary of the Treasury that it has duties and responsibilities similar to duties and responsibilities of a trustee or guardian.

"**Fiduciary**" means a bank undertaking to act alone or jointly with others primarily for the benefit of another in all matters connected with its undertaking and includes trustee, executor, administrator, registrar of stocks and bonds, guardian of estates, assignee, receiver, committee of estates of incompetents, managing agent and any other similar capacity;

"**Fiduciary powers**" means the power to act in any fiduciary capacity as authorized by Arkansas state law or any applicable federal law;

"**Fiduciary records**" means all matters which are written, transcribed, recorded, received or otherwise come into possession of a bank and are necessary to preserve information concerning the acts and events relevant to the fiduciary activities of a bank;

"**Guardian**" means the guardian or committee by whatever name employed by local law, of the estate of an infant, an incompetent individual, an absent individual, or a competent individual over whose estate a court has taken jurisdiction, other than under bankruptcy or insolvency laws;

"**Investment authority**" means the responsibility conferred by action of law or a provision of an appropriate governing instrument to make, select or change investments, review investment decisions made by others, or to provide investment advice or counsel to others;

"**Local law**" means the law of the state or other jurisdiction governing the fiduciary relationship;

"**Managing agent**" means the fiduciary relationship assumed by a bank upon the creation of an account which names the bank as agent and confers investment discretion upon the bank;

"**State bank**" means any bank, trust company, savings bank, or other banking institution, which is not a national bank and the principal office of which is located in the District of Columbia, any state, commonwealth, or territorial possession of the United States;

"**Trust department**" means that group or groups of officers and employees of a bank organized under the supervision of officers or employees to whom are designated by the board of directors the performance of the fiduciary responsibilities of the bank, whether or not the group or groups are so named;

(b) Adoption of Policies and Procedures with Respect to Brokerage Placement Practices.

Each state bank exercising investment discretion (as defined in Section 12 C.F.R. 12.2(c)) with respect to an account shall adopt and follow written policies and procedures intended to ensure that its brokerage placement practices comply with all applicable laws and regulations. Among other relevant matters, such written policies and procedures should address, where appropriate,

(1) the selection of persons to effect securities transactions and the evaluation of the reasonableness of any brokerage commissions paid to such persons (including the factors considered in these determinations);

(2) any acquisition of services or products, including research services, in return for brokerage commissions;

(3) the allocation of research or other services among accounts, including those which did not generate commissions to pay for such research or other services; and

(4) the need, in appropriate instances, to make disclosures concerning such policies and procedures to prospective and existing customers.

(c) Administration of Fiduciary Powers.

(1) (A) The board of directors is responsible for the proper exercise of fiduciary powers by the bank. All matters pertinent thereto, including the determination of policies, the investment and disposition of property held in a fiduciary capacity, and the direction and review of the actions of all officers, employees, and committees utilized by the bank in the exercise of its fiduciary powers, are the responsibility of the board. In discharging this responsibility, the board of directors may assign, by action duly entered in the minutes, the administration of such of the bank's fiduciary powers as it may consider proper to assign to such directors, officers, employees or committees as it may designate.

(B) No fiduciary account shall be accepted without the prior approval of the board, or of the directors, officers, or committees to whom the board may have designated the performance of that responsibility. A written record shall be made of such acceptances and of the relinquishment or closing out of all fiduciary accounts. Upon the acceptance of an account for which the bank has investment responsibilities, a prompt review of the assets shall be made. The board shall also ensure that at least once during every calendar year thereafter, all the assets held in or for each fiduciary account, where the bank has investment responsibilities are reviewed to determine the advisability of retaining or disposing of such assets. A written record shall be made of the approval of all purchases, sales and changes of trust assets.

(C) The board of directors shall name a Trust Committee consisting of at least three (3) directors, at least one of whom shall not be an officer of the bank, to be responsible for and supervise the activities of the trust department. The Trust Committee shall meet at least quarterly or more frequently if necessary and prudent to adequately supervise the activities of the department. The Trust Committee shall keep full minutes of its actions and make periodic reports thereof to the board.

(2) All officers and employees taking part in the operation of the trust department shall be adequately bonded.

(3) Every state bank exercising fiduciary powers shall designate, employ or retain legal counsel who shall be readily available to pass upon fiduciary matters and to advise the bank and its trust department.

(4) The trust department may utilize personnel and facilities of other departments of the bank, and other departments of the bank may utilize personnel and facilities of the trust department only to the extent not prohibited by law. Every state bank exercising fiduciary powers shall adopt written policies and procedures to ensure that the Federal and State securities laws are complied with in connection with any decision or recommendation to purchase or sell any security. Such policies and procedures, in particular, shall ensure that state bank trust departments shall not use material inside information in connection with any decision or recommendation to purchase or sell any security.

(5) The Trust Committee shall review the examination reports of the trust department by supervisory agencies and record its action thereon in its minutes. Nothing herein is intended to prohibit the board of directors from acting as the Trust Committee, from designating additional officers to administer the operations of the trust department and defining their duties, or from appointing additional committees for the trust department operation and defining the duties of such committee.

(d) <u>Books and Accounts.</u>

(1) Every state bank exercising fiduciary powers shall keep its fiduciary records separate and distinct from other records of the bank. All fiduciary records shall be so kept and retained for such time as to enable the bank to furnish such information or reports with respect thereto as may be required by the State Bank Department. The fiduciary records shall contain full information relative to each account.

(2) Every such state bank shall keep an adequate record of all pending litigation to which it is a party in connection with its exercise of fiduciary powers.

(3) Solely for purposes of examination by the State Bank Department, a state bank shall retain the records required by this section for a period of three (3) years from the later of termination of the fiduciary account relationship to which the records relate or of litigation relating to such account, unless applicable law specifically prescribes a different period.

(e) Audit of Trust Department.

A committee of directors, exclusive of any active officers of the bank, shall at least once during each calendar year make suitable audits of the trust department or cause suitable audits to be made by auditors responsible only to the board of directors and at such time shall ascertain whether the department has been administered in accordance with law, applicable regulations and sound fiduciary principles. The board of directors may elect, in lieu of such periodic audits, to adopt an adequate continuous audit system. A report of the audits and examination required under this section, together with the action taken thereon, shall be noted in the minutes of the board of directors.

(f) Investment of Funds Held as Fiduciary.

(1) Funds held by a state bank in a fiduciary capacity shall be invested in accordance with the instrument establishing the fiduciary relationship and local law. When such instrument does not specify the character or class of investments to be made and does not vest in the bank, its directors or its officers a discretion in the matter, funds held pursuant to such instrument shall be invested in any investment in which corporate fiduciaries may invest under local law.

(2) If, under local law, corporate fiduciaries appointed by a court are permitted to exercise a discretion in investments, or if a state bank acting as fiduciary under appointment by a court is vested with a discretion in investments by an order of such court, funds of such accounts may be invested in investments which are permitted by local law. Otherwise, a state bank acting as fiduciary under appointment by a court must make all investments of funds in such accounts under an order of that court. Such orders in either case shall be preserved with the fiduciary records of the bank.

(3) The collective investment of funds received or held by a state bank as fiduciary is governed by subsection (n) of this regulation.

(4) As a part of each examination of the trust department of a state bank the State Bank Department will examine the investments held by such bank as fiduciary, including the investment of funds under the provisions of subsection (n) of this section, in order to determine whether such investments are in accordance with law, this regulation and sound fiduciary principles.

(g) Self-dealing.

(1) Unless lawfully authorized by the instrument creating the relationship or by court order or by local law, funds held by a state bank as fiduciary shall not be invested in stock or obligations of, or property acquired from, the bank or its directors, officers, or employees, or individuals with whom there exists such a connection, or organizations in which there exists such an interest, as might affect the exercise of the best judgment of the bank in acquiring the property, or in stock or obligations of, or property acquired from, affiliates of the bank or their directors, officers or employees.

(2) Property held by a state bank as fiduciary shall not be sold or transferred, by loan or otherwise, to the bank or its directors, officers, or employees, or to individuals with whom there exists such a connection, or organizations in which there exists such an interest, as might affect the exercise of the best judgment of the bank in selling or transferring such property, or to affiliates of the bank or their directors, officers or employees, except:

(A) Where lawfully authorized by the instrument creating the relationship or by court order or by local law;

(B) In cases in which the bank has been advised by its counsel in writing that it has incurred as fiduciary a contingent or potential liability and desires to relieve itself from such liability, in which case such a sale or transfer may be made with the approval of the board of directors, provided that in all such cases the bank, upon the consummation of the sale or transfer, shall make reimbursement in cash at no loss to the account;

(C) As is provided in subsection (b)(8)(B) of this regulation;

(D) Where required by the State Bank Department.

(3) Except as provided in (f) (2) of this regulation, funds held by a state bank as fiduciary shall not be invested by the purchase of stock or obligations of the bank or its affiliates unless authorized by the instrument creating the relationship or by court order or by local law, provided that if the retention of stock or obligations of the bank or its affiliates is authorized by the instrument creating the relationship or by court order or by local law, it may exercise rights to purchase its own stock or securities convertible into its own stock when offered pro rata to stockholders, unless such exercise is forbidden by local law. When the exercise of rights or receipt of a stock dividend results in fractional share holdings, additional fractional shares may be purchased to complement the fractional shares so acquired.

(4) A state bank may sell assets held by it as fiduciary in one account to itself as fiduciary in another account if the transaction is fair to both accounts and if such transaction is not prohibited by the terms of any governing instrument or by local law.

(5) A state bank may make a loan to an account from the funds belonging to another such account, when the making of such loans to a designated account is authorized by the instrument creating the account from which such loans are made, and is not prohibited by local law.

(6) A state bank may make a loan to an account and may take as security therefore assets of the account, provided such transaction is fair to such account and is not prohibited by local law.

(h) Custody of Investments.

(1) The investments of each account shall be kept separate from the assets of the bank, and shall be placed in the joint custody or control of not less than two of the officers or employees of the bank designated for that purpose by the board of directors of the bank or by one

or more officers designated by the board of directors of the bank; and all such officers and employees shall be adequately bonded. To the extent permitted by law, a state bank may permit the investments of a fiduciary account to be deposited elsewhere.

(2) The investments of each account shall be either:

(A) Kept separate from those of all other accounts, except as provided in subsection (n) of this regulation, or

(B) Adequately identified as the property of the relevant account.

(i) Deposit of Securities with State Authorities.

Whenever the local law requires corporations acting as fiduciary to deposit securities with the state authorities for the protection of private or court trusts, every state bank in that state authorized to exercise fiduciary powers shall, before undertaking to act in any fiduciary capacity, make a similar deposit with the state authorities. If the state authorities refuse to accept such a deposit, the securities shall be deposited with the Federal Reserve Bank of the district in which such state bank is located, and such securities shall be held for the protection of private or court trusts with like effect as though the securities had been deposited with the state authorities.

(j) Compensation of Bank.

(1) If the amount of the compensation for acting in a fiduciary capacity is not regulated by local law or provided for in the instrument creating the fiduciary relationship or otherwise agreed to by the parties, a state bank acting in such capacity may charge or deduct a reasonable compensation for its services. When the bank is acting in a fiduciary capacity under appointment by a court, it shall receive such compensation as may be allowed or approved by that court or by local law.

(2) No state bank shall, except with the specific approval of its board of directors, permit any of its officers or employees, while serving as such, to retain any compensation for acting as a co-fiduciary with the bank in the administration of any account undertaken by it.

(k) Receivership or Voluntary Liquidation of Bank.

(1) Whenever a receiver is appointed for a state bank by the Commissioner, such receiver shall, pursuant to the instructions of the Commissioner and to the orders of the court having jurisdiction, proceed to close such accounts as can be closed promptly and transfer all other accounts to substitute fiduciaries.

(2) Whenever a state bank exercising fiduciary powers is placed in voluntary liquidation, the liquidating agent shall, in accordance with the local law, proceed at once to liquidate the affairs of the trust department as follows:

(A) All trust and estates over which a court is exercising jurisdiction shall be closed or disposed of as soon as practical in accordance with the orders or instructions of such court;

(B) All other accounts which can be closed promptly shall be closed as soon as practicable and final accounting made therefore, and all remaining accounts shall be transferred by appropriate legal proceedings to substitute fiduciaries.

(l) Surrender or Revocation of Fiduciary Powers. Any state bank which has been granted the right to exercise fiduciary powers and which desires to surrender such right shall file with the Commissioner a certified copy of the resolution of its board of directors signifying such desire. Upon receipt of such resolution, the Commissioner shall make an investigation and if satisfied that the bank has been discharged from all fiduciary duties which it has undertaken, shall issue a certificate to such bank certifying that it is no longer authorized to exercise fiduciary powers.

COLLECTIVE INVESTMENT FUNDS

Collective Investment. (Common Trust Funds as in A.C.A. § 28-69-202)

(a) Where not in contravention of local law, funds held by a state bank as fiduciary may be invested collectively:

(1) In a common trust fund maintained by the bank exclusively for the collective investment and reinvestment of moneys contributed thereto by the bank in its capacity as trustee, executor, administrator, guardian, or custodian under a Uniform Gifts to Minors Act.

(2) In a fund consisting solely of assets of retirement, pension, profit sharing, stock bonus or other trusts which are exempt from federal income taxation under the Internal Revenue Code.

(b) Collective investment of funds or other property by state banks under paragraph a of this section (referred to in this paragraph as "collective investment funds") shall be administered as follows:

(1) Each collective investment fund shall be established and maintained in accordance with a written plan (referred to herein as the Plan) which shall be approved by a resolution of the bank's board of directors and filed with the Comptroller of the Currency. The Plan shall contain appropriate provisions not inconsistent with the rules and regulations of the Comptroller of the Currency and the State Bank Department as to the manner in which the fund is to be operated, including provisions relating to the investment powers and a general statement of the investment policy of the bank with respect to the fund; the allocation of income, profits and losses; the terms and conditions governing the admission or withdrawal of participations in the fund; the auditing of accounts of the bank with respect to the fund; the basis and method of valuing assets in the fund, setting forth criteria for each type of asset; the minimum frequency for valuation of assets of the fund; the period following each such valuation date during which the

valuation may be made (which period in usual circumstances should not exceed 10 business days); the basis upon which the fund may be terminated; and such other matters as may be necessary to define clearly the rights of participants in the fund. Except as otherwise provided in paragraph (b)(15) of this section of this regulation, fund assets shall be valued at market value unless such value is not readily ascertainable, in which case a fair value determined in good faith by the fund trustees may be used. A copy of the Plan shall be available at the principal office of the bank for inspection during all banking hours and upon request a copy of the Plan shall be furnished to any person.

(2) Property held by a bank in its capacity as trustee of retirement, pension, profit sharing, stock bonus, or other trusts which are exempt from federal income taxation under any provisions of the Internal Revenue Code may be invested in collective investment funds established under the provisions of subparagraph (1) or (2) of paragraph (a) of this section of this regulation, subject to the provisions herein contained pertaining to such funds, and may qualify for tax exemption pursuant to section 584 of the Internal Revenue Code. Assets of retirement, pension, profit sharing, stock bonus, or other trusts which are exempt from federal income taxation by reason of being described in Section 401 of the Internal Revenue Code may be invested in collective investment funds established under the provisions of subparagraph (2) of paragraph (a) of section this of this regulation if the fund qualifies for tax exemption under Revenue Ruling 81-100, and following rules.

(3) All participations in the collective investment fund shall be on the basis of a proportionate interest in all of the assets. In order to determine whether the investment of funds received or held by a bank as fiduciary in a participation in a collective investment fund is proper, the bank may consider the collective investment fund as a whole and shall not, for example, be prohibited from making such investment because any particular asset is non-income producing.

(4) Not less frequently than once during each period of three (3) months, a bank administering a collective investment fund shall determine the value of the assets in the fund as of the date set for the valuation of assets. No participation shall be admitted to or withdrawn from the fund except (i) on the basis of such valuation and (ii) as of such valuation date. No participation shall be admitted to or withdrawn from the fund unless a written request for or notice of intention of taking such action shall have been entered on or before the valuation date in the fiduciary records of the bank and approved in such manner as the board of directors shall prescribe. No requests or notices may be canceled or countermanded after this valuation date. If a fund described in paragraph (a)(2) of this section of this regulation is to be invested in real estate or other assets which are not readily marketable, the bank may require a prior notice period not to exceed one (1) year, for withdrawals.

(5) (A) A bank administering a collective investment fund shall at least once during each period of twelve (12) months cause an adequate audit to be made of the collective investment fund by auditors responsible only to the board of directors of the bank. In the event such audit is performed by independent public accountants, the reasonable expenses of such audit may be charged to the collective investment fund.

(B) A bank administering a collective investment fund shall at least once during a period of twelve (12) months prepare a financial report of the fund. This report, based upon the above audit, shall contain a list of investments in the fund showing the cost and current market value of each investment; a statement for the period since the previous report showing purchases, with cost; sales, with profit or loss and any other investment changes; income and disbursements; and an appropriate notation as to any investments in default.

(C) The financial report may include a description of the fund's value on previous dates, as well as its income and disbursements during previous accounting periods. No predictions or representations as to future results may be made. In addition, as to funds described in subparagraph (1) of paragraph (a) of this section of this regulation, neither the report nor any other publication of the bank shall make reference to the performance of funds other than those administered by the bank.

(D) A copy of the financial report shall be furnished, or notice shall be given that a copy of such report is available and will be furnished without charge upon request, to each person to whom a regular periodic accounting would ordinarily be rendered with respect to each participating account. A copy of such financial report may be furnished to prospective customers. The cost of printing and distribution of these reports shall be borne by the bank. In addition, a copy of the report shall be furnished upon request to any person for a reasonable charge. The fact of the availability of the report for any fund described in subparagraph (1) of paragraph (a) of this section of this regulation may be given publicity solely in connection with the promotion of the fiduciary services of the bank.

(E) Except as herein provided, the bank shall not advertise or publicize its collective investment fund(s) described in subparagraph (1) of paragraph (a) of this section of this regulation.

(6) When participations are withdrawn from a collective investment fund, distributions may be made in cash or ratably in kind, or partly in cash and partly in kind, provided that all distributions as of any one valuation date shall be made on the same basis.

(7) If for any reason an investment is withdrawn in kind from a collective investment fund for the benefit of all participants in the fund at the time of such withdrawal and such investment is not distributed ratably in kind, it shall be segregated and administered or realized upon for the benefit ratably of all participants in the collective investment fund at the time of withdrawal.

(8) (A) No bank shall have any interest in a collective investment fund other than in its fiduciary capacity. Except for temporary net cash overdrafts or as otherwise specifically provided herein, it may not lend money to a fund, sell property to, or purchase property from a fund. No assets of a collective investment fund may be invested in stock or obligations, including time or savings deposits, of the bank or any of its affiliates, provided that such deposits may be made of funds awaiting investment or distribution. Subject to all other provisions of this section, funds held by a bank as fiduciary for its own employees may be

invested in a collective investment fund. A bank may not make any loan on the security of a participation in a fund. If because of a creditor relationship or otherwise the bank acquires an interest in a participation in a fund, the participation shall be withdrawn on the first date on which such withdrawal can be effected. However, in no case shall an unsecured advance until the time of the next valuation date to an account holding a participation be deemed to constitute the acquisition of an interest by the bank.

(B) Any bank administering a collective investment fund may purchase for its own account from such fund any defaulted fixed income investment held by such fund, if in the judgment of the board of directors the cost of segregation of such investment would be greater than the difference between its market value and its principal amount plus interest and penalty charges due. If the bank elects to so purchase such investment, it must do so at its market value or at the sum of cost, accrued unpaid interest, and penalty charges, whichever is greater.

(9) Except in the case of collective investment funds described in paragraph (a)(2) of this section of this regulation:

(A) No funds or other property shall be invested in a participation in a collective investment fund if as a result of such investment the participant would have an interest aggregating in excess of ten percent (10%) of the then market value of the fund, provided that in applying this limitation if two or more accounts are created by same person or persons and as much as one-half (½) of the income or principal of each account is payable or applicable to the use of the same person or persons, such accounts shall be considered as one;

(B) No investment for a collective investment fund shall be made in stocks, bonds or other obligations of any one person, firm or corporation if as a result of such investment the total amount invested in stocks, bonds, or other obligations issued or guaranteed by such person, firm or corporation would aggregate in excess of ten percent (10%) of the then market value of the fund, provided that this limitation shall not apply to investments in direct obligations of the United States or other obligations fully guaranteed by the United States as to principal and interest;

(C) A bank administering a collective investment fund shall maintain, in cash and readily marketable investments, such percentage of the assets of the fund as is necessary to provide adequately for the liquidity needs of the fund and to prevent inequities among fund participants.

(10) The reasonable expenses incurred in servicing mortgages held by a collective investment fund may be charged against the income account of the fund and paid to servicing agents, including the bank administering the fund.

(11) (A) A bank may (but shall not be required to) transfer up to five percent (5%) of the net income derived by a collective investment fund from mortgages held by such fund during any regular accounting period to a reserve account, provided that no such transfers shall be made which would cause the amount in such account to exceed one percent (1%) of the outstanding principal amount of all mortgages held in the fund. The amount of such reserve account, if established, shall be deducted from the assets of the fund in determining the fair market value of the fund for the purposes of admissions and withdrawals.

(B) At the end of each accounting period, all interest payments which are due but unpaid with respect to mortgages in the fund shall be charged against such reserve account to the extent available and credited to income distributed to participants. In the event of subsequent recovery of such interest payments by the fund, the reserve account shall be credited with the amount so recovered.

(12) A state bank administering a collective investment fund shall have the exclusive management thereof. The bank may charge a fee for the management of the collective investment fund provided that the fractional part of such fee proportionate to the interest of each participant shall not, when added to any other compensations charged by a bank to a participant, exceed the total amount of compensations which would have been charged to said participant if no assets of said participant had been invested in participations in the fund. The bank shall absorb the costs of establishing or reorganizing a collective investment fund.

(13) No bank administering a collective investment fund shall issue any certificate or other document evidencing a direct or indirect interest in such fund in any form.

(14) No mistake made in good faith and in the exercise of due care in connection with the administration of a collective investment fund shall be deemed to be a violation of this part if promptly after the discovery of the mistake the bank takes whatever action may be practicable in the circumstances to remedy the mistake.

(15) Short-term investment funds established under paragraph (a) of this section of this regulation may be operated on a cost, rather than market value, basis for purposes of admissions and withdrawals, if the plan of operation satisfies the following conditions:

(A) investments must be limited to bonds, notes or other evidences of indebtedness which are payable on demand (including variable amount notes) or which have a maturity date not exceeding ninety-one (91) days from the date of purchase. However, twenty percent (20%) of the value of the fund may be invested in longer term obligations;

(B) the difference between the cost and anticipated principal receipt on maturity must be accrued on a straight-line basis;

(C) assets of the fund must be held until maturity under usual circumstances; and

(D) after effecting admissions and withdrawals, not less than twenty percent (20%) of the value of the remaining assets of the fund must be composed of cash, demand obligations and assets that will mature on the fund's next business day.

(c) In addition to the investments permitted under paragraph 1 of this regulation, funds or other property received or held by a state bank as fiduciary may be invested collectively, to the extent not prohibited by local law, as follows:

(1) In shares of a mutual trust investment company, organized and operated pursuant to a statute that specifically authorizes the organization of such companies exclusively for the investment of funds held by corporate fiduciaries, commonly referred to as a "bank fiduciary fund."

(2) (A) In a single real estate loan, a direct obligation of the United States, or an obligation fully guaranteed by the United States, or in a single fixed amount security, obligation or other property, either real, personal or mixed, of a single issuer; or

(B) On a short term basis in a variable amount note of a borrower of prime credit, provided that such note shall be maintained by the bank on its premises and may be utilized by it only for investment of moneys held in its trust department accounts, provided further, that the bank owns no participation in the loans or obligations authorized under (A) or (B) hereof, and has no interest in any investment therein except in its capacity as fiduciary.

(3) In a common trust fund maintained by the bank for the collective investment of cash balances received or held by a bank in its capacity as trustee, executor, administrator, or guardian, which the bank considers to be individually too small to be invested separately to advantage. The total investment for such fund must not exceed one hundred thousand dollars ($100,000); the number of participating accounts is limited to one hundred (100), and no participating account may have an interest in the fund in excess of ten thousand dollars ($10,000), provided that in applying these limitations if two or more accounts are created by the same person or persons and as much as one-half (½) of the income or principal of each account is presently payable or applicable to the use of the same person or persons such account shall be considered as one, and provided that no fund shall be established or operated under this subparagraph for the purpose of avoiding the provisions of paragraph (b) of this section of this regulation.

(4) In any investment specifically authorized by court order, or authorized by the instrument creating the fiduciary relationship, in the case of trusts created by a corporation, its subsidiaries and affiliates or by several individual settlors who are closely related, provided that such investment is not made under this subparagraph for the purpose of avoiding the provisions of paragraph (b) of this section of this regulation.

(5) In such other manner as shall be approved in writing by the State Bank Department.

SECTION 8

CHANGE IN CONTROL

48-317.1 - TRANSFERS AFFECTING CHANGE IN CONTROL (Reference A.C.A. § 23-48-317)

(a) The acquisition of a state bank by a bank holding company, or the acquisition of twenty-five percent (25%) or more of the common stock of a state bank or a bank holding company controlling a state bank subsidiary, will be considered a change in control. The ownership of more than five percent (5%) of the outstanding voting shares of a state bank is considered a controlling interest.

(b) Any person(s) or entity desiring to obtain "control" of a state chartered bank or bank holding company controlling a state bank subsidiary shall be required to file an application with the Commissioner on a form prescribed by the Commissioner containing the information set forth in A.C.A. §23-48-317(d) and such other information as the Commissioner may require.

(c) An application for a change in control which will authorize the applicant's ownership to initially exceed of twenty-five percent (25%) of the stock in a bank or bank holding company controlling a state bank subsidiary shall be accompanied by a filing fee of $5,000.

48-317.2 - TIME FOR COMMISSIONER'S RULING (Reference A.C.A. § 23-48-317)

Generally, the Commissioner will consider and make a decision on a change in control application within thirty (30) days of receipt of all requested information. However, the Commissioner reserves the right to extend the such period as necessary to make a complete determination on the application.

48-317.3 - ANTI-COMPETITIVE ACQUISITIONS (Reference A.C.A. § 23-48-317)

If a proposed change in control would result in one person, or group of associated persons, firms or corporations, controlling two or more banks competing in the same market, the Commissioner would be inclined to disapprove the transfer unless the applicant clearly demonstrated that the proposed transaction would not materially reduce competition in the market.

DIVIDENDS

48-203.1 - DIVIDENDS; PRIOR APPROVAL (Reference A.C.A. § 23-48-203)

Prior approval of the Commissioner shall be obtained prior to declaration and payment of any dividend by any State Bank which shall amount to seventy-five percent (75%) or more of the net profits of the bank after all taxes for the current year (annualized) plus seventy-five (75%) of the retained net profits for the immediately preceding year.

STOCK ISSUE AND TRANSFER
ISSUE OF STOCK

48-311.1 - PAYMENT FOR STOCK (Reference A.C.A. § 23-48-311)

Under Section 8, Article 12 of the Arkansas Constitution, corporate stock can be issued only for "money or property actually received or labor done". A bank may not issue stock against the purchaser's promissory note; and it cannot issue stock at a price less than the par value thereof. Bank of Dermott v. Measel, 172 Ark. 193; Bank of Manila v. Wallace, 177 Ark. 190; Blanks v. American So. Trust Co., 177 Ark. 832; Murray v. Murray Laboratories, Inc., 223 Ark. 907; Bank of Commerce v. Goolsby, 129 Ark. 416.

48-311.2 - DISCRIMINATORY SALES OF STOCK (Reference A.C.A. § 23-48-311)

The issuance of new shares at an inadequate price operates to dilute the value of outstanding shares. Therefore, even when the shareholders agree that shares may be sold free of preemptive rights the directors are under a fiduciary duty to fix a reasonable price for the shares thus sold.

48-313.1 - COMMON AND PREFERRED; VOTING, NONVOTING (Reference A.C.A. 23-48-313)

A bank may issue both common and preferred stock of different classifications. It may also issue voting and nonvoting stock; but stock issued as nonvoting may nevertheless vote in respect to a dissolution, merger, consolidation or in respect to any proposal that would adversely affect the preferences, privileges and other rights annexed to the shares; nor may a stockholder's right to vote, under Article 12, Section 8, of the Arkansas Constitution, upon a proposal to increase the capital stock be abridged through the issuance of nonvoting stock.

48-313.2 - FRACTIONAL SHARES; SCRIP (Reference A.C.A. § 23-48-313)

Unless prohibited by the Articles of Agreement, or any amendment thereto, or By-Laws, a bank may issue a certificate for a fractional share. The creation of fractional shares sometimes occurs in connection with stock dividends. In lieu of issuing certificates for fractional shares the bank may issue scrip. A scrip certificate specifies that the holder has rights in respect to a designated number of fractional shares; and a person holding scrip certificates covering fractional interests equal to a full share may exchange such certificates for a certificate covering one share. Unless otherwise provided in the Articles or By-Laws, a fractional share shall (but scrip will not) entitle the holder to vote or receive dividends. Where scrip is issued, the directors may provide that it shall become void unless exchanged for certificates representing full shares before a specified date. Where scrip is issued it is customary to establish certain officials as a clearing house to handle the sale of the fractional interests whose holders desire to sell and to handle the purchase for those who desire to purchase additional rights for the purpose of matching them into full shares. Further, where scrip is issued, the directors may provide that it will become void if not exchanged for certificates representing full shares before a specified date; or the State Banking Board may provide that the shares for which the scrip is exchangeable may be sold by the bank and the proceeds thereof distributed to the holders of such scrip.

48-314.1 - PREEMPTIVE RIGHTS (Reference A.C.A. § 23-48-314)

(a) Banks chartered on or prior to May 30, 1997. Unless otherwise provided by the Articles of Agreement, or an amendment thereto, every stockholder, upon the sale for cash of any new stock of the same class as that which the stockholder already holds, shall have the right to purchase his/her pro rata share thereof at a price not exceeding the price at which it may be offered to others, which price may be in excess of par. Where the Articles of Agreement, or amendment thereto, do not prohibit such preemptive rights, the terms and conditions of such rights, and the time limit fixed for the exercise thereof may be prescribed in the Articles of Agreement, or amendment, or, if not so prescribed in the Articles of Agreement, or amendment, then in the By-Laws or in the resolution of the board of directors adopted in connection with such stock increase.

(b) Banks chartered after May 30, 1997. Except as expressly provided in the Articles of Agreement, or an amendment thereto, upon the sale for cash of any new stock whether or not of the same class as the stock which is outstanding, no stockholder shall have the right to purchase any portion thereof by reason of his/her stock ownership.

48-314.2 - WAIVER OF PREEMPTIVE RIGHTS (Reference A.C.A. § 23-48-314)

The waiver of preemptive rights of a shareholder, if applicable, involves a personal act by each stockholder; and such waiver cannot be accomplished by a stockholder vote at a stockholders' meeting, except for the waiver by shareholders of any applicable preemptive rights which would attach to shares which are authorized by a due vote of the shareholders to be issued upon the conversion of any convertible capital notes or pursuant to any stock option, stock purchase, employee stock ownership plan or other compensation plan authorized by A.C.A. § 23-47-101(a)(10).

48-316.1 - STOCK ISSUANCE TO BE REPORTED (Reference A.C.A. § 23-48-316)

The initial issuance of shares of a state bank or a bank holding company which has a state bank subsidiary pursuant to the provisions of the Articles of Incorporation, or any amendment thereto, authorizing the issuance of additional shares must be reported in each instance as and when issued.

48-316.2 - TRANSFERS TO BE REPORTED (Reference A.C.A. § 23-48-316)

Every transfer of outstanding shares issued by a state bank or a bank holding company which has a state bank subsidiary shall be promptly reported to the Commissioner. If an Arkansas bank holding company is a reporting company under §§13 or 15(d) of the Securities and Exchange Act of 1934, then the reporting of the transfer of shares shall only be required once each calendar year.

48-316.3 - INFORMATION REQUIRED ON REPORTED TRANSFERS (Reference A.C.A. § 23-48-316)

Except in the case of bank holding companies which are reporting companies, the bank or the bank holding company must certify to the Commissioner the number of shares held by the transferee prior to such transfer and the name of every person known by it to be holding any shares as nominee of the transferee, or in trust for or otherwise for the benefit of such transferee, and the number of shares so held by each such person. In the case of a bank holding company which is a reporting company under the Securities and Exchange Act of 1934, the bank holding company shall promptly report after the calendar year end all transactions by any record owner of shares (other than a nominee for an institution) which owns as of the end of such calendar year 3% or more of the outstanding stock of the bank holding company. Such report shall show for each transaction by such persons the number of shares held by such person prior to such transfer and the name of every person known by the bank holding company to be holding any shares as nominee of such person, or in trust for or otherwise for the benefit of such person, and the number of shares so held.

STOCKHOLDERS' MEETINGS

48-320.1 - PROXY VOTING (Reference A.C.A. § 23-48-329)

Proxy voting is authorized. A proxy, unless it otherwise provides, will expire eleven (11) months from the date of its execution. Ordinarily, a proxy would become void upon the death or insanity of the stockholder who executed the proxy. However, a proxy may be of indefinite duration if it is coupled with an interest.

48-318.1 - NOTICE OF MEETING (Reference A.C.A. § 23-48-318)

Written notice of a special meeting must be given to the shareholders by mail according to the bylaws, but in no event for less than ten (10) days. Written notice of an annual meeting, even though only routine matters are to be considered at the meeting, must be given at least ten (10) days before the meeting. If the capital stock or the bonded indebtedness is to be increased at either a special or annual meeting, 60 days notice is required under Article 12, Section 8 of the Arkansas Constitution. The notice of a special or annual meeting should indicate the time, place and purpose of the meeting and be sent by first class mail. The act of mailing constitutes notice. Any officer may sign the notice. Moreover, at an annual meeting, if the charter is to be amended or any other extraordinary matters submitted to the stockholders, the notice of the meeting must specify that such charter amendment or other such extraordinary matters will be submitted.

48-320.2 - CUMULATIVE VOTING (Reference A.C.A. § 23-48-320)

(a) For state banks incorporated on or before May 30, 1997, unless otherwise provided in the Articles or bylaws, cumulative voting for directors or on any other issues, is permitted. Thus, if there are five (5) directors to be elected, a stockholder owning fifty (50) shares could vote fifty (50) shares for each director or the stockholder could cast two hundred fifty (250) votes for one director (A.C.A. § 23-32-222). The statute authorizes cumulative voting in connection with the election of directors or on any other issue.

(b) For state banks incorporated after May 30, 1997, cumulative voting is not permitted unless and only to the extent provided for in the Articles of Incorporation of the bank.

DIRECTORS AND STOCKHOLDERS

48-322.1 - BOARD OF DIRECTORS (Reference A.C.A. § 23-48-322)

The affairs of every bank organized under the laws of this state shall be managed and controlled by a board of directors of not less than three (3) persons who shall be selected at such times and in such manner as may be provided by its Articles of Incorporation or bylaws. Except as required in the Articles of Incorporation or bylaws, no director of a state bank shall be required to be a stockholder of such bank.

48-322.2 - OFFICER OR DIRECTOR REMOVAL (Reference A.C.A. § 23-48-322)

Any officer or director found by the Commissioner to be violating state or federal law, State Bank Department Rules and Regulations, or basic principals of safety and soundness in the operation of a bank may be reported in writing to the directors of the bank of which he is an officer or director, or the Commissioner may cause such officer or director to be removed from service to the institution by means of a cease and desist order issued by the Commissioner against the bank and its board of directors. If the Commissioner reports such activities in writing to the bank's board of directors and the Board neglects or refuses to remove such officer or director, the directors may be individually liable for any loss that may occur to the bank by reason of their lack of action and may be subject to the assessment of monetary penalties for such failure by the Commissioner.

PROCEDURE AT BANK MEETINGS
DIRECTORS' MEETINGS

48-322.3 - DIRECTORS' MEETINGS (Reference A.C.A. § 23-48-322)

The procedure at the regular and special meeting of the Board of Directors shall be governed by the terms of the Articles of Incorporation and Bylaws of the bank; provided, however, no proxy given by a director for any meeting of the Board of Directors shall be effective for determining a quorum, voting or any other purpose.

RESERVES OF BANKS

48-202 - PENALTY-FAILURE TO MAINTAIN RESERVE (Reference A.C.A. § 23-48-202)

If any state bank shall fail during any period to maintain the reserve required under the Banking Code, the Commissioner may require such bank to pay a penalty computed on the basis of eight percent (8%) per annum on the amount of such deficit for the period that the deficit continues; provided that the Commissioner, in his/her discretion, may waive any penalty for a period which is less than twenty-five dollars ($25.00). This penalty shall not prevent the Commissioner, under other applicable provisions of the law, from placing a state bank in liquidation due to a violation of reserve requirements.

SECTION 9

BRANCH BANKS

48-309.2 - BANK FICTITIOUS NAMES (Reference A.C.A. § 23-48-309)

A state bank planning to file an application for use of a fictitious name must complete the following procedures prior to filing an application with the State Bank Department:

A) Publish legal notice of intention to file an application for use of a fictitious name one (1) time in a newspaper of statewide circulation. Such notice shall include the current corporate name, the proposed fictitious name, and the location or locations where the proposed fictitious name will be used. A copy of the legal notice must accompany the application; and
B) Request a current check of both state and federal trademark or servicemark filings on the proposed fictitious name. Evidence must accompany the application for use of a fictitious name verifying the applicant has made a trademark or servicemark search and no trademark or servicemark exists for the proposed fictitious name.

Once the application for use of a fictitious name is received by the State Bank Department, notice of the filing of the application will be sent to all state-chartered banks by electronic transmission. Any protestant will have seven (7) days from the date the Department notice was sent to file an official protest to the application. An official protest must be provided to the Department in written form delineating the reasons for the protest and must be accompanied by a filing fee of twenty-five dollars ($25). The Bank Commissioner will make the final determination on the use of a fictitious name.

Notwithstanding the above requirements, an applicant bank that has previously filed and been approved for the use of a specific fictitious name is not required to perform the publication of notice or trademark search requirements for subsequent use of the same fictitious name. However, the bank must file an application for subsequent use of the same fictitious name at a new location.

FULL SERVICE BRANCHES;
LIMITED PURPOSE OFFICES

48-701 HEALTHY BANK (Reference A.C.A. § 23-48-701)

A "healthy bank" is defined as an institution meeting all of the following criteria:

1) Received a composite rating of 1 or 2 under the Uniform Financial Institutions Rating System (CAMELS) as a result of its most recent commercial bank examination;
2) Received a satisfactory or better Community Reinvestment Act (CRA) rating from its primary federal regulator at its most recent examination;
3) Received a compliance rating of 1 or 2 from its primary federal regulator at its most recent examination;
4) Is well-capitalized as defined in the appropriate capital regulation and guidance of the institution's primary federal regulator;
5) Is not subject to a cease and desist order, consent order, prompt corrective action directive, written agreement, memorandum of understanding, or board resolution with its primary federal regulator or chartering authority; and
6) Have no major unresolved supervisory issues outstanding or other significant concerns (as determined by the Commissioner).

Only a "healthy bank" is eligible to file an expedited branch application. If any one of the listed criteria is not met, a standard branch application must be filed.

48-702.1 RELOCATION OF EXISTING FULL SERVICE BRANCH (Reference A.C.A. § 23-48-702)

A state bank may file a notice with the Commissioner to relocate any existing full service branch to another location then authorized by law. The following rules govern such notice:

(a) Fees. A fee of three hundred dollars ($300) shall accompany the notice to the Commissioner as set by this regulation.

(b) Notice to the Commissioner. Written notice shall be filed with the Commissioner (on a form prescribed by the Commissioner) at least thirty (30) days prior to the proposed relocation of the existing full service branch.

(c) Publication of Notice. The state bank shall publish a notice of the proposed relocation of the existing full service branch in a newspaper of statewide circulation one (1) time prior to filing notice of relocation with the Commissioner. A proof of publication must accompany the notice of relocation to the Commissioner. The publication may be run no more than three (3) weeks before the filing of the notice.

(d) Approval by Commissioner. A notice of relocation of existing full service branch is deemed approved if the Commissioner takes no action on the notice within thirty (30) days after filing of the notice.

(e) Formal Protest. Each bank, corporation, or individual that files with the Commissioner a formal written protest to the relocation of an existing full service branch shall be required to pay a protest fee of three hundred dollars ($300). The fee must accompany or precede the formal written protest, which must be received by the Commissioner within fifteen (15) calendar days of the actual filing of the notice of relocation. The written protest must include a specific reason or reasons for protesting the relocation. Further, the State Banking Board requires all formal protests be specific to those principles set forth in A.C.A. § 23-48-703(a).

(f) Letters of Opposition. Any aggrieved bank, corporation, or individual may file a letter of opposition (not an official protest) to a notice of relocation of an existing full service branch without incurring any liability for the fee assessed to formal protesting parties.

(g) Date of Filing. Written notice to the Commissioner to relocate an existing full service branch, formal protest(s), and letter(s) of opposition are considered “filed” the date stamped as filed by the Commissioner.

(h) Public Hearing at the Commissioner’s Discretion. The Commissioner at his/her discretion may hold a public hearing on a notice of relocation of existing full service branch. If a hearing is to be held, the Commissioner shall give notice in a newspaper of statewide circulation once at least ten (10) days prior to the date of the hearing. Further, the Commissioner shall notify by mail the party sending notice of relocation and official protestant(s) at least ten (10) days prior to the hearing.

48-702.2 SHORT DISTANCE RELOCATION (Reference A.C.A. § 23-48-702)

(a) In accordance with A.C.A. § 23-48-702 (d)(5)(A) and (B), the State Banking Board rules a bank may relocate an existing full service branch within an immediate neighborhood without requiring publication of notice pursuant to Act 42 of 2007; however, the bank must file written notice of relocation within an immediate neighborhood with the Commissioner. The following rules govern such notice:

1. Fees. A fee of two hundred and fifty dollars ($250) shall accompany the notice to the Commissioner as set by this regulation.
2. Notice to the Commissioner. Written notice shall be filed with the Commissioner (on a form prescribed by the Commissioner) at least thirty (30) days prior to the proposed relocation of an existing full service branch within an immediate neighborhood.

3. Approval by Commissioner. A notice of relocation within an immediate neighborhood is deemed approved by the Commissioner if the Commissioner takes no action on the notice within thirty (30) days after filing of the notice.
4. Date of Filing. Notice to the Commissioner to relocate a branch within an immediate neighborhood is considered "filed" the date stamped as filed by the Commissioner.

(b) The statute defines "within the immediate neighborhood" as including, but not limited to:

1. Across the street;
2. Around the corner;
3. Within two (2) blocks;
4. Within one thousand feet (1000'); or
5. In densely populated areas, within five thousand feet (5000').
6. For the purpose of relocating within the immediate neighborhood, "densely populated area" is defined as a community with a population of over five thousand (5,000) people.

48-702.3 - LIMITED PURPOSES OFFICES (Reference A.C.A. § 23-48-702)

(a) Establishment of limited purpose office:

1. Within the State of Arkansas. Any bank may establish a limited purpose office anywhere in the state to conduct non-core banking activities upon satisfaction of the notice requirement set forth in this subsection.
2. Outside the State of Arkansas. Any state bank may establish a limited purpose office in another state subject to the rules and regulations of the state in which it seeks to establish the limited purpose office. The state bank must also satisfy the notice requirement set forth in this section.

(b) As to each limited purpose office which a state bank proposes to establish or use within or outside the State of Arkansas, the state bank shall give not less than thirty (30) days prior written notice of its intention to establish or use the limited purpose office to the Commissioner.

(c) The written notice to the Commissioner (on a form prescribed by the Commissioner) shall include the following information:

1. The location and general description of the surrounding area;
2. Whether the location will be owned or leased;
3. The non-core banking activities to be conducted;
4. An estimate of the initial cost of the limited purpose office; and
5. Such other relevant information as may be required by the regulatory authority.

6. If the limited purpose office involves an increase in fixed assets (acquisition of real estate or construction of facilities) the bank must request prior approval for incurring these costs.

48-703.1 EXPEDITED, STANDARD, AND MOBILE BRANCH APPLICATION PROCEDURES (Reference A.C.A. § 23-48-703)

A state bank's expedited, standard, or mobile branch application (on separate forms required by the Commissioner) for authority to establish a new branch shall be filed with the Commissioner. The following rules govern the procedure on such applications:

(a) Expedited, Standard, and Mobile Branch Applications.

1. Expedited Application. To file an expedited application, a bank must meet the criteria of a healthy bank as set forth by regulation. The application will be processed within sixty (60) days of filing with the Commissioner.
2. Standard Application. An application not filed as an expedited application will be filed as a standard application.
3. Mobile Application. A separate application must be filed with the Commissioner for each separate county the state bank proposed to operate the mobile branch

(b) Fees.

1. The sponsor(s) of an expedited branch application are required to pay a filing fee of three hundred dollars ($300) as set by regulation. This fee must accompany the filing of the application. The Commissioner at his/her discretion may or may not require a field investigation of a branch application.
2. The sponsor(s) of a standard branch application are required to pay a filing fee of five hundred dollars ($500) as set by regulation. This fee must accompany the filing of the application. The Commissioner at his/her discretion may or may not require a field investigation of a branch application.
3. The sponsor(s) of a mobile branch application are required to pay a filing fee of three hundred dollars ($300) as set by regulation. This fee must accompany the filing of the application. The Commissioner at his/her discretion may or may not require a field investigation of an application

(c) Notice Published by Applicant. The applicant, for either an expedited, standard, or mobile branch application, shall publish notice of the application in a newspaper of statewide circulation one (1) time per week for four (4) consecutive weeks prior to filing the application with the Commissioner. The application may not be filed with the Commissioner less than thirty (30) days from the date of the first publication, and not later than twenty (20) days after the fourth and final publication. A proof of publication must be submitted to the Commissioner.

(d) Notice by Commissioner. The Commissioner shall give notice of the application to Arkansas state-chartered banks with a bank or a full service branch currently open and operating within the market area of the proposed new branch. As set by this regulation, the following shall apply:

1. All state chartered banks are required to file with the Commissioner a designated officer (not to be confused with the designated agent for service of process) and email address for which service can be made on that bank for the purpose of giving notice of an expedited, standard, or mobile branch application for a new branch. All state chartered banks are required to file at least one (1) designated officer, and may file up to three (3), with the Commissioner. This must be filed with the Commissioner by state chartered banks currently open and operating within the State of Arkansas no later than March 26, 2007. All new state chartered banks open and operating after March 26, 2007, must file a designated officer and email address with the Commissioner not more than thirty (30) days from the day of opening the new state chartered bank. Failure to file this information with the Commissioner will constitute a waiver of notice in regards to expedited, standard, or mobile branch applications. Failure to file a change of designated officer and email address with the Commissioner will also constitute a waiver of notice in regards to expedited, standard, or mobile branch applications.
2. The Arkansas State Banking Board defines “market area” as within the county where the applicant proposes to open the new branch.
3. “Open and operating” is determined by checking the Federal Deposit Insurance Corporation database. Those banks having a main banking office or branch office(s) actually open and operating as of the date of the actual filing of an application, as reflected by the Federal Deposit Insurance Corporation database, in the proposed market area will receive notice from the Commissioner.
4. The Commissioner will email the banks a notice of the filing of the expedited, standard, or mobile branch application. This email will constitute as notice to the Arkansas state-chartered banks currently open and operating within the market area of the proposed new branch.
5. The Commissioner will send notice to banks entitled to notice under this subsection not more than two (2) business days from the filing of the application. The notice will include the date the application was filed.
6. An application for an expedited, standard, or mobile branch is considered “filed” the date stamped as filed by the Commissioner.

(e) Expiration of Approval. The Commissioner’s Order approving a branch application shall expire eighteen (18) months from the date of approval unless a request for extension has been approved in writing by the Commissioner.

48-703.2 MOBILE BRANCH (Reference A.C.A. § 23-48-701 and § 23-48-703)

The State Banking Board, in accordance with Act 42 of 2007, promulgates the following rules governing mobile branches:

1) A mobile branch only conducts banking business within the same county as the main office or another full service branch of the bank; A mobile branch may not have a single, permanent site;
2) A mobile branch may not remain within five (5) miles of any banking location for more than two (2) business days;
3) A mobile branch travels to various locations within the county(s) to enable customers to conduct banking business; and
4) A mobile branch must maintain a log of operations indicating the date and specific location of each stop.

48-703.3 PROTEST (Reference A.C.A. § 23-48-703)

A protest may be filed with the Commissioner as to the filing of a branch application, an expedited branch application, or a mobile branch application. The following rules govern such protest:

(a) Formal protest. Each bank, corporation, or individual must file with the Commissioner a formal written protest within fifteen (15) calendar days of the actual filing of a branch application, an expedited application, or a mobile branch application. The written protest must include a specific reason or reasons for protesting the application. The following fees apply:

1. Expedited Branch Application. A fee of three hundred dollars ($300) is required to be paid when filing a formal protest to an expedited branch application. The fee must accompany or precede the formal written protest.
2. Standard Branch Application. A fee of five hundred dollars ($500) is required to be paid when filing a formal protest to a branch application. The fee must accompany or precede the formal written protest.
3. Mobile Branch Application. A fee of three hundred dollars ($300) is required to be paid when filing a formal protest to a mobile branch application. The fee must accompany or precede the formal written protest.

(b) Letters of Opposition. Any aggrieved bank, corporation, or individual may file a letter of opposition (not an official protest) to a branch application, an expedited branch application, or a mobile branch application without incurring any liability for the fee assessed to formal protesting parties.

(c) Date of Filing. Formal written protest(s) and letter(s) of opposition filed with the Commissioner under this subsection are considered "filed" the date stamped as filed by the Commissioner.

(d) Public Hearing at Commissioner's Discretion. The Commissioner at his/her discretion, regardless of whether any formal protest or letters of opposition were filed, may hold a public hearing on a branch application, an expedited branch application, or a mobile branch application. If a hearing is to be held, the Commissioner shall give notice in a newspaper of statewide circulation once at least ten (10) days prior to the date of the hearing. Further, the Commissioner shall notify by mail the party(s) filing the application and official protestant(s) at least ten (10) days prior to the hearing.

SECTION 10

BANK HOLDING COMPANIES

(RESERVED)

SECTION 11

PLAN OF EXCHANGE

48-601.1 - AUTHORITY TO ADOPT PLAN OF EXCHANGE -- NOTICE - COURT REPORTER (Reference A.C.A. § 23-48-601)

The Commissioner requires that the bank, intending to adopt a Plan of Exchange, publish a legal notice of the Commissioner's fairness hearing in a newspaper of state-wide circulation. These notices must be published at least once, ten (10) days prior to the Commissioner's fairness hearing. Proof of publication must be delivered to the Commissioner's office. In addition, the Commissioner requires that the notice of the Commissioner's fairness hearing be included in the proxy material mailed to the stockholders of the bank at least ten (10) days prior to the date of the stockholders meeting at which the Plan of Exchange will be voted upon.

COURT REPORTER REQUIRED.

The Commissioner requires that the bank arrange for a court reporter to be present to transcribe the proceedings of the Commissioner's fairness hearing. The bank is responsible for the fees and costs of the court reporter and transcript of the proceedings.

DISSOLUTION AND LIQUIDATION

49-118.1 - EXECUTION AND FILING ARTICLES WITH DEPARTMENT. CERTIFICATE OF DISSOLUTION – FEES (Reference A.C.A. § 23-49-118)

When the dissolution of an Arkansas state-chartered bank has been completed , the receiver shall file Articles of Dissolution with the State Bank Department in accordance with the procedures as set out by state statute and accompanied by a filing fee of two hundred dollars ($200.00).

VOLUNTARY LIQUIDATION.

Applications for the voluntary liquidation of an Arkansas state-chartered bank shall be accompanied by a filing fee of two hundred dollars ($200.00).

VOLUNTARY LIQUIDATION. SURRENDER OF CHARTER.

Prior to accepting the surrender of any bank charter, applicant must provide the Commissioner with evidence satisfactory to him that all deposits and trust accounts (if any) have been sold, surrendered, transferred, or terminated.

SECTION 12

POLICY REQUIREMENTS

LOAN POLICY

I. **LOAN POLICY.** The State Banking Board hereby requires all state banks to maintain a written loan policy. A well written loan policy will, at a minimum, address the following:

A. the bank's principal trade area;

B. the bank's legal lending limit;

C. the lending authority of the bank's lending officers;

D. the principal types of loans considered suitable for the investment of depositor's funds;

E. the maturity schedule desired for various types of loans;

F. the pricing schedule desired for various types of loans;

G. the collateral requirements desired for various types of loans; and

H. the documentation requirements for various types of loans.

Furthermore, the loan policy will describe the process by which loans shall receive prior approval or subsequent approval by a loan committee and the bank's board of directors, repricing opportunities of loans subject to renewal or extensions, procedures for the purchase and sale of loan participations, and procedures for approving loans to insiders; executive officers, directors, and principal shareholders.

A bank's loan policy, and any revisions or additions, must receive the approval of the board of directors and reviews are recommended on an annual basis.

LOAN PARTICIPATION POLICY

II. **LOAN PARTICIPATION POLICY.** A state chartered bank investing in loan participations shall maintain the following credit controls over the purchase of loans, commitments to purchase loans, and loan participations: (For the purposes of this Regulation, a "loan" includes any binding agreement to advance funds on the basis of an obligation to repay the funds.)

A. written lending policies and procedures governing these transactions;

B. an independent analysis of credit quality by the purchasing bank;

C. agreement by the obligor to make full credit information available to the selling bank;

D. agreement by the selling bank to provide available information on the obligor to the purchaser; and

E. written documentation of recourse arrangements outlining the rights and obligations of each party.

III. **GUIDELINES WHEN PURCHASING.** Prudent purchases of loans, loan participations, commitments to purchase loans, and loan portfolios are governed by the credit principles and procedures embodied in the purchasing bank's formal lending policy. The policy ordinarily entails:

A. complete analysis and documentation of the credit quality of obligations to be purchased;

B. an analysis of the value and lien status of the collateral; and

C. the maintenance of full credit information of the obligor during the term of the loan.

IV. **INDEPENDENT CREDIT ANALYSIS.** To make a prudent credit decision, a purchaser conducts an independent credit analysis to satisfy itself that a loan, loan participation, or loan portfolio is a credit which it would make directly. The nature and extent of the independent analysis is a function of the type of transaction at issue and the purchaser's lending policies and procedures. Where loans are purchased in bulk, for example, a prudent purchaser might assess the credit of the class of obligors rather than each obligor.

The acceptance by a purchaser of a favorable analysis of a loan issued by the seller, a credit rating institution, or another entity does not satisfy the need to conduct an independent credit analysis. A prudent purchaser may, however, consider such analyses obtained from the seller and other sources as factors when independently assessing a loan.

V. **TRANSFERS OF CREDIT INFORMATION.**

A. **PRUDENT TRANSFER AGREEMENTS.** The indirect relationship between the obligor and the purchaser makes it difficult for the purchaser to assess the quality of the loan without the cooperation of the selling or servicing bank. The purchaser ordinarily needs to obtain full credit information on the obligor from the selling institution to perform a continuing independent assessment of the credit. Thus, a prudent purchase or participation document would generally include an agreement by the selling or servicing bank to provide credit information on the obligor to the purchasing bank on a continuing basis. To ensure that full credit information will be available to the seller, a loan document would ordinarily include an agreement by the obligor to furnish such information to the seller on a continuing basis.

The absence of prudent transfer agreements may effect a purchaser's ability to obtain, assess, and maintain sufficient credit information. Accordingly, the purchase of a loan or participation absent such transfer obligations may be viewed as an unsafe or unsound banking practice.

B. **SCOPE OF PRUDENT TRANSFERS.** Prudent transfers of credit information are sufficient in scope so as to enable a purchaser to make an informed and independent credit decision. Thus, prudent transfers encompass full and timely financial and nonfinancial information bearing on the quality of a loan.(*) Financial information ordinarily includes:

(1) accrual status;
(2) status of principal and interest payments;
(3) financial statements, collateral values, and lien status; and
(4) any factual information bearing on the continuing creditworthiness of the obligor.

VI. **RECOURSE ARRANGEMENTS.** Repurchase agreements are subject to a bank's legal lending limit. Other direct or indirect recourse arrangements, written or oral, provided by the selling bank will be considered as extensions of credit to the selling bank and be subject to the selling bank's legal loan limit.

Prudent recourse arrangements should be documented in writing and reflected on the books and records of both the buying and selling bank.

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*References to "full" and "timely" transfers of credit information are made herein to provide supervisory guidelines on safe and sound transfers of credit information. The guidelines describe the scope of transfers required for a purchaser to make an informed and independent credit decision. Apart from such supervisory considerations, use of the terms "full" and "timely" is not intended to suggest that the terms have particular legal significance; thus, other terms may be used. The drafting and negotiation of standards governing transfers of credit information is the responsibility of bank management and counsel.

LOAN LOSS RESERVE

VII. **LOAN LOSS RESERVE REQUIRED.** The State Banking Board requires that state banks maintain a reserve for loan losses in an amount commensurate with the risk inherent in the bank's loan portfolio. Additionally, the State Banking Board requires a bank's board of directors to analyze the risk in the bank's loan portfolio and make provisions for such loss account at least quarterly. Such review should be noted in the minutes of a bank's board of directors meetings.

INVESTMENT POLICY

VIII. **INVESTMENT POLICY.** The State Banking Board hereby requires all state banks to maintain a written investment policy. A well written investment policy will, at a minimum, address the following:

A. the bank's investment goals;

B. the type of investments considered eligible for the bank's investment portfolio;

C. the percent of each eligible type of investment desired to be maintained;

D. the maturity distribution and length of maturity desired for each type of investment;

E. the bank officers authorized to enter into a purchase and/or sale transaction;

F. the documentation requirements for each type of investment authorized;

G. the safekeeping procedures required; and

H. a list of each qualified, acceptable dealer with which bank officers may conduct investment business.

A bank's investment policy, and any revisions and additions, must receive the approval of the board of directors, and reviews are recommended on an annual basis.

ASSET/LIABILITY MANAGEMENT

IX. **ASSET/LIABILITY MANAGEMENT POLICY.** The State Banking Board hereby requires all state banks to develop and maintain written asset/liability management policies. A well written policy will, at a minimum, address the following:

A. the establishment of a goal of the ratio of rate sensitive assets to rate sensitive liabilities consistent with safe and sound banking practices;

B. the establishment of a net interest margin goal that the bank shall strive to maintain;

C. the establishment of liquidity goals to meet the needs of the bank;

D. the policy shall call for the establishment of an asset/liability committee which shall, at a minimum, monitor the adherence to the policy and recommend changes appropriate for the sound operation of the bank (the bank's board of directors may function as the committee);

E. the policy shall call for management to submit quarterly reports to the board of directors detailing the bank's ratio of rate sensitive assets to rate sensitive liabilities for time horizons as may be defined in the policy;

F. reports are to be reviewed by the board of directors no less frequently than quarterly and such reports are to be made a part of the minutes of the meeting.

A bank's asset/liability policy, and any revisions and addition, must receive the approval of the board of directors, and reviews are recommended on an annual basis.

Agency # 210.00

POLICY STATEMENT **MAY 3, 2000**

ORDER OF THE STATE BANK COMMISSIONER

SUBJECT: FINANCIAL SUBSIDIARIES

The Arkansas Bank Commissioner, pursuant to his authority under A.C.A. § 23-47-101(37)(c), hereby authorizes Arkansas state banks to conduct permitted activities through a "financial subsidiary" in the same manner and with the same requirements as those provided for national banks by the Office of the Comptroller of the Currency. State banks that wish to conduct any of the permitted activities through a financial subsidiary must submit an application and receive approval from the Bank Commissioner, as well as any other licensing requirements prior to entering into such activity.

Signed this 3rd day of May 2000.

SIGNED: FRANK WHITE
BANK COMMISSIONER

Agency # 210.00

POLICY STATEMENT **APRIL 7, 2003**

ORDER OF THE STATE BANK COMMISSIONER

SUBJECT: BANK PURCHASES OF LIFE INSURANCE

The Arkansas State Bank Commissioner, in accordance with his authority under A.C.A. § 23-47-101(c), hereby adopts the following policy:

Arkansas state chartered banks are authorized to purchase or take an interest in life insurance for a purpose incidental to the business of banking in accordance with the same guidelines used by the Comptroller of the Currency for national banks. For reference see OCC 2000-23 dated July 20, 2000, issued by the Office of the Comptroller of the Currency, which is reproduced following this Order.

Signed this 7th day of April 2003.

SIGNED: FRANK WHITE
BANK COMMISSIONER

Revised July 20, 2007
Candace A. Franks
Bank Commissioner

OCC 2000-23

Bank Purchase of Life Insurance

To: Chief Executive Officers of all National Banks, Department and Division Heads, and all Examining Personnel

Purpose

This circular provides general guidelines for national banks to use in determining whether they may legally purchase a particular life insurance product.

BACKGROUND

Corporate-owned life insurance (COLI) includes all life insurance that a corporation, such as a bank, purchases and owns or has a beneficial interest in. Life insurance is a financial instrument which serves many necessary and useful business purposes. However, as with most financial instruments, COLI can be complicated and is not without risk. Furthermore, COLI transactions are unique and represent activities which differ greatly from the main business activity of most corporations. Some national banks have purchased COLI without fully understanding the transactions and the associated risks.

This bulletin is designed to help national banks make informed decisions consistent with safe and sound **banking** practices. Bankers should complete a thorough analysis before purchasing COLI. This bulletin sets forth supervisory policy, including minimum standards for pre-purchase analyses, applicable to the purchase of COLI by national banks. The bulletin also includes discussions of the most common uses of COLI and the associated risks.

LEGAL AUTHORITY

The authority for national banks to purchase and hold life insurance is found in 12 USC 24 (Seventh), which provides that national banks may exercise "all such incidental powers as shall be necessary to carry on the business of **banking."** Purchases of life insurance that the OCC has found to be incidental to **banking** include key-person insurance, insurance on borrowers, insurance purchased in connection with employee compensation and benefit plans, and insurance taken as security for loans. [1] The OCC may approve other uses for bank-owned life insurance on a case-by-case basis. However, a purchase of life insurance must address a legitimate need of the bank for insurance. Life insurance may not be purchased to generate funds for the bank's normal operating expenses, for speculation, or for the primary purpose of providing estate planning benefits for bank insiders unless it is part of a reasonable compensation package. In addition, the purchase of life insurance is subject to supervisory considerations, and life insurance holdings must be consistent with safe and sound **banking** practices.

SUPERVISORY POLICY

The purchase of permanent life insurance (permanent insurance) policies subjects the policyholder to several risks. The cash surrender value (CSV) of most life insurance products is subject to credit risk. [2] Usually, the CSV is a long-term, unsecured, nonamortizing obligation of the insurance company. The CSV is also subject to several other risks, such as transaction risk, interest rate risk, liquidity risk, compliance risk, and price risk.

National banks holding life insurance in a manner inconsistent with safe and sound **banking** practices may be subject to supervisory action. This bulletin outlines supervisory considerations to be used in making this assessment. Supervisory action may include, but is not limited to, partial surrender or divestiture of affected policies.

Pre-purchase Analysis:

The safe and sound use of bank-owned life insurance depends on effective senior management and board oversight. Regardless of the bank's financial capacity and risk profile, the board must understand the role bank-owned life insurance plays in the overall business strategies of the bank.

The board's role in analyzing and overseeing bank-owned life insurance should be commensurate with the size, complexity, and risk inherent in the transaction. Although the board may delegate decision-making authority related to bank purchases of life insurance to management, the board remains responsible for ensuring that purchases of life insurance are consistent with safe and sound **banking** practices.

The objective of the pre-purchase analysis is to help ensure that the bank understands the risks, rewards, and unique characteristics of COLI. As such, each purchase or assumption of a beneficial interest in COLI should be preceded by a thorough pre-purchase analysis. At a minimum, the pre-purchase analysis should consider the following standards.

I. Determination of the Need for Insurance

The bank should determine the need for insurance by identifying the specific risk of loss or obligation to be insured against. The existence of a risk of loss or an obligation does not necessarily mean that a national bank can purchase or hold an interest in life insurance. For example, a national bank may not purchase life insurance on a borrower as a mechanism for effecting a recovery on obligations that have been charged-off, or are expected to be charged-off for reasons other than the borrower's death. [3] Also, a national bank should surrender or otherwise dispose of permanent life insurance acquired through debts previously contracted (DPC) within a short time frame, generally 90 days, of obtaining control of the policy. [4]

Additionally, the purchase of insurance to indemnify a national bank against a specific risk does not relieve a national bank from other responsibilities related to managing that risk. For example, a national bank may purchase life insurance to indemnify itself from the loss of a "key-person." However, "key-person" life insurance should not be used in place of, nor does it diminish the need for, adequate management or "key-person" succession planning. [5]

II. Quantification of the Amount of Insurance Needed

The bank should estimate the size of the obligation or the risk of loss and ensure that the amount of insurance purchased is not excessive in relation to the estimate. For such estimates, national banks may include the cost of insurance and the time value of money in determining the amount of insurance needed. The estimate of the amount of insurance needed should be based on reasonable financial and actuarial assumptions. In situations where a national bank purchases life insurance on a group of employees or a homogenous group of borrowers, it can estimate the size of the obligation or the risk of loss for the group on an aggregate basis and compare that to the aggregate amount of insurance purchased.

Purchasing or holding excessive permanent insurance may be an unsafe and unsound practice if it subjects the bank to unwarranted risks. Bank-owned life insurance subjects the bank to several risks which may be significant. The risks are explained in the "Risks Associated With COLI" section of this bulletin.

III. Vendor Selection

The vast majority of COLI purchases are made through vendors, either brokers/consultants or agents. Most corporations have used brokers/consultants. However, some corporations have purchased COLI through agents who work for specific insurance companies. It is also possible to purchase COLI directly from insurance carriers without using a vendor.

The role of the vendor, if any, depends on the type of vendor selected. For example, the vendor may be an agent of a specific insurance company who serves as the bank's primary contact with the insurance company, explains the company's various products, and helps the bank in making product selection. Or, the vendor may be an independent broker who has established working relationships with many insurance companies. In addition to being the bank's primary contact with the insurance company, the broker will work with the bank in selecting a carrier and in designing, negotiating, and administering/servicing the COLI.

The bank does not have to use a vendor. In deciding whether or not to use a vendor or what type of vendor to use, the bank should consider its knowledge of COLI, the amount of resources it can and is willing to spend servicing/administering the COLI, and the benefits a vendor may provide. Depending on the role of the vendor, the vendor's services can be extensive and critical to successful implementation and operation of a COLI plan. If the bank uses a vendor, it should make appropriate inquiries to satisfy itself regarding the vendor's ability to honor its commitments, which may be long term. In assessing the vendor's ability to honor its commitments, the bank should typically review the vendor's services, general reputation, experience, and financial capacity. The nature and thoroughness of the review should be determined by the size and complexity of the potential COLI purchase.

IV. Carrier Selection

COLI plans are typically of long duration and may represent significant risks for the bank. Therefore, carrier selection is one of the most critical steps in a COLI purchase. The bank should review the product design, pricing, and administrative services of the carrier(s) and compare them with the bank's needs. In addition, the bank should also review the carrier's ratings, general reputation, experience in the market place, and past performance. A broker/consultant, if used, may assist the bank in this regard.

Furthermore, before purchasing life insurance, the bank should perform a credit analysis on the selected carrier(s) in a manner consistent with safe and sound **banking** practices for commercial lending. A more complete discussion of the credit analysis is included in the "Credit Risk" section of this bulletin.

V. Review the Characteristics of the Available Insurance Products

There are a few basic types of life insurance products in the marketplace. However, these products can be combined and modified in many different ways. The resulting final product can be quite complex. The bank should review the characteristics of the various insurance products available. It should select the product or products with characteristics that match the institution's objectives and needs. To do this, the bank should thoroughly analyze and understand the products being considered.

When purchasing insurance on "key-persons" and individual borrowers, the bank should consider whether the bank's need for the insurance will be eliminated before the insured individual dies. In such cases, term or declining term insurance may be the most appropriate form of life insurance. [6]

VI. Analyze the Benefits of COLI

The bank should analyze the benefits of COLI purchases being considered. The analysis should include an assessment of how the purchase will accomplish the objective specified in "I. Determination of the Need for Insurance." It should also include an analysis of the anticipated performance of the insurance. A more complete discussion of this analysis is included in the "Transaction Risk" section of this bulletin.

VII. Determine the Reasonableness of Compensation Provided to the Insured Employee if the Insurance Results in Additional Compensation

Split-dollar insurance arrangements [7] typically provide additional compensation and/or other benefits to the employee. Before a national bank enters into a split-dollar arrangement, it should identify and quantify the compensation objective, and ensure that the arrangement is consistent with the stated objective. Also, the bank should combine the compensation provided by the split-dollar arrangement with all other compensation to ensure that total compensation is not excessive. Excessive compensation is prohibited as an unsafe and unsound practice. Guidelines for determining excessive compensation can be found in Appendix A to 12 CFR Part 30- Interagency Guidelines Establishing Standards for Safety and Soundness.

VIII. Analyze the Associated Risks and the Bank's Ability to Monitor and Respond to those Risks

Ownership of or beneficial interests in COLI may subject a national bank to several risks. These risks include: transaction, credit, interest rate, liquidity, compliance, and price. A bank's prepurchase analysis should include a thorough evaluation of these risks. An explanation of each risk is included in the "Risks Associated With COLI" section of this bulletin.

Furthermore, the pre-purchase analysis should allow a national bank to determine whether the transaction is consistent with safe and sound **banking** practices. In making this determination, a national bank should consider, among other things:

- The complexity of the transaction.
- The size of the transaction relative to the bank's capital.
- The diversification of the credit risk.
- The financial capacity of the bank.
- The financial capacity of the insurance carrier(s).
- The bank's ability to identify, measure, monitor, and control the associated risks.

In assessing the size of the transaction, a national bank should consider the CSV relative to its capital levels at the time of purchase. The bank should also consider projected increases in the CSV and projected changes in capital levels for the duration of the contract.

Consistent with prudent risk management practices, a national bank should establish internal quantitative guidelines. These guidelines generally limit the aggregate CSV of policies from any one insurance company and the aggregate CSV of policies from all insurance companies. Among other things, a bank should consider the legal lending limits (12 CFR Part 32) and concentration of credit guidelines (OCC Bulletin 95-7, dated February 9, 1995) when establishing the respective limits.

IX. Evaluate Alternatives

Some COLI purchases involve indemnifying the bank against a specific risk. For example, COLI is sometimes purchased to indemnify the bank against the potential for loss arising from the untimely death of a "key-person." As an alternative to purchasing COLI, a bank may choose to self-insure against this risk. Other COLI purchases are used to recover costs or provide for employee benefits. In these cases, a bank may choose to generate the necessary funds through investments instead of by purchasing insurance. Regardless of the purpose of COLI, a complete pre-purchase analysis will include an analysis of the alternatives.

X. Document Decision

The primary objective of this bulletin is to provide guidelines that will help national banks make informed decisions consistent with safe and sound **banking** practices. In doing so, national banks generally should consider the pre-purchase analysis just described. A national bank should maintain documentation adequate to show that the bank made an informed decision. The bank should continue to monitor that decision based on the standards set forth in this bulletin.

RISKS ASSOCIATED WITH COLI

For purposes of the OCC's discussion of risk, examiners assess **banking** risk relative to its impact on capital and earnings. From a supervisory perspective, risk is the potential that events, expected or unanticipated, may have an adverse impact on the bank's capital or earnings. The OCC has defined nine categories of risk for bank supervision purposes. These risks are: Credit, Interest Rate, Liquidity, Price, Foreign Exchange, Transaction, Compliance, Strategic, and Reputation. These categories are not mutually exclusive; any product or service may expose the bank to multiple risks. For analysis and discussion purposes, however, the OCC identifies and assesses the risks separately.

The applicable risks associated with COLI are: Transaction, Credit, Interest Rate, Liquidity, Compliance, and Price. The definitions of these six risks are summarized below. For complete definitions, see the "Bank Supervision Process" booklet of the Comptroller's Handbook. An analysis of how each of these risks impact the decision to purchase and hold COLI is set forth in the following paragraphs.

Transaction Risk

Transaction risk is the risk to earnings or capital arising from problems with service or product delivery. The degree of transaction risk associated with COLI is a function of a bank not fully understanding or properly implementing a transaction. In addition to following the other guidelines included in this bulletin, national banks should take two additional steps to help reduce transaction risk. Bank management should have a thorough understanding of how the insurance product works and the variables that dictate the product's performance. The variables most likely to affect product performance are the policy's interest crediting rate, [8] mortality cost, [9] and other expense charges. Typically, the most significant variable is the interest crediting rate, followed by the mortality cost. Therefore, before purchasing COLI, a national bank should analyze projected policy values (CSV and death benefits) from multiple illustrations provided by the carrier. Banks should consider using different interest crediting rates and mortality costs assumptions for each illustration.

Bank management should also understand and analyze how COLI will affect the bank's financial condition. Given the anticipated performance of the insurance, management should analyze the effect on the bank's earnings, capital, and liquidity. Management should also consider the impact on the bank's earnings and capital should the bank, for any reason, surrender the insurance before maturity at the death of the insured.

Credit Risk

Credit risk is the risk to earnings or capital arising from an obligor's failure to meet the terms of any contract with the bank or otherwise fail to perform as agreed. All life insurance policyholders are exposed to credit risk. The credit quality of the insurance company and duration of the contract are key variables. With term insurance, credit risk arises from the insurance carrier's contractual obligation to pay death benefits upon the death of the insured. Credit risk is primarily a function of the insurance carrier's ability (financial condition) and willingness to pay death benefits as promised. Credit risk may be reduced by the support provided by state insurance guaranty associations or funds. A bank's credit exposure through the ownership of term life insurance is not reflected on the bank's balance sheet.

With permanent insurance, credit risk arises from the insurance carrier's obligation to pay death benefits upon death of the insured and from its obligation to return the CSV to the policyholder upon request. The risk is similar to that with term insurance, but there are a few differences. With most permanent insurance COLI plans, the expected time frame for collection of death proceeds is extremely long term. Additionally, the CSV is an unsecured, long-term, and nonamortizing obligation of the insurance carrier. The risk inherent in the insurance company's failure to return the CSV value is, reflected on the bank's balance sheet.

Before purchasing life insurance, bank management should evaluate the financial condition of the insurance company and continue to monitor its condition on an ongoing basis. In addition to reviewing the insurance carrier's ratings, the bank should conduct an independent financial analysis consistent with safe and sound **banking** practices for commercial lending. As with lending, the depth and frequency of the analysis should be a function of the relative size and complexity of the transaction.

Interest Rate Risk

Interest rate risk is the risk to earnings or capital arising from movements in interest rates. General account [10] products expose the policyholder to interest rate risk. The interest rate risk of these products is primarily a function of the policy's interest crediting rate. Interest crediting rates are established by the insurance carrier. Over the long term, interest crediting rates are primarily a function of the carrier's investment portfolio performance. The policy's CSV is negatively affected (grows at a slower rate) by a declining interest crediting rate. Since a bank's investment in permanent insurance is recorded at the policy's CSV, the bank's earnings decline as the policy's interest crediting rate declines.

Due to the interest rate risk inherent in this product, it is particularly important that management fully understand the risk before purchasing the policy. Before purchasing permanent insurance, bank management should:

- Review the policy's past performance over various business cycles.
- Analyze projected policy values (CSV and death benefits).
- Consider having the carrier use a different interest crediting rate for each set of policy projections.

Variable or separate account [11] products may also expose the bank to interest rate risk depending on the types of assets held in the separate account. For example, if the separate account assets consist solely of Treasury securities, the bank is exposed to interest rate risk in the same way as holding Treasury securities directly in its investment portfolio. However, because the bank does not control the separate account assets, it is more difficult for the bank to control this risk. Therefore, before purchasing a separate account product, bank management should thoroughly review and understand the instruments governing the investment policy and management of the separate account. Management should understand the risk inherent within the separate account and ensure that the risk is appropriate for the bank. Also, the bank should establish monitoring and reporting systems that will enable the bank to monitor and respond to price fluctuations.

Liquidity Risk

Liquidity risk is the risk to earnings or capital arising from a bank's inability to meet its obligations when they come due, without incurring unacceptable losses. Usually, life insurance policies are not marketable and are illiquid. A secondary market for life insurance does not exist. Although the CSV of policies can be accessed quickly, it typically involves substantial loss. To access the CSV, the bank must withdraw from or borrow against the policy. This may subject the bank to surrender charges, taxes on the gain, and a tax penalty. In addition, the policyholder generally does not receive any cash flow until the death benefit is paid. The lack of liquidity in the product is more significant given that banks normally purchase life insurance policies through a conversion of a liquid asset (cash or marketable securities).

Before purchasing permanent insurance, management should recognize the illiquid nature of the product and ensure the bank has the long-term financial flexibility to hold this asset in accordance with its expected use. The inability of a bank to hold the life insurance until maturity (collection of death benefits) may compromise the success of the COLI plan.

Compliance Risk

Compliance risk is the risk to earnings or capital arising from violations of, or non-conformance with, laws, rules, regulations, prescribed practices, or ethical standards. Failure to comply with applicable laws, rules, regulations, and prescribed practices (including this bulletin) could compromise the success of a COLI program and result in significant losses for the bank as a result of fines, penalties, or loss of tax benefits. Because tax benefits are critical to the success of most COLI plans, management of a national bank should exercise caution to ensure that its plans comply with all applicable tax laws. In addition, bank management should ensure compliance with other applicable legal and regulatory standards. Other common legal and regulatory considerations include compliance with state insurable interest laws, the Employee Retirement Income Security Act of 1974 (ERISA), sections 23A and 23B of the Federal Reserve Act, 12 CFR Part 215 (Regulation O), and Appendix A to 12 CFR Part 30--Interagency Guidelines Establishing Standards for Safety and Soundness. Due to the significance of the compliance risk, a national bank may want to seek the advice of qualified counsel.

Price Risk

Price risk is the risk to earnings or capital arising from changes in the value of portfolios of financial instruments. Typically, the policyholder of separate account products assumes all price risk associated with the investments within the separate account. Usually, neither the CSV nor the interest crediting rate on separate account products is guaranteed by the carrier. The amount of price risk is dependent upon the type of assets held within the separate account.

Because the bank does not control the separate account assets, it is more difficult for the bank to control the price risk. Therefore, before purchasing a separate account life insurance product, bank management should thoroughly review and understand the instruments governing the investment policy and management of the separate account. Management should understand the risk inherent in the separate account and ensure that the risk is appropriate for the bank. Also, bank management should establish monitoring and reporting systems that will enable them to monitor and respond to price fluctuations.

Banks may purchase separate account insurance products that hold equity securities for the purpose of hedging their obligations under employee compensation and benefit plans. [12] This lessens the effect of price risk on the bank's financial statements because changes in the amount of the bank's liability will be hedged by changes in the value of the separate account assets. An example of such a relationship would be where the amount of the bank's deferred compensation obligation is measured by the value of a stock market index, and the separate account contains a stock mutual fund that mirrors the performance of that index. If the insurance cannot be characterized as an effective hedging transaction, the presence of equity securities in a separate account is impermissible.

In addition to the general considerations discussed above, which are applicable to any separate account product, further analysis should be performed when purchasing a separate account product involving equity securities. At a minimum, national banks should:

1. Analyze the bank liability being hedged (e.g., deferred compensation) and the equity securities to be held as a hedge in the separate account. Such an analysis usually documents the correlation between the liability and the equity securities, expected returns for the securities (including standard deviation of returns), and current and projected asset and liability balances.

2. Determine a target hedge effectiveness ratio and establish a method for measuring hedge effectiveness. Establish a process for altering the program if hedge effectiveness drops below acceptable levels. Consideration should be given to the potential costs of program changes.

3. Establish a process for analyzing and reporting the effect of the hedge on the bank's income statement and capital ratios. Such an analysis usually shows results both with and without the hedging transaction. O

ACCOUNTING CONSIDERATIONS

National banks should follow generally accepted accounting principles (GAAP) for financial reporting and Call Report purposes. Financial Accounting Standards Board (FASB) Technical Bulletin 85-4, "Accounting for Financial Purchases of Life Insurance" (TB 85-4) discusses how to account for investments in life insurance. The guidance set forth in TB 85-4 is generally appropriate for all forms of COLI.

Under TB 85-4, a national bank should record its interest in the policy's CSV as an "other asset." The increase in the CSV over time would be recorded as "other noninterest income." In accordance with Call Report requirements, the bank should update its interest in the CSV at least quarterly.

APPLICATION OF THE GUIDELINES

The guidelines in this bulletin are applicable to all purchases of life insurance entered into after the date of this bulletin. Purchases of life insurance policies entered into before the date of this bulletin will be evaluated in the following manner.

Policies purchased after issuance of former **Banking Circular (BC)-249,** Bank Purchases of Life Insurance

Policies purchased after February 4, 1991, should comply with either the guidelines contained in former BC-249 or with the guidelines in this bulletin.

Policies Purchased before the issuance of former BC-249, Bank Purchases of Life Insurance

Policies purchased before February 4, 1991, are provided a "safe harbor" if the following three conditions are met:

- The policies are convenient or useful in connection with the conduct of the bank's business.
- The policies do not threaten the safety and soundness of the, institution.
- The policies do not represent insider abuse or violate other laws, rules, or regulations.

If these conditions are met, no further action by the bank is needed. However, the OCC may require corrective action at any time during the bank's ownership or while it has a beneficial interest in a policy, if any of the three conditions are not met. Such determinations will be made on a case by case basis.

ORIGINATING OFFICE

For further information about this bulletin, contact the Office of the Deputy Comptroller for Credit Risk at (202) 874-5170.

APPENDIX

COMMON TYPES OF LIFE INSURANCE POLICIES

Life insurance can be categorized into two broad types, temporary insurance and permanent insurance. There are numerous variations of these products. However, basic life insurance provisions generally fall within one or a combination of the following categories.

Temporary Insurance

Temporary insurance consists of the various forms of term insurance. Term insurance provides life insurance protection for a specified time period. Death benefits are payable only if the insured dies during the specified period. If a loss does not occur during the specified term, the policy lapses and provides no further protection. All premiums are retained by the insurance company. Typically, term insurance premiums do not have a "savings component"; thus, term insurance does not usually create cash value.

Permanent Insurance

Permanent insurance is intended to provide life insurance protection for the entire life of the insured. Permanent insurance also differs from term insurance in that its premium structure includes a "savings component." Permanent insurance policy premiums have two components, the insurance cost (mortality cost, [1] administrative fees, sales loads, etc.) and the "savings component." The "savings component" typically is referred to as cash value. The policyholder may use the cash value to make the minimum premium payments necessary to maintain the death benefit protection, may access the cash value by taking out loans or making partial surrenders, or use any combination of these techniques. If permanent insurance is surrendered before death, a surrender charge may be assessed against the cash value. Generally, surrender charges are assessed if the policy is surrendered within the first 10 or 15 years. The amount of money a policyholder will receive upon surrendering a policy is referred to as the cash surrender value (CSV).

There are a variety of types of permanent insurance. Some of these include:

- Whole Life--A traditional form of permanent insurance designed so that fixed premiums are paid for the entire life of the insured. However, premiums may be paid from the CSV. Death benefit protection is provided for the life of the insured, assuming all premiums are paid.

- Universal Life--A form of permanent insurance designed to provide flexibility in premium payments and death benefit protection. The policyholder can pay maximum premiums and maintain a very high cash value. Alternatively, the policyholder can make minimal payments in an amount just large enough to cover mortality and other expense charges.

- General Account--form of whole or universal life insurance where the policyholder's cash value is supported by the general assets of the insurance company.

- Variable or Separate Account--form of whole life or universal life where the policyholder's cash value is supported by assets segregated from the general asset structure of the carrier. Theoretically, the cash value of a separate account insurance policy can go down to zero which would result in termination of the policy. The policyholder assumes all investment and price risk. The separate account is used solely for payment of policyholder benefits.

LIFE INSURANCE AS A FINANCING OR COST RECOVERY VEHICLE FOR BENEFITS PLANS

National banks may, as other corporations frequently do, use corporate-owned life insurance (COLI) as a financing or cost recovery vehicle for pre- and post-retirement employee benefits. In these arrangements, banks and other corporations insure the lives of certain employees to reimburse the corporation for the cost of employee benefits. The group of insured employees is often different from the group of employees who receive benefits. The corporation's obligation to provide employee benefits is separate and distinct from the purchase of the life insurance. The life insurance purchased by the corporation remains a corporate asset even after the employer/employee relationship is terminated. The employees, whether insured or not, have no interest in the insurance (other than their general claim against corporate assets arising from the corporation's obligation to provide the stated benefits). Permanent insurance is used for this purpose.

There are two common methods of financing or effecting cost recovery of employee benefits. The first is the cost recovery method. Under this method, the corporation sustains the cost of providing the employee benefits and the cost of purchasing the life insurance. The corporation holds the life insurance and collects the death benefit to reimburse the corporation for the cost of the benefits and the insurance.

The cost recovery method usually involves present value analysis. The corporation typically projects the dollar amounts of the expected benefits owed to employees and determines the present value of the benefits. Then, the corporation purchases a sufficient amount of life insurance on the lives of certain employees so that the gain (present value of the life insurance proceeds less the present value of the premium payments) from the insurance proceeds reimburses the corporation for the benefit payments.

The second method of financing employee benefits is known as cost offset. With this method, the corporation projects the annual employee benefit expense associated with the benefit plan. Then, the company purchases life insurance on the lives of certain employees. The amount of insurance purchased is great enough so that the income earned on the CSV offsets the benefit expense. The collection of death benefits may further enhance the company's return.

SPLIT-DOLLAR INSURANCE ARRANGEMENTS

National banks may, as many other corporations do, use split-dollar life insurance arrangements to provide retirement benefits and/or death benefits to certain employees. Under split-dollar arrangements, the employer and the employee share the rights to the policy's CSV and death benefits. The employer and the employee may share premium payments. If the employer pays the entire premium, the employee must recognize the economic value of the insurance as taxable income each year. Typically, split-dollar arrangements are set forth in written contracts that specify the terms and conditions of the agreement between the employer and employee.

Split-dollar arrangements may be structured in a number of ways. However, there are three basic types of split-dollar arrangements.

Endorsement Split-Dollar

In endorsement split-dollar arrangements, the employer owns the policy and controls all rights of ownership. The employer provides the employee an endorsement of the death benefit provided to the employee under the plan agreement. The employee may designate a beneficiary for the designated portion of the death benefit.

Under this arrangement, the employer typically holds the policy until the employee's death. At that time, the employee's beneficiary receives the designated portion of the death benefits, and the employer receives the remainder of the death benefits.

Collateral Assignment Split-Dollar

The employee owns the policy and controls all rights of ownership. Under these arrangements, the employer usually pays the entire premium or a substantial part of the premium. The employee assigns a collateral interest in the policy to the employer that is equal to the employer's interest in the policy. The employer's interest in the policy usually is equal to the premium paid by the employer or the premium plus a return on the premium.

Under this arrangement, the employee upon retirement usually has an option to buy the employer's interest in the policy. The employee usually withdraws money from the cash value or borrows against the cash value to purchase the policy. Sometimes, the employer may give the employee a bonus to purchase the employer's interest in the policy, or the employer may simply give the employee the corporation's interest in the policy as a bonus. This transfer of the employer's interest to the employee is typically referred to as a "roll-out."

If a "roll-out" is not provided or exercised, the employer does not receive its interest in the policy until the employee's death. Upon the employee's death, the employer would receive an amount equal to the premium paid or the premium plus a return on the premium. The employee's beneficiary would receive the remainder of the death benefits.

If the employee dies before reaching retirement age, the insurance policy's death benefit may be divided a number of ways. For example, the employer may receive an amount equal to the premium paid or the premium plus a return on the premium, and the employee's beneficiary would receive the remainder of the death benefit. As an alternative, the employer may retain the policy's entire death benefit.

Reverse Split-Dollar

Reverse split-dollar arrangements are very similar to collateral assignment split-dollar. The employee owns the policy and the employee provides the employer with an endorsement of part of the death benefit. The employer's interest in the policy is usually equal to or closely related to the pure insurance protection and used as "key-person" insurance. The employer's share of the premium is equal to the economic value of the pure insurance protection. The employee's interest in the policy is typically equal to or closely related to the cash value of the policy. The employee pays the remainder of the premium. This type of split-dollar arrangement is not frequently used in banks.

Split-Dollar Insurance Arrangements Used for Estate Planning Purposes or to Fund Buy-Sell Agreements

National banks may use split-dollar insurance arrangements as an estate planning tool for insiders or to fund buy-sell arrangements between the bank and insiders. However, such arrangements should be part of a reasonable compensation program. As stated in part VII of the pre-purchase analysis, national banks should combine the additional compensation provided to the insured by the split-dollar arrangement with all other compensation provided to the insured. Furthermore, national banks should ensure that total compensation provided to the insured is not excessive. Excessive compensation is prohibited as an unsafe and unsound practice. Guidelines for determining excessive compensation can be found in Appendix A to 12 CFR Part 30-Interagency Guidelines Establishing Standards for Safety and Soundness.

Typically, shareholders and other insiders who are not bank employees or directors do not provide goods or services to the bank and do not receive compensation. Therefore, national banks should only participate in such arrangements as a means of providing compensation for goods or services provided by insiders.

"KEY-PERSON" INSURANCE

A national bank may obtain life insurance to protect itself against the loss of "key-persons." As such, a national bank may purchase insurance on the life of an employee whose death would be of such consequence to the bank as to give it an insurable interest in his or her life. Certain directors of the bank may also be "key-persons."

The purpose of "key-person" insurance is to indemnify the bank against a potential loss of net income that may result from the untimely death of the insured employee. The determination of whether an individual is a "key-person" does not turn on that individual's status as an officer, but on the nature of the individual's economic contribution to the bank.

The first step in indemnifying a bank against the loss of a "key-person" is to identify the "key- person." In essence, a "key-person" is anyone whose absence for an extended period of time would result in a significant loss of net income for the bank. The next and possibly most difficult step is estimating the value of the "key-person." The value of the employee is an estimate of the potential loss of net income that the bank may incur from the untimely death of the "key-person." This value should be an estimate of the impact on net income from the loss of revenues, increased expenses, loss of operating efficiency, or other profit reductions that may result from the untimely death of the "key-person." This estimate of loss should represent a significant amount of the bank's profit or profit potential.

Determining the value of a "key-person" is not easy. Also, the most appropriate method for determining the value of a "key-person" is dependent upon the individual circumstances that created the "key-person" status. For these reasons, the OCC has not established a formula nor a specific process for estimating the value a "key-person" brings to a bank. Instead, the OCC affords bank management the opportunity to consider and analyze all relevant factors, and use their judgment to make the decision.

Additionally, "key-person" life insurance should not be used in place of, and does not diminish the need for, adequate management or "key-person" succession planning. Indeed, if a bank has an adequate management or "key-person" succession plan, its reliance on a "key-person" should decline as the person gets closer to retirement. Since a bank's reliance on a "key-person" declines as the individual moves toward retirement, the potential loss of net income which may result from the death of a "key-person" also should diminish.

As previously stated, holding permanent insurance in an amount in excess of the bank's risk of loss may be an unsafe and unsound practice. [2] Once an individual, because of retirement, resignation, discharge, change of responsibilities, or for any other reason, is no longer a "key-person" for the bank, the bank's risk of loss has been eliminated. Therefore, national banks may be required to surrender or otherwise dispose of life insurance held on a former "key-person." For this reason, the economic consequences of terminating the insurance should be considered in selecting the type of insurance and in structuring the policy. Typically, term or declining term insurance may be the most appropriate form of life insurance for "key-person" protection. It also may be appropriate to use permanent insurance that allows the substitution of insureds to provide for this protection.

LIFE INSURANCE ON BORROWERS

State law generally recognizes that a lender has an insurable interest in the life of a borrower to the extent of the borrower's obligation to the lender. In some states, the lender's insurable interest may equal the borrower's obligation plus the cost of insurance and the time value of money. Furthermore, national banks may protect themselves against the risk of loss from the death of a borrower. That protection may be provided through self-insurance in the form of debt cancellation contracts, or by the purchase of life insurance policies on borrowers.

National banks can take two approaches in purchasing life insurance on borrowers. First, a. national bank can purchase life insurance on an individual borrower for the purpose of protecting the bank specifically against loss arising from that borrower's death. Second, a national bank may employ a cost recovery technique similar to that used in conjunction with employee benefit plans. Under this method, the bank insures a group of borrowers in a homogenous pool of loans for the purpose of protecting the bank from loss arising from the death of any borrower in the homogenous pool. Examples of homogenous pools of loans include consumer loans that have distinctly similar characteristics such as automobile loans, credit card loans, and residential real estate mortgages.

Regardless of which approach is used, national banks should adhere to part 11 of the pre-purchase analysis. That is, banks should determine the risk of loss and ensure that the amount of insurance purchased is not excessive in relation to that estimate. When purchasing insurance on individual borrowers, bank management should, given the facts and circumstances known at the time of the insurance purchase, take reasonable efforts to ensure that the expected insurance proceeds match the expected repayment terms of the debt. To accomplish this, management should estimate the risk of loss over the life of the loan and match the anticipated insurance proceeds to the risk of loss. The insurance policy should be structured so that the expected death proceeds never substantially exceed the risk of loss. Generally, the risk of loss will be closely related to the outstanding principal of the debt. To properly structure the insurance policy, consideration should be given to the repayment terms of the debt. For example, for amortizing credit, banks should typically choose declining term insurance where the death proceeds are decreasing in amounts that match the loan amortization.

As previously stated, holding permanent insurance in an amount in excess of the bank's risk of loss may be an unsafe and unsound practice. [3] Once a credit is repaid, otherwise satisfied in full, or charged-off, the bank's risk of loss has been eliminated. Therefore, national banks may be required to surrender or otherwise dispose of life insurance on individual borrowers under these circumstances. For this reason, the economic consequences of terminating the insurance should be considered in selecting the type of insurance and in structuring the policy. Typically, term or declining term insurance is the most appropriate form of life insurance for insuring the lives of individual borrowers.

When purchasing life insurance on borrowers in a homogenous pool of loans, bank management should, given the facts and circumstances known at the time of the insurance purchase, take reasonable efforts to match the insurance proceeds on an aggregate basis to the total outstanding loan balances. If allowed by state law, national banks may match the insurance proceeds to the outstanding loan balances plus the cost of insurance on either a present value or future value basis. This relationship should be maintained throughout the duration of the program. When using this aggregate or group concept, it is acceptable for banks to continue to hold policies on the lives of borrowers that have been charged-off. However, loans in the homogeneous pool cannot include loans that have been charged-off. This will help ensure that national banks using this approach do not hold life insurance once the risk of loss has been eliminated.

The purchase of life insurance on a borrower is not an appropriate mechanism for effecting a recovery on obligations that have been charged-off, or are expected to be charged-off for reasons other than the borrower's demise. In the case of charged-off loans, the purchase of life insurance does not protect the bank from a risk of loss since the loss has already occurred. Since the insurance does not protect the bank from a risk of loss, the bank does not need the insurance. Holding insurance the bank does not need may subject the bank to unwarranted risks, an unsafe and unsound **banking** practice. In the case of loans the bank expects to charge-off for reasons other than the borrower's demise, the risk of loss is so pronounced that the purchase of life insurance by the bank would be purely speculative and an unsafe and unsound **banking** practice.

LIFE INSURANCE AS SECURITY FOR LOANS

National banks may take an interest in an existing life insurance policy as security for a loan. National banks also may make loans to individuals to purchase life insurance, taking a security interest in the policy. As with any other type of lending, extensions of credit secured by life insurance should be made on terms that are consistent with safe and sound **banking** practices. For instance, the borrower should be obligated to repay the loan according to an appropriate amortization schedule.

Generally, a national bank may not rely on its security interest in a life insurance policy to extend credit on terms that excuse the borrower from making interest and principal payments during the life of the borrower with the result that the bank is repaid only when the policy matures at the death of the insured. Lending on such terms is generally speculative and an unsafe and unsound **banking** practice.

Frequently, banks acquire ownership of life insurance policies through debts previously contracted (DPC). That is, banks invoke their security interest in a policy after a borrower defaults. Life insurance policies do not have a secondary market. National banks should surrender or otherwise dispose of permanent life insurance acquired through DPC within a short time frame, generally 90 days, of obtaining control of the policy. It is possible that a national bank may find a means to dispose of permanent life insurance acquired through DPC which would require a longer holding period. Therefore, a national bank may request an extended holding period from its supervisory office. In order to receive an extension, the bank should have a well-documented plan that is reasonably certain to allow the bank to dispose of the policy through means other than speculating on the death of the insured. Additionally, the extended holding period should be in the best interest of the bank.

National banks may retain temporary insurance until the next renewal date or the next premium date, whichever comes first. National banks may not continue to make premium payments on term insurance acquired through DPC. This activity is speculative and an unsafe and unsound **banking** practice.

Emory W. Rushton

Senior Deputy Comptroller for Bank Supervision Policy

[1]The appendix contains a discussion of each of these four uses of COLI.

[2]Permanent insurance and cash surrender value are described in the appendix on page 1.

[3]The purchase of life insurance on borrowers whose obligations have been charged-off, or are expected to be charged-off, is further discussed in the appendix on pages 6-7.

[4]Life insurance acquired through DPC is further discussed in the appendix on page 7.

[5]The relationship between "key-person" insurance and management succession planning is discussed in the appendix on pages 4-5.

[6]"Key-person" insurance and life insurance on borrowers are discussed further in the appendix on pages 4-7.

[7]Split-dollar insurance arrangements are defined and discussed in the appendix on pages 3-4.

[8]The interest crediting rate refers to the gross yield on the investment in the insurance policy, i.e., the rate at which the cash value increases before considering any deductions for mortality cost, load charges, or other costs that are periodically charged against the policy's cash value. Insurance companies frequently disclose a current interest crediting rate and a guaranteed minimum interest crediting rate. The guaranteed rate may be less than the current rate. As a result, the potential exists for future declines in the interest crediting rate.

[9]Mortality cost represents the cost imposed on the policyholder by the insurance company to cover the amount of pure insurance protection for which the insurance company is at risk.

[10]General account products are defined in the appendix on page 2.

[11]Variable or separate account products are defined in the appendix on page 2.

[12]An economic hedge exists when changes in the value of the liability or other risk exposure being hedged are offset by counterbalancing changes in the value of the hedging instrument.

[1]Mortality cost represents the cost imposed on the policyholder by the insurance company to cover the amount of pure insurance protection for which the insurance company is at risk. With term insurance, the insurance company is generally exposed to risk of loss for the entire face amount of the policy. With permanent insurance, the net amount at risk for the insurance company is the difference between the policy's death benefit and the cash value,

[2]See part (II), Quantification of the Amount of Insurance Needed, of the pre-purchase analysis on page 4 of the bulletin.

[3]See part (II), Quantification of the Amount of Insurance Needed, of the pre-purchase analysis on page 4 of the bulletin.

Agency # 210.00

POLICY STATEMENT **JULY 14, 2003**

ORDER OF THE STATE BANK COMMISSIONER

SUBJECT: DEBT CANCELLATION CONTRACTS AND DEBT SUSPENSION AGREEMENTS

Arkansas State Banks are authorized, pursuant to A.C.A. § 23-47-101(a)(33), to enter into agreements to provide for losses arising from the cancellation of outstanding loans upon the death of borrowers. In order to further authorize this activity, the Arkansas State Bank Commissioner, in accordance with his authority under A.C.A. § 23-47-101(c), hereby adopts the following policy:

Arkansas state chartered banks are authorized to enter into debt cancellation contracts and debt suspension agreements and charge a fee therefore, in connection with extensions of credit that it makes in accordance with the same guidelines used by the Comptroller of the Currency for national banks. For reference see 12 C.F.R. Part 37, effective June 16, 2003, which is reproduced following this order.

Signed this 14th day of July 2003.

SIGNED: ROBERT H. ADCOCK, JR.
BANK COMMISSIONER

Revised July 20, 2007
Candace A. Franks
Bank Commissioner

12 C.F.R. Part 37, Effective June 16, 2003

Debt Cancellation Contracts and Debt Suspension Agreements

Sec.

Authority: 12 U.S.C. 1 *et seq.*, 24(Seventh), 93a, 1818.

Source: 67 FR 58962, September 19, 2002, unless otherwise noted.

§ 37.1 Authority, purpose, and scope.

(a) *Authority*. A national bank is authorized to enter into debt cancellation contracts and debt suspension agreements and charge a fee therefor, in connection with extensions of credit that it makes, pursuant to 12 U.S.C. 24(Seventh).

(b) *Purpose*. This part sets forth the standards that apply to debt cancellation contracts and debt suspension agreements entered into by national banks. The purpose of these standards is to ensure that national banks offer and implement such contracts and agreements consistent with safe and sound banking practices, and subject to appropriate consumer protections.

(c) *Scope.* This part applies to debt cancellation contracts and debt suspension agreements entered into by national banks in connection with extensions of credit they make. National banks' debt cancellation contracts and debt suspension agreements are governed by this part and applicable Federal law and regulations, and not by part 14 of this chapter or by State law.

§ 37.2 Definitions.

For purposes of this part:

(a) *Actuarial method* means the method of allocating payments made on a debt between the amount financed and the finance charge pursuant to which a payment is applied first to the accumulated finance charge and any remainder is subtracted from, or any deficiency is added to, the unpaid balance of the amount financed.

(b) *Bank* means a national bank and a Federal branch or Federal agency of a foreign bank as those terms are defined in part 28 of this chapter.

(c) *Closed-end credit* means consumer credit other than open-end credit as defined in this section.

(d) *Contract* means a debt] cancellation contract or a debt suspension agreement.

(e) *Customer* means an individual who obtains an extension of credit from a bank primarily for personal, family or household purposes.

(f) *Debt cancellation contract* means a loan term or contractual arrangement modifying loan terms under which a bank agrees to cancel all or part of a customer's obligation to repay an extension of credit from that bank upon the occurrence of a specified event. The agreement may be separate from or a part of other loan documents.

(g) *Debt suspension agreement* means a loan term or contractual arrangement modifying loan terms under which a bank agrees to suspend all or part of a customer's obligation to repay an extension of credit from that bank upon the occurrence of a specified event. The agreement may be separate from or a part of other loan documents. The term debt suspension agreement does not include loan payment deferral arrangements in which the triggering event is the borrower's unilateral election to defer repayment, or the bank's unilateral decision to allow a deferral of repayment.

(h) *Open-end credit* means consumer credit extended by a bank under a plan in which:

(1) The bank reasonably contemplates repeated transactions;

(2) The bank may impose a finance charge from time to time on an outstanding unpaid balance; and

(3) The amount of credit that may be extended to the customer during the term of the plan (up to any limit set by the bank) is generally made available to the extent that any outstanding balance is repaid.

(i) *Residential mortgage loan* means a loan secured by 1-4 family, residential real property.

§ 37.3 Prohibited practices.

(a) *Anti-tying*. A national bank may not extend credit nor alter the terms or conditions of an extension of credit conditioned upon the customer entering into a debt cancellation contract or debt suspension agreement with the bank.

(b) *Misrepresentations generally*. A national bank may not engage in any practice or use any advertisement that could mislead or otherwise cause a reasonable person to reach an erroneous belief with respect to information that must be disclosed under this part.

(c) *Prohibited contract terms*. A national bank may not offer debt cancellation contracts or debt suspension agreements that contain terms:

(1) Giving the bank the right unilaterally to modify the contract unless:

(i) The modification is favorable to the customer and is made without additional charge to the customer; or

(ii) The customer is notified of any proposed change and is provided a reasonable opportunity to cancel the contract without penalty before the change goes into effect; or

(2) Requiring a lump sum, single payment for the contract payable at the outset of the contract, where the debt subject to the contract is a residential mortgage loan.

§ 37.4 Refunds of fees in the event of termination or prepayment of the covered loan.

(a) *Refunds*. If a debt cancellation contract or debt suspension agreement is terminated (including, for example, when the customer prepays the covered loan), the bank shall refund to the customer any unearned fees paid for the contract unless the contract provides otherwise. A bank may offer a customer a contract that does not provide for a refund only if the bank also offers that customer a bona fide option to purchase a comparable contract that provides for a refund.

(b) *Method of calculating refund*. The bank shall calculate the amount of a refund using a method at least as favorable to the customer as the actuarial method.

§ 37.5 Method of payment of fees.

Except as provided in **§** 37.3(c)(2), a bank may offer a customer the option of paying the fee for a contract in a single payment, provided the bank also offers the customer a *bona fide* option of paying the fee for that contract in monthly or other periodic payments. If the bank offers the customer the option to finance the single payment by adding it to the amount the customer is borrowing, the bank must also disclose to the customer, in accordance with **§** 37.6, whether and, if so, the time period during which, the customer may cancel the agreement and receive a refund.

§ 37.6 Disclosures.

(a) *Content of short form of disclosures*. The short form of disclosures required by this part must include the information described in appendix A to this part that is appropriate to the product offered. Short form disclosures made in a form that is substantially similar to the disclosures in appendix A to this part will satisfy the short form disclosure requirements of this section.

(b) *Content of long form of disclosures*. The long form of disclosures required by this part must include the information described in appendix B to this part that is appropriate to the product offered. Long form disclosures made in a form that is substantially similar to the disclosures in appendix B to this part will satisfy the long form disclosure requirements of this section.

(c) *Disclosure requirements; timing and method of disclosures*--(1) *Short form disclosures*. The bank shall make the short form disclosures orally at the time the bank first solicits the purchase of a contract.

(2) *Long form disclosures*. The bank shall make the long form disclosures in writing before the customer completes the purchase of the contract. If the initial solicitation occurs in person, then the bank shall provide the long form disclosures in writing at that time.

(3) *Special rule for transactions by telephone*. If the contract is solicited by telephone, the bank shall provide the short form disclosures orally and shall mail the long form disclosures, and, if appropriate, a copy of the contract to the customer within 3 business days, beginning on the first business day after the telephone solicitation.

(4) *Special rule for solicitations using written mail inserts or "take one" applications*. If the contract is solicited through written materials such as mail inserts or "take one" applications, the bank may provide only the short form disclosures in the written materials if the bank mails the long form disclosures to the customer within 3 business days, beginning on the first business day after the customer contacts the bank to respond to the solicitation, subject to the requirements of **§** 37.7(c).

(5) *Special rule for electronic transactions*. The disclosures described in this section may be provided through electronic media in a manner consistent with the requirements of the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. 7001 et seq.

(d) *Form of disclosures*--(1) *Disclosures must be readily understandable*. The disclosures required by this section must be conspicuous, simple, direct, readily understandable, and designed to call attention to the nature and significance of the information provided.

(2) *Disclosures must be meaningful*. The disclosures required by this section must be in a meaningful form. Examples of methods that could call attention to the nature and significance of the information provided include:

(i) A plain-language heading to call attention to the disclosures;

(ii) A typeface and type size that are easy to read;

(iii) Wide margins and ample line spacing;

(iv) Boldface or italics for key words; and

(v) Distinctive type style, and graphic devices, such as shading or sidebars, when the disclosures are combined with other information.

(e) *Advertisements and other promotional material for debt cancellation contracts and debt suspension agreements*. The short form disclosures are required in advertisements and promotional material for contracts unless the advertisements and promotional materials are of a general nature describing or listing the services or products offered by the bank.

§ 37.7 Affirmative election to purchase and acknowledgment of receipt of disclosures required.

(a) *Affirmative election and acknowledgment of receipt of disclosures*. Before entering into a contract the bank must obtain a customer's written affirmative election to purchase a contract and written acknowledgment of receipt of the disclosures required by Sec. 37.6(b). The election and acknowledgment information must be conspicuous, simple, direct, readily understandable, and designed to call attention to their significance. The election and acknowledgment satisfy these standards if they conform with the requirements in Sec. 37.6(b) of this part.

(b) *Special rule for telephone solicitations*. If the sale of a contract occurs by telephone, the customer's affirmative election to purchase may be made orally, provided the bank:

(1) Maintains sufficient documentation to show that the customer received the short form disclosures and then affirmatively elected to purchase the contract;

(2) Mails the affirmative written election and written acknowledgment, together with the long form disclosures required by **§** 37.6 of this part, to the customer within 3 business days after the telephone solicitation, and maintains sufficient documentation to show it made reasonable efforts to obtain the documents from the customer; and

(3) Permits the customer to cancel the purchase of the contract without penalty within 30 days after the bank has mailed the long form disclosures to the customer.

(c) *Special rule for solicitations using written mail inserts or "take one"' applications*. If the contract is solicited through written materials such as mail inserts or "take one" applications and the bank provides only the short form disclosures in the written materials, then the bank shall mail the acknowledgment of receipt of disclosures, together with the long form disclosures required by **§** 37.6 of this part, to the customer within 3 business days, beginning on the first business day after the customer contacts the bank or otherwise responds to the solicitation. The bank may not obligate the customer to pay for the contract until after the bank has received the customer's written acknowledgment of receipt of disclosures unless the bank:

(1) Maintains sufficient documentation to show that the bank provided the acknowledgment of receipt of disclosures to the customer as required by this section;

(2) Maintains sufficient documentation to show that the bank made reasonable efforts to obtain from the customer a written acknowledgment of receipt of the long form disclosures; and

(3) Permits the customer to cancel the purchase of the contract without penalty within 30 days after the bank has mailed the long form disclosures to the customer.

(d) *Special rule for electronic election.* The affirmative election and acknowledgment may be made electronically in a manner consistent with the requirements of the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. 7001 *et seq.*

§ 37.8 Safety and soundness requirements.

A national bank must manage the risks associated with debt cancellation contracts and debt suspension agreements in accordance with safe and sound banking principles. Accordingly, a national bank must establish and maintain effective risk management and control processes over its debt cancellation contracts and debt suspension agreements. Such processes include appropriate recognition and financial reporting of income, expenses, assets and liabilities, and appropriate treatment of all expected and unexpected losses associated with the products. A bank also should assess the adequacy of its internal control and risk mitigation activities in view of the nature and scope of its debt cancellation contract and debt suspension agreement programs.

Appendix A to Part 37--Short Form Disclosures

This product is optional

Your purchase of [PRODUCT NAME] is optional. Whether or not you purchase [PRODUCT NAME] will not affect your application for credit or the terms of any existing credit agreement you have with the bank.

Lump sum payment of fee

[Applicable if a bank offers the option to pay the fee in a single payment]

[Prohibited where the debt subject to the contract is a residential mortgage loan]

You may choose to pay the fee in a single lump sum or in [monthly/quarterly] payments. Adding the lump sum of the fee to the amount you borrow will increase the cost of [PRODUCT NAME].

Lump sum payment of fee with no refund

[Applicable if a bank offers the option to pay the fee in a single payment for a no-refund DCC]

[Prohibited where the debt subject to the contract is a residential mortgage loan]

You may choose [PRODUCT NAME] with a refund provision or without a refund provision. Prices of refund and no-refund products are likely to differ.

Refund of fee paid in lump sum

[Applicable where the customer pays the fee in a single payment and the fee is added to the amount borrowed]

[Prohibited where the debt subject to the contract is a residential mortgage loan]

[Either:] (1) You may cancel [PRODUCT NAME] at any time and receive a refund; or (2) You may cancel [PRODUCT NAME] within **___** days and receive a full refund; or (3) If you cancel [PRODUCT NAME] you will not receive a refund.

Additional disclosures

We will give you additional information before you are required to pay for [PRODUCT NAME]. [If applicable]: This information will include a copy of the contract containing the terms of [PRODUCT NAME].

Eligibility requirements, conditions, and exclusions

There are eligibility requirements, conditions, and exclusions that could prevent you from receiving benefits under [PRODUCT NAME].

[Either:] You should carefully read our additional information for a full explanation of the terms of [PRODUCT NAME] *or* You should carefully read the contract for a full explanation of the terms of [PRODUCT NAME].

Appendix B to Part 37--Long Form Disclosures

This product is optional

Your purchase of [PRODUCT NAME] is optional. Whether or not you purchase [PRODUCT NAME] will not affect your application for credit or the terms of any existing credit agreement you have with the bank.

Explanation of debt suspension agreement [Applicable if the contract has a debt suspension feature]

If [PRODUCT NAME] is activated, your duty to pay the loan principal and interest to the bank is only suspended. You must fully repay the loan after the period of suspension has expired. [If applicable]: This includes interest accumulated during the period of suspension.

Amount of fee

[For closed-end credit]: The total fee for [PRODUCT NAME] is _____.

[For open-end credit, either:] (1) The monthly fee for [PRODUCT NAME] is based on your account balance each month multiplied by the unit-cost, which is _____; *or* (2) The formula used to compute the fee is ______].

Lump sum payment of fee

[Applicable if a bank offers the option to pay the fee in a single payment]

[Prohibited where the debt subject to the contract is a residential mortgage loan]

You may choose to pay the fee in a single lump sum or in [monthly/quarterly] payments. Adding the lump sum of the fee to the amount you borrow will increase the cost of [PRODUCT NAME].

Lump sum payment of fee with no refund

[Applicable if a bank offers the option to pay the fee in a single payment for a no-refund DCC]

[Prohibited where the debt subject to the contract is a residential mortgage loan]

You have the option to purchase [PRODUCT NAME] that includes a refund of the unearned portion of the fee if you terminate the contract or prepay the loan in full prior to the scheduled termination date. Prices of refund and no-refund products may differ.

Refund of fee paid in lump sum

[Applicable where the customer pays the fee in a single payment and the fee is added to the amount borrowed]

[Prohibited where the debt subject to the contract is a residential mortgage loan]

[Either:] (1) You may cancel [PRODUCT NAME] at any time and receive a refund; or (2) You may cancel [PRODUCT NAME] within ______ days and receive a full refund; or (3) If you cancel [PRODUCT NAME] you will not receive a refund.

Use of card or credit line restricted

[Applicable if the contract restricts use of card or credit line when customer activates protection]

If [PRODUCT NAME] is activated, you will be unable to incur additional charges on the credit card or use the credit line.

Termination of [PRODUCT NAME]

[Either]: (1) You have no right to cancel [PRODUCT NAME]; *or* (2) You have the right to cancel [PRODUCT NAME] in the following circumstances: _______.

[And either]: (1) The bank has no right to cancel [PRODUCT NAME]; *or* (2)The bank has the right to cancel [PRODUCT NAME] in the following circumstances: ________.

Eligibility requirements, conditions, and exclusions

There are eligibility requirements, conditions, and exclusions that could prevent you from receiving benefits under [PRODUCT NAME].

[Either]: (1) The following is a summary of the eligibility requirements, conditions, and exclusions. [The bank provides a summary of any eligibility requirements, conditions, and exclusions]; *or* (2) You may find a complete explanation of the eligibility requirements, conditions, and exclusions in paragraphs _______ of the [PRODUCT NAME] agreement.

Last Revised: Tuesday, December 10, 2002 20:19:06

Agency # 210.00

POLICY STATEMENT **DECEMBER 12, 2006**

ORDER OF THE STATE BANK COMMISSIONER

ACTIVITIES FOR STATE-CHARTERED BANK AUTHORIZED BY THE BANK COMMISSIONER PURSUANT TO A.C.A. § 23-47-102(C)

SUBJECT: MERGER OR CONSOLIDATION

The Arkansas Bank Commissioner, acting pursuant to the authority granted under A.C.A. § 23-47-101(c), hereby adopts the following Resolution:

Arkansas state chartered banks, by the approving vote of the holders of their capital stock as required by their Articles of Incorporation or other organizational documents, may merge or consolidate with a stock federal or state savings association, in the same manner in which a national bank is authorized, pursuant to Title V of the Federal Deposit Insurance Corporation Improvement Act of 1991 (12 U.S.C. 215c(a)). Merger and/or consolidation provisions of state and federal law and regulations will be applied in consideration of such transactions.

Signed this 12th day of December 2006.

SIGNED: ROBERT H. ADCOCK, JR.
BANK COMMISSIONER

Agency # 210.00

POLICY STATEMENT **JULY 20, 2007**

ORDER OF THE STATE BANK COMMISSIONER

SUBJECT: BANK INVESTMENT IN LIMITED LIABILITY COMPANIES OR LIMITED LIABILITY PARTNERSHIPS

The Arkansas Bank Commissioner in accordance with his/her authority pursuant to A.C.A. § 23-47-101(c), hereby authorizes Arkansas state banks to engage in the activity to invest in a limited liability company, or limited liability partnership, in the same manner in which national banks are authorized to do so.

The Comptroller of the Currency generally authorizes national banks to make such investment so long as four standards are met. These are as follows:

1. The activities of the enterprise in which the investment is made must be limited to activities that are part of, or incidental to, the business of banking.

2. The bank must be able to prevent the enterprise from engaging in activities that do not meet the foregoing standard.

3. The bank's loss exposure must be limited, as a legal and accounting matter, and the bank must not have open-ended liability for the obligation of the enterprise.

4. The investment must be convenient or useful to the bank in carrying out its business and not a mere passive investment unrelated to that bank's banking business.

(See Office of the Comptroller of the Currency re: Investment in Limited Liability Companies or Limited Liability Partnerships)

Signed this 20th day of July 2007.

SIGNED: CANDACE A. FRANKS
BANK COMMISSIONER

Agency # 210.00

POLICY STATEMENT **JULY 20, 2007**

ORDER OF THE STATE BANK COMMISSIONER

SUBJECT: LOAN PRODUCTION OFFICE – ACTIVITIES PERMITTED

Act 42 of 2007 authorizes Arkansas state banks to establish limited purpose offices. A limited purpose office may function as a loan production office.

Pursuant to the authority provided by A.C.A. § 23-48-702, Arkansas state banks may perform the same authorized activities at a loan production office as national banks are authorized to do so. These activities are:

Title 12: Banks and Banking
Part 7 – Bank Activities and Operations
Subpart A – Bank Powers

§ 7.1003 Money lent at banking offices or at other than banking offices.

(a) *General*. For purposes of what constitutes a branch within the meaning of 12 U.S.C. 36(j) and 12 CFR 5.30, "money" is deemed to be "lent" only at the place, if any, where the borrower in-person receives loan proceeds directly from bank funds:

(1) From the lending bank or its operating subsidiary; or

(2) At a facility that is established by the lending bank or its operating subsidiary.

(b) *Receipt of bank funds representing loan proceeds*. Loan proceeds directly from bank funds may be received by a borrower in person at a place that is not the bank's main office and is not licensed as a branch without violating 12 U.S.C. 36, 12 U.S.C. 81 and 12 CFR 5.30, provided that a third party is used to deliver the funds and the place is not established by the lending bank or its operating subsidiary. A third party includes a person who satisfies the requirements of §7.1012(c)(2), or one who customarily delivers loan proceeds directly from bank funds under accepted industry practice, such as an attorney or escrow agent at a real estate closing.

§ 7.1004 Loans originating at other than banking offices.

(a) *General*. A national bank may use the services of, and compensate persons not employed by, the bank for originating loans.

(b) *Approval*. An employee or agent of a national bank or of its operating subsidiary may originate a loan at a site other than the main office or a branch office of the bank. This action does not violate 12 U.S.C. 36 and 12 U.S.C. 81 if the loan is approved and made at the main office or a branch office of the bank or at an office of the operating subsidiary located on the premises of, or contiguous to, the main office or branch office of the bank.

§ 7.1005 Credit decisions at other than banking offices.

A national bank and its operating subsidiary may make a credit decision regarding a loan application at a site other than the main office or a branch office of the bank without violating 12 U.S.C. 36 and 12 U.S.C. 81, provided that " money" is not deemed to be "lent" at those other sites within the meaning of §7.1003.

Signed this 20th day of July 2007.

SIGNED: CANDACE A. FRANKS
BANK COMMISSIONER

Agency # 210.00

POLICY STATEMENT **JULY 20, 2007**

ORDER OF THE STATE BANK COMMISSIONER

SUBJECT: INDEMNIFICATION TO OFFICERS, DIRECTORS

WHEREAS, pursuant to Arkansas Statute Annotated Section 64-309 (Repl. 1980) (the "State Statute"), (A.C.A. § 4-26-814) all business corporations incorporated pursuant to the laws of the State of Arkansas have the power to indemnify officers, directors and other persons for: (i) all expenses of litigation and other legal proceedings when such persons are successful on the merits, as specified in said State Statute; (ii) expenses, judgments, fines, and amounts paid in settlement of such litigation and other legal proceedings (other than derivative actions) even if such persons are not successful on the merits if they acted in good faith and in a manner reasonably believed to be in or not opposed to the best interests of the corporation; and (iii) expenses incurred in a derivative action, if such persons acted in good faith and in a manner reasonably believed in or not opposed to the best interests of the corporation, provided that the court in which such action or suit is brought shall determine, upon application, that despite such adjudication of liability, such persons are fairly and reasonably entitled to indemnity for such expenses; and

WHEREAS, the General Assembly of the State of Arkansas in the 1987 regular legislative session adopted and enacted a new Arkansas Corporate Code, the same being Arkansas Statute Annotated Sections 64-101 through 64-1706, (A.C.A. § 4-26-101 through A.C.A § 4-26-308) inclusive (the "New Code") which is to become effective for all Arkansas business corporations established on or after January 1, 1988 and for existing Arkansas business corporations whose stockholders elect to be governed by the New Code on or after January 1, 1988, and the New Code contains similar provisions of indemnification as the code which it replaces; and

WHEREAS, pursuant to such actions of the General Assembly, it is the public policy of the State of Arkansas to allow Arkansas business corporations to indemnify officers, directors and such other persons as set forth hereinabove and as more particularly specified in the State Statute and the New Code; and

WHEREAS, national banking associations organized pursuant to the laws of the United States of America are granted the power to indemnify officers, directors and other persons pursuant to an Office of the Comptroller of the Currency Interpretive Ruling promulgated at 12 C.F.R. 7.5217 and, under such Interpretive Ruling, the Office of the Comptroller of the Currency will recognize a national banking association's indemnification provisions in its Articles of Association if such substantially reflect general standards of law as evidenced by the law of the state in which a national banking association is headquartered, the law of the state in which the national banking association's holding company is incorporated, or the relevant provisions of the Model Business Corporation Act; and

WHEREAS, liability insurance for officers, directors and other persons has become increasingly cost prohibitive, uneconomical and extremely difficult to obtain for corporations in general including state and nationally chartered banking associations, and even if obtained, such insurance typically contains broad exclusions from its coverage thereby severely reducing the transfer of risk to the insurance carrier; and

WHEREAS, the Arkansas Banking Act, Arkansas Statute Annotated Section 67-101 et seq., (A.C.A. § 23-31-201), does not specifically grant the power to indemnify officers, directors and other persons of an Arkansas state chartered banking institution; and

WHEREAS, it is necessary for Arkansas state chartered banking institutions to be able to offer officers, directors and other persons protection against liability for actions taken by them on behalf of such institutions and in order for such institutions to be able to attract capable and talented individuals to serve as officers, directors and employees thereof; and

WHEREAS, pursuant to Arkansas Statute Annotated Section 67- 501.1(o), [A.C.A. § 23-32-701(16)], the State Bank Commissioner, with the approval of the State Bank Department Board, is empowered to grant Arkansas state chartered banking institutions the power to engage in any activities in which said institutions could engage were they acting as national banking associations at the time such authority is granted, including, but not limited to, the power to indemnify officers, directors and other persons in the same manner and to the same extent officers, directors and other persons of a national banking association are indemnified pursuant to said Interpretive Ruling of the Office of the Comptroller of the Currency, promulgated at 12 C.F.R. 7.5217;

NOW, THEREFORE, BE IT RESOLVED, that the Arkansas State Banking Board, under the authority granted to it pursuant to said Arkansas Statute Annotated Section 67-501.1(o), [A.C.A. § 23-32-701(16)], hereby approves and empowers the State Bank Commissioner the right to grant Arkansas state chartered banking institutions the power to indemnify officers, directors and other persons to the maximum extent as such is permitted by the Arkansas Business Corporation Act, including but not limited to the State Statute and the New Code, as the same now exists or may hereafter be amended; provided, however, that such power shall not be construed to allow the indemnification of officers, directors and other persons of an Arkansas state chartered banking institution against expenses, penalties or other payments incurred in an administrative proceeding or action instituted by an appropriate bank regulatory agency which proceeding or action results in a final order assessing civil money penalties or requiring affirmative action by an individual or individuals in the form of payments to an Arkansas state chartered banking institution; and

BE IT FURTHER RESOLVED, that the power of an Arkansas state chartered banking institution to provide indemnification to officers, directors and other persons may be specified, in accordance with the terms hereof, under any article of incorporation or bylaw provision, legal agreement or contract, vote of shareholders or disinterested directors, or other lawful means including the right of Arkansas state chartered banking institutions the power to purchase and maintain insurance on behalf of officers, directors and other persons; provided, however, that such insurance shall explicitly exclude coverage for a formal order assessing civil money penalties against a bank officer, director or employee; and

BE IT FURTHER RESOLVED, that the State Bank Commissioner shall have the power to do all things necessary to implement the intents and purposes of the above resolution and to allow Arkansas state chartered banking institutions the power to indemnify, through insurance or otherwise, officers, directors and other persons to the maximum extent as is authorized or permitted by the Arkansas Business Corporation Act, including but not limited to the State Statute and the New Code, as the same now exists or may hereafter be amended.

Signed this 20th day of July 2007.

SIGNED: CANDACE A. FRANKS
BANK COMMISSIONER

Agency # 210.00

POLICY STATEMENT **JULY 20, 2007**

ORDER OF THE STATE BANK COMMISSIONER

SUBJECT: DEFINITION OF CAPITAL, SURPLUS, AND UNDIVIDED PROFITS (LEGAL LENDING LIMIT)

The Arkansas State Bank Commissioner, in accordance with her authority under Arkansas Code Annotated (A.C.A.) § 23-47-101(c), hereby adopts the following policy:

A.C.A. § 23-47-501(a) limits the total indebtedness to any state bank of any person to twenty percent (20%) of the capital base of the bank. Capital base means "the sum of capital, surplus, and undivided profits, plus any additions and less any subtractions which the Bank Commissioner may by regulation prescribe", as provided by A.C.A. § 23-45-102(a)(10).

For the purpose of lending limits, capital and surplus is defined under 12 CFR 32.2(b) as meaning:

(1) The sum of a bank's Tier 1 and Tier 2 capital, per the state bank's most recent call report; plus

(2) Any remaining amount of the allowance for loan and lease losses, per the state bank's most recent call report, not included in the calculation of Tier 2 capital.

The above is the method state banks shall use in determining capital, surplus, and undivided profits for the purpose of determining their legal lending limit. Further, the legal lending limit is calculated as of the most recent call date.

Signed this 20th day of July 2007.

SIGNED: CANDACE A. FRANKS
BANK COMMISSIONER

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ADMINISTRATIVE POLICY #001

BILL J. FORD, BANK COMMISSIONER	**RETAIN FOR**
NOVEMBER 16, 1987	**FUTURE**
SUBJECT: ELIGIBLE BANK INVESTMENTS	**REFERENCE**

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Administrative Policy #001 is being issued to all State chartered banks in regard to the legality of investing in certain instruments such as CMO's (Collateralized Mortgage Obligations), CMO residuals, REMICs and SMBS's (Stripped Mortgage-Backed Securities). The purpose of the directive is to state the position and requirements of the Bank Department with respect to these investment vehicles.

Before consideration can be given to investment into any of these non-traditional instruments it will be necessary for the Board of Directors to approve amendments to the bank's investment policy.

COLLATERALIZED MORTGAGE OBLIGATIONS (CMO'S)

A state chartered bank may only invest in CMO's in which the collateral consists of securities in which repayment of both principal and interest is 100% guaranteed by an agency of the United States government. CMO's which meet this criteria may be purchased without legal lending limitations so long as the CMO meets the definition of "Mortgage related securities" as defined in section 101 of the Secondary Mortgage Market Enhancement Act of 1984 which has been codified at 15 U.S.C. S 78 c(a) (41). The definition includes any security which satisfied all of the following requirements:

- The security must be rated in one of the two highest rating categories by at least one nationally recognized statistical rating organization.

- The security must be secured by one or more promissory notes or certificates of interest or participations in such notes.

- The security must provide for payments of principal in relation to payments or reasonable projections of payments on the underlying notes or certificates.

- The notes or certificates underlying the CMO's must be directly secured by a first lien on a single parcel of real estate, stock allocated to a dwelling unit in a residential cooperative housing corporation, upon which is located a dwelling or mixed residential and commercial structure, or on a residential manufactured home.

- The underlying notes or certificates must have been originated by a savings and loan association, savings bank, commercial bank, credit union, insurance company, or similar institution which is supervised and examined by a Federal or State authority or by a mortgagee approved by the Secretary of Housing and Urban Development.

Banks making such investments are required to maintain the following information in the files of the bank:

(1) The CMO bond instrument or a descriptive safekeeping receipt identifying the specific instrument certifying that the described instrument is being held for subject bank;

(2) A prospectus describing the trust indenture. A bank may wish to obtain monthly documentation reflecting the unpaid balances and performance of the collateral held by the trust.

Although the CMO's described may be obtained without limitation, management and the board of directors are reminded of the sound tenet of banking of diversification of risk. Consideration should also be given to the liquidity needs of the bank prior to making such investment.

Investments in CMO's which are backed by any other collateral <u>are subject to</u> legal lending limitations.

<u>CMO AND REMIC RESIDUALS</u>

Residual and stripped coupon securities represent packages of various combinations of selected cash flows from a pool of mortgage receivables (either mortgage loans or mortgage-backed securities) and are typically issued under a Real Estate Mortgage Investment Conduit (REMIC) or collateralized mortgage obligation (CMO) structure.

CMO and REMIC Residual instruments reflect an ownership interest in the trust and do not indicate an investment in principal or a stated interest rate. The investor is purchasing an interest in the trustee's ability to earn money sometime in the future. It is the opinion of the State Bank Department that such investments represent an equity interest in the trust, are speculative in nature, and, as such, **<u>are not considered eligible</u>** investments for state chartered banks.

STRIPPED MORTGAGE-BACKED SECURITIES (SMBS)

Principal-only strips (P/O) represents an undivided percentage ownership interest in the principal portion of the pass through certificate. Banks may invest in principal-only strips provided that payment of the principal portion of the underlying security is 100% guaranteed by an agency of the U. S. Government. Banks that invest in these investments must maintain the same documentation as required for CMO's.

Since a P/0 is essentially a "zero coupon" security, its market value may be extremely volatile in a changing interest rate environment. A bank must have sufficient liquidity to be able to hold the instrument to term despite wide swings in its market value or must have the expertise to react quickly to interest rate changes.

Interest-only strips (I/O) have many of the same characteristics as CMO Residuals. Such investment in future interest, which may or may not be realized, is considered speculative. These instruments **are not considered eligible** investments for state chartered banks, **unless** utilized for interest rate hedging purposes.

Any hedging activity must be supported by a board approved hedging policy that sets forth parameters under which the activity will take place. The board of directors must establish limitations applicable to the hedging activity and the board of directors, a duly authorized committee of the board, or the bank internal auditors must review periodically (at least monthly) the hedging position to ascertain performance with the limitations set forth in the policy.

If a bank holds these securities as a hedge, the current accounting guidance on hedging is primarily contained in FASB Statement No. 80, Accounting for Futures Contracts, which includes two criteria that must be met for a futures contract to qualify as a hedge:

(1) The item to be hedged exposes the bank to interest rate risk.

(2) The futures contract reduces that exposure and is designated as a hedge.

Investment in Interest-only strips in any manner other than provided above will be considered an unsafe and unsound banking practice.

Interest-only strips (I/0) investments **are subject to the bank's legal lending limit**.

ACCOUNTING

Information will be forthcoming from the appropriate federal supervisory agency regarding the recommended accounting for Call Report purposes of the various instruments discussed.

Agency # 210.00

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ADMINISTRATIVE POLICY #002 ***REVISED – 06/30/04***
Robert H. Adcock, Jr., Bank Commissioner
BILL J. FORD, BANK COMMISSIONER **RETAIN FOR**
MAY 31, 1997 **FUTURE**
SUBJECT: BANK HOLDING COMPANY SUPERVISION **REFERENCE**

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The Bank Commissioner requires that all bank holding companies owning Arkansas state-chartered banks to submit certain Federal Reserve System reports. Copies of reports submitted to the Federal Reserve Bank, which are executed according to individual report instructions, will comply with this Order. These forms and their instructions may be obtained via Internet at the following address:
http://www.federalreserve.gov/boarddocs/reportforms/CategoryIndex.cfm?WhichCategory=1

The following is a list of the bank holding company reports that your institution may be required to file. Retain the list for periodic review as the status of your institution may change.

Note: All **FR Y-9 and FR Y-11** reports are now submitted to the Federal Reserve through Internet Electronic Submission (IESUB); therefore, paper copies of these reporting forms are no longer required for submission to Arkansas State Bank Department. In the course of examining holding companies, Arkansas State Bank Department reserves the right to request paper copies of these forms as needed to effectively analyze and complete the examination process.

Paper copies of the following reports are required to be submitted to the Arkansas State Bank Department as follows:

Report: **FR Y-6 –** Annual Report of Bank Holding Companies.

Frequency: Annually, within 90 days following calendar year end.

Reporting Criteria: All top-tier bank holding companies.

Report:	**FR Y-8 --** Report of Bank Holding Company Report of Insured Depository Institutions' Section 23A Transactions with Affiliates.
Frequency:	Quarterly, submitted to the Arkansas State Bank Department if reportable activity has occurred.
Reporting Criteria:	All top-tier bank holding companies, including financial holding companies. A separate **FR Y-8** report form should be filed for each depository institution.

Report:	**FR Y-10 –** Report of Changes in Organizational Structure.
Frequency:	As needed, submitted within thirty calendar days of a reportable transaction or event.
Reporting Criteria:	All top-tier bank holding companies and state member banks that are not controlled by a bank holding company.

Agency # 210.00

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ADMINISTRATIVE POLICY #003 ***Revised – 09/30/01***
Frank White, Bank Commissioner
Revised – 01/31/06
Robert H. Adcock, Jr., Bank Commissioner

BILL J. FORD, BANK COMMISSIONER **RETAIN FOR**
ISSUED: MARCH 30, 1988 **FUTURE**
SUBJECT: RISK RATING/RESERVE ALLOCATION **REFERENCE**

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OVERVIEW

This guidance is intended to update Administrative Policy #003, originally issued on March 30, 1988 and most recently revised on September 30, 2001.

The Federal Financial Institutions Examination Council (FFIEC) issued a Joint Interagency Policy Statement on July 6, 2001 on the Allowance for Loan and Lease Losses Methodologies and Documentation for Banks and Savings Institutions (FIL-63-2001). Since that time, the Securities and Exchange Commission (SEC) has raised the issue of the allowance for loan and lease losses (ALLL) in publicly traded institutions and whether the support provided within reserve methodologies complies with existing generally accepted accounting principals.

The Policy Statement clarified the expectations regarding methodologies and documentation support for the ALLL. It further states that the ALLL should be determined in accordance with generally accepted accounting principles (GAAP). GAAP requires that an institution maintain written documentation to support the ALLL reported in financial statements and the call report.

Two accounting statements issued through the Financial Accounting Standards Board address the ALLL. Statement No. 5, *Accounting for Contingencies*, issued in 1975 and Statement No. 114, *Accounting by Creditors for Impairment of a Loan*, issued in 1993 both provide general principles an institution should consider when determining the appropriate level for the ALLL. FASB #114 addresses impairment of individually impaired credits while FASB #5 addresses the allowance for all other loan types based on many different risk characteristics which will be addressed below. Financial institutions should also consult their respective accountant to assist them in meeting documentation requirements of these and other supporting accounting statements.

Based on the Policy Statement, it is clear that institutions should no longer **only** use the traditional formula method of 15% for Substandard, 50% for Doubtful, 100% for Loss and 1% for all other loans as the only basis to establish the ALLL without further documented support. **The lack of documentation to support risk weighting percentages and qualitative adjustments is often where banks fall short and can lead to regulatory criticism.**

Institutions should address the reserve methodology in their loan or related policies. The policies should describe the procedures and primary elements of the ALLL methodology including portfolio segmentation and impairment measurement.

The Arkansas State Bank Department recognizes the need for all Arkansas institutions to comply with GAAP but also recognizes the potential burden these guidelines could place on smaller institutions with non complex lending practices or portfolios. **Larger and more complex institutions would be expected to have more sophisticated methodologies than smaller institutions that are involved in less complex activities.** An institution's loan loss allowance methodology is influenced by entity specific factors such as size, organizational structure, business environment and strategy, management style, loan portfolio characteristics, loan administration procedures, and management information systems. While different institutions may use different methods, there are certain common elements that should be included in any ALLL methodology. These include:

- A detailed analysis of the loan portfolio, performed on a regular basis;
- Consider all loans (whether on an individual or group basis);
- A method to identify loans to evaluate for impairment on an individual basis under FASB No. 114 and to segment the remainder of the portfolio into groups of loans with similar risk characteristics for evaluation and analysis under FASB No. 5;
- Include all known relevant internal and external factors that may affect loan collectibility;
- Be applied consistently but, when appropriate, should be modified for new factors affecting collectibility;
- Consideration of the particular risks inherent in different kinds of lending;
- Consideration of current collateral values (less costs to sell), where applicable;
- Analyses, estimates, reviews and other loan loss allowance methodology functions be performed by competent and well-trained personnel;
- Be based on current and reliable data;
- Be well documented, in writing, with clear explanations of the supporting analyses and rationale;
- Include a systematic and logical method to consolidate the loss estimates and ensure the loan loss allowance balance is recorded in accordance with GAAP.

COMPONENTS OF AN EFFECTIVE ALLL METHODOLOGY

An appropriate methodology to establish the allowance for loan and lease losses will generally consist of two components. This includes an analysis of individual loans that are impaired and some form of risk rating for all other types of loans. In addition, an evaluation of other qualitative factors (both internally and externally) that may affect the level of the ALLL should be performed. Each of the two components is addressed below:

FASB #114

A loan is considered impaired when, based on current information and events, it is probable that a creditor will be unable to collect all contractual interest and/or principal according to the terms of the loan agreement. If a loan is considered to be impaired, then management must evaluate the impairment using one of three methods:

- Discounted Present Value of Cash Flows
- Quoted Market Value
- Fair Value of the Collateral

In most cases, particularly less sophisticated credits and in smaller financial institutions, fair value of the collateral would most likely be the method used to determine impairment.

The following criteria are examples of considerations that should be considered when determining the fair value of collateral:

1) The holding period before collateral will be sold.
2) The costs of maintaining the collateral during the holding period.
3) The probable discount of value because the bank is the seller.
4) The costs of selling the collateral.
5) Any other economic/financial factors impacting the realizable value of the collateral.

FASB guidelines do not address at what exact point a bank should record a charge-off; however, call report instructions state that if the fair value of collateral test for impairment is used, then the loan is most likely collateral dependent. Call report instructions further state in general, any portion of book value in a collateral dependent loan, that exceeds the fair value of collateral and can be identified as uncollectible, should be promptly charged off against the ALLL. If this threshold has not been reached, then potential exposure should be allocated specific to that loan within the ALLL. Specific allocations would most likely be appropriate when other possible means of repayment exist on impaired loans.

NOTE: When reviewing a loan individually under FASB No. 114, it would not be appropriate to measure loan impairment by applying a loss rate to each loan based on the average historical loss percentage of all of its commercial loans.

FASB Statement #5

Financial institutions should make attempts to determine the reserve needed against the remainder of the portfolio. Banks should segment their loan portfolio by groups that have similar risks.

Historical losses for different types of credits should be considered and often would be the minimum basis considered under FASB No. 5 to support risk allocations. Banks should maintain supporting documentation for the technique used to develop loss rates, including the period of time over which the losses where incurred. If a range of loss is determined, banks should maintain documentation to support the identified range and rationale used for determining which estimate is the best estimate within the range of loan losses. Factors that should be considered in developing loss measurements include:

- Levels of and trends in delinquencies;
- Levels of and trends in charge-offs and recoveries;
- Trends in volume and terms of loans;
- Effects of any change in risk selection and underwriting standards, and other changes in lending policies, procedures, and practices;
- Experience, ability, and depth of lending management and other relevant staff;
- National and local economic trends and conditions;
- Industry conditions; and
- Effects of changes in credit concentrations.

For any adjustment of loss measurements for environmental factors, whether external or internal, an institution should maintain sufficient, objective evidence to support the amount of the adjustment and explain why the adjustment is necessary to reflect current information, events, circumstances, and conditions in the loss measurement. Policies addressing the ALLL should also cover acceptable limits concerning these adjustments.

If a bank does not have a loss history of its own, it may be appropriate to reference the loss experience of other banks, provided the bank can demonstrate that its portfolio is similar in nature to the comparable institution.

BANK POLICIES

In order for an institution's ALLL methodology to be effective, written policies and procedures should address the primary elements of its loan loss methodology, including portfolio segmentation and impairment measurement. Written policies should describe the methodology in the following way:

For segmenting the portfolio

- o How the segmentation process is performed (i.e. loan type, risk ratings, industry, etc.)
- o When a loan grading system is used to segment the portfolio:
  - ▪ The definitions of each loan grade;
  - ▪ A reconciliation of the internal grades to supervisory loan grades;
  - ▪ The delineation of responsibilities for the loan grading system;

(2) For determining and measuring impairment under FASB No. 114:

- o The methods used to identify loans to be analyzed individually;
- o For individually reviewed loans that are impaired, how the amount of any impairment is determined and measured, including:
  - ▪ Procedures describing the impairment measurement techniques available, and
  - ▪ Steps performed to determine which technique is most appropriate in a given situation

(3) For determining and measuring impairment under FASB No.5, institutions should consider:

- o How loans with similar characteristics are grouped to be evaluated for loan collectibility (such as loan type, past-due status, and risk);
- o How loss rates are determined (i.e. historical loss rates adjusted for environmental factors or migration analysis) and what factors are considered when establishing appropriate time frames over which to evaluate loss experience; and
- o Descriptions of qualitative factors (i.e. industry, geographical, economic, and political factors) that may affect loss rates or other measurements.

UNFUNDED COMMITMENTS

Call report instructions state that institutions should maintain, as a separate liability account, an allowance sufficient to absorb estimated credit losses associated with off-balance sheet credit instruments such as loan commitments, standby letters of credit and guarantees. The amount of risk of loss associated with these types of instruments should be evaluated the same as loans on the balance sheet as the majority of these commitments may be funded, especially in significant agricultural production or construction lending areas. Any off-balance sheet reserve level should be reported in the call report as “Other Liabilities.” Neither the allowance for loan and lease losses or any allowance for credit losses on off-balance sheet credit exposures are considered part of Tier 1 Capital but both would be considered part of Tier 2 Capital, subject to the 1.25 percent of gross risk-weighted asset limit.

COMMONLY NOTED DEFICIENCIES & POINTS TO CONSIDER:

(1) Lack of documentation to support qualitative adjustments is often where banks will fall short.
(2) Each adjustment must be supported.
(3) Estimate conservatively so the overall ALLL reflects a margin for the imprecision inherent in most estimates of expected/incurred losses.
(4) The ALLL methodology should be reviewed by the board at least annually.
(5) The ALLL methodology should be validated at least annually.
(6) Values should not be assigned based on a formula method, but a formula method can be used as a benchmark to judge ALLL adequacy.
(7) The ALLL balance should not have a constant relationship to the dollar volume of loans in the loan portfolio.
(8) Changes in the ALLL should be in the same direction as the changes in risks. As risks change, the amount of the ALLL should change.

CONCLUSION & REGULATORY GUIDANCE

The above guidelines are intended to assist Arkansas financial institutions to better document ALLL methodologies and comply with GAAP guidelines associated with this important item on a bank's balance sheet. The majority of Arkansas financial institutions, especially smaller non complex institutions, have historically used elements of the previous Arkansas State Bank Department's Administrative Order #003 as a basis for the ALLL methodology. This further guidance is not intended to imply that guidance previously issued is no longer acceptable; however, documented support for each part of the ALLL is required. Also remember, policies must be updated to address the methodology employed by the bank.

Examinations by the ASBD and our federal counterparts will continue to review methodologies employed by state chartered financial institutions to ensure documented support is adequate to comply with generally accepted accounting principals.

Agency # 210.00

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ADMINISTRATIVE POLICY #004

BILL J. FORD, BANK COMMISSIONER	**RETAIN FOR**
AUGUST 22, 1988	**FUTURE**
SUBJECT: NONACCRUAL OF INTEREST	**REFERENCE**

* *

NONACCRUAL OF INTEREST

Banks shall not accrue interest or discount on:

1) any asset which is maintained on a cash basis because of deterioration in the financial position of the borrower;

2) any asset for which payment in full of principal and interest is not expected; or

3) any asset upon which principal or interest has been in default for a period of 90 days or more unless it is **both** well secured **and** in the process of collection. A nonaccrual asset may be restored to an accrual status when none of its principal and interest is past due.

If the principal or interest on an asset becomes due and unpaid for 90 days or more, the asset should be placed in nonaccrual status as of the date it becomes 90 days past due. Interest accrued to date on a loan placed in nonaccrual status must be reversed from current year earnings. The loan must remain in nonaccrual status until it meets the criteria for restoration to accrual status described above.

DEFINITIONS

1. A debt is **well secured** if it is secured:

a) by collateral in the form of liens on or pledges of real or personal property, including securities, that have a realizable value sufficient to discharge the debt (including accrued interest) in full; or

b) by the guaranty of a financially responsible party.

2. A debt is **<u>in the process of collection</u>** if collection of the debt is proceeding in due course either through legal action, including judgement enforcement procedures; or, **<u>in appropriate circumstances</u>**, through collection efforts not involving legal action which are reasonably expected to result in repayment of the debt or in its restoration to a current status within 105 calendar days of its due date.

<u>No loan</u> past due 105 days or more will be considered in process of collection.

Agency # 210.00

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ADMINISTRATIVE POLICY #005

BILL J. FORD, BANK COMMISSIONER	**RETAIN FOR**
DATE: FEBRUARY 15, 1989	**FUTURE**
SUBJECT: STRATEGIC PLANNING	**REFERENCE**

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Recent legislative action which provides for the expansion of banking through expanded branching powers and regional acquisitions and efforts to repeal antiquated bank laws and thus expand powers for banks make it even more apparent that bankers must address the issues that effect the future of their institution. In this era of deregulation and change, the successful community bank will be the one that is prepared for and able to effectively adjust to change.

An effective means of coping with "change" is the development of a **"strategic plan"**. Though it may seem difficult to realize where the time will be found to organize and formalize a "plan", it should be noted that a properly utilized and well thought out plan will improve decision making and make time commitments more easily prioritized and allocated. The banker who doesn't have time for planning is the banker who will seldom have time to act rather than react.

<u>**THE STRATEGIC PLAN**</u>: A strategic plan sets forth the bank's goals and addresses how to achieve them. To be effective, the plan must project beyond the current fiscal year. Given the rapidly changing banking environment, a one year and three year time frame are considered reasonable. The plan must use the best available data to evaluate economic and market conditions and then determine a realistic set of goals.

Profitability is important. However, it may be counterproductive to maximize short-term profits at the expense of achieving long-term goals. A balance must be found between a comfortable profit margin and the resources needed to meet strategic objectives.

Before writing a strategic plan, the following points must be acknowledged and accepted: you and your staff are qualified to write your plan; a strategic plan is basically defining your goals and objectives into written form; and the first attempt will not be perfect, but will be the basis for building an improved plan.

THE PLANNING PROCESS: A plan should address two distinct criteria: one that identifies **what** the organization is and **what** it desires to be, often referred to as the **"mission statement"**, and one that defines **how** to achieve the mission of the organization, i.e., goals and objectives.

MISSION STATEMENT: The **mission statement** identifies the organization and should include an identification of products offered and markets served, as well as a description of the primary factor for determining why you do what you do.

The mission statement can be reduced to a few concise statements addressing basic issues such as: What business are we in? What business should we be in? Who are our customers? Who should our customers be? and, How do we want our customers to know us or view us?

OBJECTIVES: After having determined what the mission is, strategy must be developed giving guidances as to **how** the mission will be achieved. The objectives defined in the "how to achieve" strategy should never conflict with the bank's stated mission, but should be in harmony with the mission statement. When necessary, an outline of programs needed to accomplish the objectives should be included. Objectives reflect what it is that is to be accomplished and should be measurable; realistic; understandable; and they must have a defined time frame.

If nothing more is accomplished than defining the **"mission statement"** and outlining the highest priority objectives for the upcoming year, including the financial expectations, the probability of accomplishing those objectives will be dramatically increased. While such an exercise is not the ultimate goal, it should suffice as a temporary plan.

COMMUNICATION AND INVOLVEMENT: It is strongly suggested that the strategic plan be in written form and reviewed by the board of directors. Further, in order for the planning process to achieve maximum effectiveness, it is imperative that the entire plan be presented to all bank personnel. **Communication is vital to the success of the plan**. Top management must communicate to all employees that it is committed to its long-range plans and that every manager is expected to use it.

Following a presentation of the plan, it is appropriate to conduct meetings between each level of supervision and their subordinates. The primary purpose of such meetings is to respond to subordinates questions and concerns, solicit their ideas and establish their commitment to support the strategic plan.

The **secondary purpose** is to encourage a sense of employee participation. This idea is based on two management concepts: **1)** good ideas for improvement often exist in the minds of people who actually perform the work and **2)** people will more readily commit to accomplishing objectives that they have had a personal role in establishing.

<u>REVIEW AND MONITORING</u>: Managers at the highest level will need to consult the plan periodically and even reexamine the plan itself from time to time. To help achieve the goals established, progress must be monitored. Management must meet at regular intervals to evaluate how each department is accomplishing its specific tasks.

The plan must be flexible. Goals that are no longer realistic should be changed or eliminated. However, caution is advised against changing the plan too frequently. Once that happens, employees come to believe that management only uses the plan when it is convenient.

EXAMINER EVALUATION: The personnel of the State Bank Department firmly believe that a well-managed bank is one that conscientiously **<u>plans for change</u>** rather than merely **<u>reacts to change</u>**. With this in mind, one objective of the examining process will be to perform a review of management's planning process. The examiner is not to evaluate bank planning based on the preconception that every bank will have a model planning process. In fact, just the opposite will be emphasized - the planning process should be structured to reflect the unique characteristics of the bank in order for the process to be most effective. The examiner's criticism of planned actions will only be appropriate if the action contemplated will seriously harm the bank to a degree that requires regulatory concern or action.

In the event bank management has not developed a formal plan or reduced the plan to writing, the examiner shall obtain from senior management and/or the board of directors information supporting plans for such matters as growth, expansion, capital, dividend payouts, changes and mix of assets, changes in sources of funding, and changes in management and personnel.

The examiner shall review senior management's and the board of directors' commitment to the planning concept. The examiner will detail in the Report of Examination the bank's corporate planning process and determine if the following areas are addressed: adequate involvement of the bank's board; major departments are involved in the planning process; plans are effectively communicated throughout the organization; a monitoring and review process facilitates updates and revisions as warranted; and that future management and personnel needs are addressed and training and advancement policies will keep the organization viable and dynamic.

The examiner will have greater confidence in the management and future viability of the bank when it is determined that management has the ability and has taken the initiative to plan for change and is able to communicate the plan throughout the organization. Such confidence will be communicated to the Bank Commissioner and the bank's board of directors through the Report of Examination.

Strategic planning is not an end, but a means to managing change and focus on emerging opportunities.

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ADMINISTRATIVE POLICY #006

BILL J. FORD, BANK COMMISSIONER **RETAIN FOR**
DECEMBER 10, 1990 **FUTURE**
SUBJECT: ENVIRONMENTAL RISK IN LENDING **REFERENCE**

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Environmental issues and the magnitude of costs associated with remedial action regarding hazardous waste has begun to impact financial institutions. Lending transactions involving real estate as collateral are particularly at risk. Two types of environmental risk exist. In addition to the normal risk of loss of bankable assets that can be attributed to hazardous waste, there exists the potentially enormous liability of rectifying hazards existing in violation of state and federal law that far exceed an asset's value. This includes liability to third parties endangered by hazardous waste. Protection from this monetary liability, which can literally eliminate an institution's capital must be the goal of the bank's directorate, management, and legal counsel.

STATUTORY OVERVIEW

State and federal laws enacted to enforce and assess remediation of hazardous waste have been enforced to the detriment of financial institutions. The Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), commonly known as the Superfund, was created to authorize the Environmental Protection Agency to undertake remedial action or to direct others to do so. Under this law, any person or entity determined to be the owner or operator of an entity producing, causing, transporting, or storing hazardous waste can be assessed clean-up costs. This is the most important and severe law from a lender's point of view.

To be liable under CERCLA, a bank must be determined to be the owner or operator of a hazardous entity. Three defenses are recognized by CERCLA - an act of God, an act of war, or an act or omission by a third party commonly known as the **INNOCENT LANDOWNER DEFENSE**. To qualify as an innocent landowner, it must be demonstrated that due care has been exercised with respect to hazardous substances once discovered, and that precautions are taken against foreseeable acts or omissions of others. State law is often subjugated to this federal statute. Liability cannot be determined in Arkansas courts.

PRECAUTIONARY MEASURES

Education of personnel to the extent that identification of existing and potential environmental hazards can be recognized, and that appropriate actions follow, is primary in ensuring the success of all precautionary measures. Several important procedures have been identified. These include environmental assessment; loan agreement provisions; loan documentation, review, and monitoring foreclosure or workout procedures; and trust asset assessment. Incorporation of these procedures into current loan underwriting policies will help insulate financial institutions from environmental liability. A loan policy should contain provisions that allow for the identification of potentially risky transactions and include steps to follow through all stages of lending. Also included should be a system of internal checks and balances to provide for complete review, approval, and knowledge within the institution. Protective measures listed above and discussed below must begin at the earliest stage possible. Opening discussions with prospective borrowers whether written or verbal should refer to effects of any current or potential environmental hazards.

ENVIRONMENTAL ASSESSMENT

Assessment of the environmental hazards of a particular transaction is the first step that should be taken and can determine if a loan should ever be approved. The process is very site specific. The most recognized form of evaluation is an environmental audit performed in a phased approach. There is no governing body that regulates the performance of these audits, but industry standards exist. **It is recommended that only qualified professionals be used to conduct such audits.** Various private engineering and environmental service companies employ environmental engineers to perform these audits. The Federal National Mortgage Association Environmental Assessment Guidelines, Federal Home Loan Bank Thrift Bulletin 16, and Federal Home Loan Mortgage Corporation draft guidelines provide more detailed information on this topic and should be consulted to become familiar with this process. The three phases of environmental audits are highlighted briefly below.

PHASE I

- Historical review of the site
- Review of zoning, building, and regulatory codes
- Review of regulatory agency records
- Inspection of the site
- Written summary report

PHASE II

- To be performed if Phase I reveals apparent hazards
- Testing of underground storage tanks
- Soil, soil gas, bulk soil, groundwater, and surfacewater testing and sampling
- Comprehensive inspection, sampling, and analyzing of building materials
- Written summary report

PHASE III

- Contains all aspects of Phase I and II with the addition of much more involved testing and sampling procedures.

ENVIRONMENTAL QUESTIONNAIRE
A less informative type of assessment is an environmental questionnaire. This may be applied to all credit transactions to determine which steps to pursue thereafter, similar to a screening process. While an environmental questionnaire should not replace an environmental audit, it is a valuable tool and can be utilized for smaller credits when audits may be cost prohibitive.

THE LOAN AGREEMENT

A loan agreement cannot eliminate lender liability under CERCLA if the lender is otherwise liable, but it can make another party liable to the lender. The following covenants provide a starting point for protection from environmental liability in written credit instruments.

LOAN COVENANTS

- Require compliance with all laws, rules, regulations, and supervisory authorities, and notification of release of hazardous substances
- Require borrower to covenant that it will remedy any contamination that occurs
- Require borrower to indemnify lender for any losses or expenses incurred as a result of environmental problems
- Require indemnification or guaranty from a solvent parent company or individual
- Make lender beneficiary of environmental assessments by requiring audits to be addressed to borrower and lender, require access to all relevant documents
- Have borrower establish bond or trust to guarantee remediation of contamination
- Require borrower to obtain environmental impairment liability insurance if available and cost effective
- Insert due on sale clause
- Insert default or acceleration clause subject to use, storage, or disposal of hazardous materials on site
- Require default or acceleration if other breach of contract occurs
- Require additional security in event of contamination
- Require notification of violation of environmental laws
- Require borrower to allow lender access to records regarding environmental compliance and regulatory agencies

DOCUMENTATION, REVIEW, AND MONITORING

In addition to the normal documentation there are numerous items to which banks must devote special attention. These items remain almost entirely within an institution's power to control, and this power should be exercised to the institution's benefit.

- Review prior ownership and use of property
- Monitor manufacturing and operational process
- Monitor resource use and disposal
- Review litigation history
- Maintain current insurance coverage - property, liability, and environmental liability
- Maintain necessary current licenses, permits and inspections - local, state, and federal
- Monitor regulatory compliance for violations - historical and present
- Perform periodic inspection of site and underground storage tanks

FORECLOSURE OR WORKOUT SITUATIONS

As a loan enters a situation where foreclosure action is contemplated or a workout situation is apparent, special caution must be exercised regarding environmental risk. It is prudent to follow the same precautionary procedures used when a credit is originated. Prior to foreclosure, a new environmental audit should be performed to determine if there is sufficient risk of liability to a title holder that would negate any funds realized through foreclosure. Additionally, extreme care should be taken not to exert undue influence in the operation of an entity in a workout situation. A lender can be liable under CERCLA as an operator of an entity. Litigation, although case specific, does indicate that most lenders are not determined operators if their influence is limited to the financial aspects of the entity. However, the recent decision in United States v. Fleet Factors Corporation, 901 F.2d 1550 (11th Cir. 1990) is indicative of the dynamic nature of environmental liability litigation. This decision states that a secured creditor may be determined liable under CERCLA without being an operator if its influence in the financial management of the entity is of a degree that can enable it to impact hazardous waste management or environmental matters if it so chooses. Although not clearly defined by legal precedent, sufficient care must also be exercised and legal counsel consulted to preclude the conclusion that a creditor can control hazardous waste management through loan covenants or written agreements.

ENVIRONMENTAL RISK OF TRUST DEPARTMENT ASSETS

Legislation has been introduced in Congress designed to limit the liability of a fiduciary for hazardous waste contamination of property for which it holds legal title as part of an estate or trust. **Trust department assets at this stage of legislative action are essentially subject to the same environmental risk as those of the loan portfolio**. Prior to the acceptance of any real property into trust, steps similar to those delineated above should be initiated. They should include but not be ----limited to environmental assessments or audits where appropriate. The most important aspect as in any transaction affected by environmental hazards is proof of exercising due diligence. Special attention and caution must be exercised regarding decedent estates and dispersion or expenditure of funds relating to preemptive action or remediation of environmental hazards. Education of trust department personnel is paramount.

EXAMINATION CONSIDERATIONS

Examiners, when evaluating the risk inherent in the loan portfolio, will include an assessment of environmental risk. This assessment will primarily be measured against the implementation and enforcement of this policy. Foremost in the examination process is the determination that the financial institution has utilized this policy in exercising all prudent avenues available to protect their interests against the risk of environmental liability. The presence of environmental risk or noncompliance with this policy will adversely affect the determination of the soundness and viability of an institution.

REFERENCE OF APPLICABLE LAWS

There is no well defined procedure that lenders can follow that will guarantee protection from liability for environmental hazards. Nothing can entirely eliminate the risk of liability. Partially responsible for this situation is the nebulous framework of existing state and federal statutes characterized by the volatility of environmental issues and proposed legislation. Lenders may wish to consult the Environmental Protection Agency and request their Draft Rule on Lender Liability under CERCLA which should be finalized in the future. This guidance is informative and contains suggestions similar to those found within this policy. Listed in part below are state and federal laws that impact this policy. It must be recognized that while this policy is designed to protect lenders from environmental liability, noncompliance with the numerous related state and federal statutes can compromise a secured creditor's position in other ways such as monetary penalties and weakened collateral margins.

FEDERAL STATUTES

- Resource Conservation and Recovery Act (RCRA)
- Hazardous and Solid Waste Amendments (HSWA)
- Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), "Superfund Act"
- Superfund Amendments and Reauthorization Act (SARA)
- Clean Water Act
- Clean Air Act
- Toxic Substances Control Act**FEDERAL AGENCIES**
- Environmental Protection Agency (EPA)
  Enforcement and administration of federal statutes
- Department of Justice

Justice Department Land and Natural Resource Division litigates RSRA and CERCLA claims for the EPA.

STATE STATUTES

- Arkansas Hazardous Waste Management Act
- Arkansas Remedial Action Trust Fund Act (RATFA)
- Arkansas Emergency Response Fund Act (ERFA)
- Arkansas Water and Air Pollution Control Act
- Recent legislation:
- Act 172 of 1989, Codified at Secs. 8-7-801-812, A.C.A. Of 1987 (1989 Supp) Regulates underground storage tanks
- Act 173 of 1989, Codified at Secs. 8-7-901-908, A.C.A of 1987 (1989 Supp.) Cost and damage recovery for storage tank hazards: **Compliance with underground storage tank regulations can substantially reduce potential liability and provide availability of fund for remediation.**

- Act 260 of 1989, Codified at Secs. 18-49-103, 8-6-205, 8-7-409, 8-7-508, 8-7-403, and 8-7-307, Arkansas Code of 1987 Annotated (1989 Supp.) Innocent landowner's remedies and defenses

STATE AGENCIES

- Arkansas Department of Pollution Control and Ecology Enforcement and administration of state statutes

SUMMARY AND CONCLUSION

There is a general proclivity to address solutions after problems occur in the financial world. This policy is designed to combat that situation by requiring preventive measures. Pollution and hazardous waste problems are having an increasingly large monetary impact on financial institutions. Governments in some instances have the right to assign liability to persons or entities no longer holding title to contaminated property. A lender seeking to enforce a mortgage by foreclosure may be exposed to a risk of liability as the owner or operator of a hazardous waste site that far exceeds the property value or revenue generated by the site. These facts have caused traditional loan underwriting procedures to be inadequate. This policy will aid financial institutions in establishing precautionary procedures that will help them evaluate not only the normal business risk associated with hazardous waste, but the threatening liability that may arise.

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ADMINISTRATIVE POLICY #007 ***REVISED – 09/01/05***
Robert H. Adcock, Jr., Bank Commissioner

BILL J. FORD, BANK COMMISSIONER **RETAIN FOR**
DATE: JANUARY 31, 1995 **FUTURE**
SUBJECT: CONTINGENCY PLANNING **REFERENCE**

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The community bank plays a vital role in rebuilding a community in the event of a catastrophic disaster as well as a localized disaster. In order for the community bank to respond quickly and efficiently to the needs of the community and its own needs, the bank must be prepared to implement a comprehensive and effective contingency plan.

A. General Concept

The contingency plan should set forth the bank's plan of action in dealing with various emergency situations. To be effective, the plan should contain as much detail as possible and incorporate each of the bank's departments. The purpose of contingency planning is to minimize disruptions of service, minimize financial loss, and ensure timely resumption of operations.

Contingency planning is an ongoing process. After the plan is written, it should be approved by the Board of Directors and reviewed annually. In order for the plan to be successfully implemented, it must be presented and discussed with all bank personnel. Employees should be appropriately trained to handle certain emergency situations. The areas addressed in this policy apply to in-house systems, remote job entry sites and data processing servicers. Banks and data processing servicers which have not adopted a contingency plan will be cited for contravention of this policy.

B. Contingency procedures.

Written contingency procedures should, at a minimum address:

1. Conditions or situations that necessitate implementing the plan and using the backup site.
2. Responsibility for making a decision and guidelines as to when it should be made.
3. Notification of employees.
4. Backup site notification.
5. Procedures to be followed at the backup site.
6. Files, input work, special forms, etc., to be taken to the backup site and means of transportation.

7. Facility shutdown.
8. Executive succession.
9. Hardware/Software backup.
10. Data files/off-site storage.
11. Training.
12. Telecommunications backup.
13. Evacuation and shelter.
14. Emergency services and information.
15. Microcomputer processing.
16. Priority of applications to be processed.

C. Contingency plan testing and review.

The contingency plan should be tested at least every twelve months. For example, if the last test date was March 31, 1994, the bank must test the plan on or before March 31, 1995. If the contingency plan is not tested within the required time frame, the bank will be cited for contravention of this policy. It is also recommended the plan be tested whenever there are major changes in personnel, policies and procedures or hardware and software products.

Backup files should be used when testing is performed at the backup site. After testing, a summary report of the test should be presented to the Board of Directors for review.

D. Out-of-State Servicers.

If a bank has an out-of-state servicer that performs EDP contingency processing, a representative from the bank generally will not be required to attend the process testing, However, the Commissioner may require such attendance if he should determine it to be necessary for a particular institution. Such determination will be done on a case-by-case basis. If a bank representative is required to attend, the representative should ensure that:

1. The bank's data is processed in a timely manner.

2. Communication between the backup site and the bank is established and maintained.

3. Assist servicer in the processing of software applications.

Further guidance for contingency planning and procedures can be found in the Information Systems Handbook prepared by the Federal Financial Institutions Examination Council (FFIEC). Additional materials regarding contingency/disaster recovery planning may be obtained from trade associations, accounting firms, and the disaster recovery industry.

Agency # 210.00

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ADMINISTRATIVE POLICY #008

FRANK WHITE, BANK COMMISSIONER	**RETAIN FOR**
SEPTEMBER 30, 2002	**FUTURE**
SUBJECT: BANK BOARD OF DIRECTORS	**REFERENCE**

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Business Policies of state banks are formulated by the bank's Board of Directors. These Boards should be composed of persons knowledgeable about economic conditions of their community and their region, competent business persons, and skilled in financial management. The Board of Directors must be attentive to their duties, familiar with banking laws and regulations, and aware of their fiduciary responsibilities. The bank's Board of Directors has the ultimate responsibility and fiduciary liability to ensure the safe and sound operation of their financial institution for the benefit of the shareholders and general public.

In order to assist Directors in their industry education and awareness of responsibilities, all members of a state bank's Board of Directors must attend Director training approved by the Bank Commissioner. Directors first elected to the Board on or after October 15, 2002, must attend one training seminar within the first year of service. Directors first elected prior to October 15, 2002, must attend one training seminar prior to October 15, 2004.

Evidence of Director attendance at a training seminar must be maintained in the Board Minutes of the bank.

SECTION 15

COUNTY OR REGIONAL INDUSTRIAL DEVELOPMENT CORPORATIONS

A.C.A. § 15-4-1201 through A.C.A. § 15-4-1228

Purposes of Each Industrial Development Corporation: The purpose of each industrial development corporation organized pursuant to A.C.A. § 15-4-1201 et seq. is to promote, stimulate, develop, and advance the business of and economic welfare of the county or region included in its organization. The Bank Commissioner and the State Banking Board therefore rule that in order to implement the intentions of the act, companies should make every effort to use the assets raised by the corporation to pursue the intentions set out in the act. The Bank Commissioner and the State Banking board recognize that some projects will require a certain period of time to raise capital in order to fund a particular project or to identify a deserving project to fund. However, the Bank Commissioner and the State Banking Board will consider the failure of an industrial development corporation to seriously investigate worthwhile projects or make investments in economic development projects for an unreasonable period of time to be a violation of the intentions of the act.

An industrial development corporation shall not sell shares or units and fail to utilize the proceeds thereof in accordance with the purposes set forth in A.C.A. § 15-4-1214(a). Except as provided below, in the event that such proceeds are not invested, loaned or otherwise utilized in accordance with such purposes within eighteen (18) months from the date on which such funds are received, the industrial development corporation shall immediately cancel all such shares or units and refund to the purchasers of such shares or units all proceeds, plus interest or income derived thereon, on a pro rata basis, as well as all commissions or remuneration paid to any person on account of the sale thereof. Such refund, with the exception of the interest or profit derived thereon, shall not be considered to be a dividend or distribution within the meaning of A.C.A. § 15-4-1215, and shall be treated as set forth in A.C.A. § 15-4-1224 (a)(2)(A). Provided however, that upon written application and for good cause shown, the Bank Commissioner may in his discretion extend such period for two additional six (6) month periods, not to exceed a total of thirty (30) months from the date on which the proceeds from the sale of the stock or units were received by the industrial development corporation. Each extension shall require a separate application filed by the industrial development corporation with the Bank Commissioner at least ten (10) days prior to the expiration of the period sought to be extended. Proceeds, unless otherwise clearly accounted for by the industrial development corporation, shall be accounted for on a first in, first out basis.

I. **INFORMATION**. The Arkansas State Banking Board, in order to meet the statutory obligation to examine and supervise/regulate county or regional industrial development corporations organized pursuant to A.C.A. § 15-4-1201, et seq., require such organizations to submit the following information to the Arkansas State Bank Department:

A. Quarterly financial reports containing financial information requested by the Arkansas State Bank Department. Each quarterly financial report must be filed with the Department no later than forty-five days following the calendar quarter ending on March

31, June 30, September 30, and December 31 of each year. Any county or regional industrial development corporation that fails or refuses to file a financial report with the Department within the time limitations set forth by this regulation may be assessed a monetary penalty against the county or regional industrial development corporation in the amount of one hundred dollars ($100) per day for the first thirty (30) days of violation and five hundred dollars ($500) per day of violation for every day thereafter;

B. An annual independent audit of the corporation, which has been performed by a qualified accounting firm. This audit is required to be submitted to the Arkansas State Bank Department no later than April 15 of each year. Any county or regional industrial development corporation that fails or refuses to file an annual independent audit with the Department by or before April 15 of each year may be assessed a monetary penalty against the county or regional industrial development corporation in the amount of one hundred dollars ($100) per day for the first thirty (30) days of violation and five hundred dollars ($500) per day of violation for every day thereafter;

C. The Bank Commissioner may extend the time for filing a quarterly or annual report upon the request in writing by a county or regional industrial development corporation. The request must provide a good cause for such extension and must have prior approval of the Bank Commissioner.

D. An annual list of shareholders, which must be submitted to the Arkansas State Bank Department within thirty days from December 31 each year; and

E. Any changes or amendments made in the company's Articles of Incorporation.

II. **IMPAIRED ASSETS OR CAPITAL.** Arkansas Code § 15-4-1202(5) defines "impaired" capital or assets as when the capital of the company has been reduced to fifty thousand dollars ($50,000) or less.

III. **ASSESSMENT FEES**. The State Banking Board and the Bank Commissioner require that assessment fees payable on a semi-annual basis to the State Bank Department be remitted by automated processing as established by the Bank Commissioner. Exceptions for payment of assessment fees by any other method than the automated method established by the Department must be upon prior request and approval by the Bank Commissioner. Exception requests will only be approved on an extraordinary basis.

IV. **APPLICATION REQUIREMENTS**: Applications submitted to the Bank Commissioner for consideration of preliminary approval must include such information that the Bank Commissioner determines is necessary in order to consider the qualifications of the organizers. This information must include, but not be limited to, a complete financial background review, permission to seek a current credit report, past and current business involvement, prior involvement with an industrial development corporation, a listing of the proposed Board of Directors or Management Committee, and a criminal background check.

Single purpose applications shall include information, in sufficient detail for the Bank Commissioner to consider, the potential economic development or community development, or similar project, that the applicant has under serious consideration.

Multiple purpose applications shall include, in sufficient detail for the Bank Commissioner to consider, at least three potential economic development or community development, or similar projects, that the applicant has under serious consideration.

Upon a preliminary approval of an application, applicant is required to provide the Arkansas State Bank Department with evidence that the required initial capital is being held in escrow pending final approval of the Arkansas State Banking Board.

SECTION 16
TRUST INSTITUTIONS

FEES AND ASSESSMENTS SCHEDULE

A.C.A. § 23-51-101 through A.C.A. § 23-51-211

1.1 - Fees.

a) Application for new Trust Company $8,000
b) Official protest of application 2,000
c) Private Trust Company application 4,000
d) Private Trust Company Annual Certificate....................200
e) Acquisition of Control of Trust Company 1,500
f) Charter Amendments 200
g) Application for merger....................2,500
h) Registration of corporate name 25
i) Additional trust office 300
j) Out-of-state office....................300
k) Registration of out-of-state Trust Company 300

1.2 - Assessments, Examination Fees.

Assessment fees to defray the costs of examinations and the costs of operations of the State Bank Department will be charged in January and July of each year.

The assessment schedule is as follows:

> A base assessment fee of $1,250 will be billed by the State Bank Department to each state-chartered trust company on a semi-annual basis in January and July of each year. In addition, an assessment of $360 per examiner per day or partial day of examination times the number of examination days will be billed in January or July immediately following the examination in order to defray the costs of examination to the department. These assessments will be payable within ten (10) days after notice from the Commissioner in January and July of each year.

1.3 - Confidential Information.

In addition to information maintained as confidential in accordance with Section 87 of Act 940 of 1997, the following information submitted in support of an application for trust charter, office, or representative office shall be maintained as confidential:

a) Any financial statement of a proposed officer, director, or principal shareholder;
b) Names of any proposed officer requesting to remain confidential due to current employment status.

1.4 - Bonding Requirements - State Chartered Trust Company.

The board of a state trust company shall require protection and indemnity against dishonesty, fraud, defalcating, forgery, theft, and other similar insurable losses on each director, officer, and employee of the company in an amount not less than $1,000,000 or such greater amount which is determined to be reasonable in accordance with the Board of Directors resolution based upon the asset size of the trust company.

1.5 Transfer of Stock – State Chartered Trust Company

(a) The stock of every state trust company shall be transferable only on the books of the trust company.

(b) When any number of shares of the stock of a state trust company shall be transferred to any transferee or joint transferees, the state trust company shall promptly transmit to the Commissioner a certificate, on a form prescribed by the Commissioner, showing such transfer. The certificate also shall show the total number of shares at that time outstanding in the name of the transferee or anyone known by the state trust company to be the nominee of the transferee or holding in trust for the transferee.

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