



## **OVERVIEW OF GEORGIA LAW FOR INSTITUTIONS CONSIDERING CONVERSION TO A GEORGIA STATE BANK CHARTER**

The information below is provided to answer some frequently asked questions for the management of institutions considering conversion to a Georgia state-chartered bank. For more precise information, please refer to the Official Code of Georgia and the Rules of the Department of Banking and Finance, or consult a representative of the Department.

Georgia Law provides for lending limits, limitations on investments on fixed assets, and certain other limits, to be based on the bank's Statutory Capital Base. The definition of Statutory Capital Base differs significantly from the "Total Capital" definition in federal law. The definition Statutory Capital Base is designed to be fixed, and not to fluctuate day to day, so that lending limits do not change unless there is a change in the bank's capital structure, other than net income. The definition of Statutory Capital Base is contained in Section 7-1-4 (35) of the Official Code of Georgia, and consists of the sum of:

- Capital Stock
- Paid-in Capital (a.k.a. Surplus)
- Appropriated Retained Earnings
- Capital Debt
- Less any amount of good will, core deposit intangibles, or other intangible assets related to the purchase, acquisition, or merger of a bank

Appropriated Retained Earnings is that portion of the institution's Retained Earnings (a.k.a. Undivided Profits) that the Board of Directors has declared as unavailable for dividends. The Board minutes must contain the resolution of the Board, which sets aside the portion of Retained Earnings as unavailable for dividends. (For those institutions with negative undivided profits, Statutory Capital Base consists of Total Assets less Total Liabilities. This is known as "the net assets" of the institution, but does not apply to most institutions converting from a federal or national charter to a state charter.)

### **Lending Limit**

Section 7-1-285 of the Official Code of Georgia establishes limits on loans to one person or corporation. In general, state banks are limited to aggregate loans to one person or corporation of 15% of Statutory Capital Base for unsecured debt and 25% of Statutory Capital Base for loans that are secured by "good collateral or other ample security". If aggregate debt exceeds 15% of Statutory Capital Base, then all loans and obligations must be fully secured, not just the portion that exceeds the 15% limit. (There are certain types of loans exempt from the 15% and 25% limitations: these are described in detail within the code section and Rule 80-1-5 of the Department's Rules.)

The aggregate lending limits described above include all loans to one person or corporation. However, the law provides that the Department may specify that the liabilities of a group of one or more persons or corporations or limited liability corporations (LLCs) or both shall be considered as owed by one person or corporation if the group relies substantially on a common source of payments of its obligations or makes common use of funds received by it. In making this determination to combine loans of separate person, corporations, and entities for the aggregate lending limits described above, the Department shall consider both direct and indirect debt, including loans to any individual person, all amounts loaned to firms and partnerships of which that person is a member. Please do not hesitate to consult with representatives of the Department if you have any questions regarding amounts to be included for aggregate debt limits.

In lieu of following the lending limitations described above contained in Code Section 7-1-285(a) through (c), a financial institution may petition the Department for approval to utilize limits applicable to national banks regarding obligations of a single person or corporation.

For purposes of 7-1-285, "good collateral or other ample security" may include real estate that is properly supported by an independent appraisal. The Rules of the Department of Banking and Finance state that in determining whether or not a loan in excess of the 15% limitation is secured by good collateral or other ample security, the lack of a perfected lien, inadequate insurance, required margins between collateral value and the amount of the loan shall be prima facie evidence of inadequate security to the debt. Loans secured by endorsement must be supported by a financial statement on the endorser, properly signed, which is not more than eighteen months old, if the loan is to be considered properly secured, and such statement must reflect adequate income to service the loan and unencumbered equity sufficient to protect the loan.

## **Real Estate Loans**

Section 7-1-286 of the Official Code of Georgia and Rule 80-1-5 of the Department establishes standards for real estate loans and are meant to provide parity for state chartered banks with nationally chartered banks. Basically, banks must now adhere to the provisions of Part 365 of the Federal Deposit Insurance Corporation's rules and regulations, including 12 C.F.R. 365.1 and 365.2 and the Interagency Guidelines for Real Estate Lending Policies in Appendix A and 12 C.F.R. 208.51 and the guidelines contained in 12 C.F. R. Part 208 in the case of Federal Reserve member banks. Some limited state provisions remain in the rule representative of areas not covered in Part 365.

## **COMMON AREAS IN NEED OF REVISION TO COMPLY WITH GEORGIA LAW**

In addition to the lending limit requirements described previously, listed below are several areas that should be reviewed by institutions wishing to convert to a Georgia state bank charter to determine if corrective action will need to be taken to comply with state law after conversion. This is by no means an exhaustive list of all actions that must be taken to comply with Georgia law, but is provided to assist converting institutions with a short list of common areas noted at other institutions converting to a state charter.

As provided for in Georgia law, when a conversion becomes effective, the existence of the national bank shall continue in the resulting state bank, which shall have all the property, rights, powers, trusts, duties, and obligations of the national bank. The resulting state bank shall have the authority to engage only in such lines of business and activities and exercise only such powers or hold such assets as are then permissible upon original incorporation; provided, however, that if the converting institution owns or holds assets, engages in any business, or has powers that would not be allowed for a state bank, then the plan of conversion shall include a plan for holding or disposal of such nonconforming assets or the continuation or termination of such line of business, activity, or power. The Department will review the plan to determine whether, in the interest of safety and soundness, the activity, power, asset, or line of business should be approved, denied, or phased out within a reasonable period of time (normally up to four years from effective date of conversion).

## **Fixed Assets Limitation**

Rule 80-1-10-.01 (2) of the Georgia Department of Banking and Finance limits the amount of investment in fixed assets by a bank to a maximum of 60% of the bank's Statutory Capital Base, unless prior approval from the Department is granted to exceed this limit. The institution's investment in fixed assets should be reviewed for compliance with this statutory limit. If the fixed assets investment is in excess of this limit, this situation may be corrected either by immediately restructuring the capital accounts to increase the 60% limit, or by applying to the Department to exceed the limitation described above. The application should be in letter form and must provide for an orderly plan for restoring the fixed asset investment to the 60% limitation within five years, either through

depreciation or predetermined plans to restructure the capital accounts to increase the 60% legal limitation, or a combination of these methods.

### **Approval of Other Real Estate**

Section 7-1-263 of the Financial Institutions Code of Georgia states, in part, that a bank or trust company may acquire and hold property for the purpose of avoiding loss subject to a determination by a majority vote of its Directors at least once each year as to the advisability of retaining any such property, provided that no such property may be held for more than five years without the prior written approval of the Department. All assets acquired through foreclosure should be appraised within (1) one year from acquisition and subsequent appraisals should be at intervals not to exceed 5 years. An independent appraiser should perform the appraisal, unless the book value of the property does not exceed 2% of the bank's statutory capital base, in which case a qualified bank officer can perform the appraisal.

### **Oath of Directors**

Section 7-1-484 of the Financial Institutions Code of Georgia states, in part, that each Director, before assuming office, shall take an oath or affirmation that he/she will diligently and honestly perform his/her duties in the administration of the affairs of the bank or trust company, that he/she will not permit a willful violation of law by the bank or trust company, and that he/she meets the eligibility requirements of this chapter and of the articles and bylaws. A copy of the oath shall be signed by each Director and shall be placed into the minutes of the meetings of the directors. No Director shall be authorized to participate in the affairs of the Board or receive any compensation for service as a Director until the oath has been executed by such Director. A form for the completion of the oaths is available from the Department.

### **Term and Meetings of Directors**

Section 7-1-482 (b) of the Financial Institutions Code of Georgia states, in part, that each Director shall be elected by the shareholders for a term of one year or for staggered terms as provided in Section 14-2-806 and shall serve until he/she resigns, is removed, or becomes disqualified or until his successor shall have been duly elected and qualified. The institution's bylaws should be reviewed to determine the length of the term for the institution's Directors. That term shall meet the requirements of either Section 7-1-482 or 14-2-806. A copy of the Department's "Standard Bylaws for Banks" is available from the Department.

The board of directors should hold at least one meeting in each of ten different months unless an alternative schedule is approved in writing by the department. In no case should the board meet less frequently than once each calendar quarter.

### **Director's Committees**

The board of directors may designate three or more directors to constitute a committee, which shall have and exercise the authority of the board.

### **Directors Financial Statements**

Rule 80-1-6-.03 of the Department of Banking and Finance requires each director to maintain a financial statement on file with the CEO of the bank. The financial statement shall be revised annually, but in no event shall the statement on file be more than eighteen months old. At the discretion of the Board of Directors of each bank, such financial statements may be maintained in sealed envelopes available for inspection only by state and federal examiners.

## **Management**

At each regulatory examination, management will be asked to provide salary and bonus information relating to the officers of the bank. Management may also be requested to provide a copy of the bank's Compensation Policy and/or Plan.

## **Dividends**

Banks may declare and the bank may pay cash dividends on its outstanding stock without Department approval under the following conditions:

1. Total classified assets at the most recent examination do not exceed 80% of Tier 1 Capital plus the Allowance for Loan Losses as reflected at such examination.
2. The aggregate amount of dividends declared or anticipated to be declared in a calendar year does not exceed 50% of the net profits after taxes but before dividends for the previous calendar year. A Subchapter S – Corporation may pay an additional amount of dividends without Department approval equivalent to fifty (50) percent of the income taxes which the bank would have had to pay as a Subchapter C-Corporation.
3. The ratio of Tier 1 Capital to Adjusted Total Assets shall not be less than six (6) percent.
4. Paid-in capital and appropriated retained earnings equal at least 20 percent of capital stock.

Please refer to Section 7-1-460 of the OCGA and Rule 80-1-12 of the Department of Banking and Finance for further discussion related to dividend requirements.

## **Audit**

Section 7 -1-487 of the Financial Institutions Code of Georgia states, in part, that the Board of Directors shall at least once each year have made by an independent certified public accountants an audit of the books and affairs of the bank. A signed copy of the audit report shall be submitted to the board for approval or rejection and kept in the files of the bank. The minutes of the board should indicate that the audit was submitted to the Board, and the minutes should specify that the audit was either accepted or rejected.

## **Cash Items Register, Overdrafts, and Charged Off Assets**

Rule 80-1-3-.01 (l)(d) of the Georgia Department of Banking and Finance requires the bank's cash item register to show the maker of the item, last endorser, if any, date acquired by the bank, amount of the item, and reason held. The Board of Directors is required to review the current register at least monthly. The institution's cash item register should be reviewed to ensure that all five items are recorded.

Rule 80-1-3-01 (l)(g) of the Georgia Department of Banking and Finance requires the most current record of overdrafts to be approved by the Board of Directors or Loan Committee at least monthly, and such approval shall be recorded in the minutes of the meeting at which the action was taken.

Rule 80-1-3-.01 (l)(h) of the Georgia Department of Banking and Finance requires that charge-offs must be approved by the Loan Committee, in the case of loans, or Board of Directors and such approval shall be recorded in the minute book. A record of all charge-offs and recoveries thereon must be maintained.

Paragraph 80-1-3-.01(2) states that where a bank has common capital, surplus, and capital securities of \$5,000,000 or more, the review by the Board for cash items, overdrafts, and charged-off assets may be delegated to a specific officer or department of the bank, provided such delegation is recorded in the minutes of the Board of Directors. A properly constituted Loan Committee, as described above in the section entitled "Committees", may perform this function for the full Board of Directors regardless of the size of the bank.

## **Public Funds**

Section 45-8-12 of the Financial Institutions Code of Georgia states that deposits of a public body must be secured by a surety bond, or in lieu of a surety bond, by a pledge of securities or deposit insurance. The market value of securities pledged must equal 110% of the value of the deposit after the deduction of the amount of deposit insurance. The institution's public deposits should be reviewed to ensure that each individual public depositor is secured by sufficient bond or pledge.

## **Other**

Many of the forms and applications that state-chartered banks frequently require can be accessed via the Department's web site at <http://dbf.georgia.gov/>.