

1/

{{6-30-96 p.C-4187}}

[¶11,283] **In the Matter of First State Bank, Moulton, Texas, Docket No. FDIC-95-162b (4-26-96)**

Bank to cease and desist from such unsafe or unsound practices as operating with management whose policies and practices are detrimental to the bank and jeopardize the safety of its deposits; operating without adequate supervision and direction by the board of directors; operating with an inadequate level of capital protection; engaging in hazardous lending and/or ineffective and lax collection practices; failing to provide an adequate allowance for loan and lease losses; operating without adequate written loan policies and procedures; failing to accurately reflect the condition of the bank in published statements and consolidated reports of condition and income; and operating in violation of applicable federal and state laws and regulations.

- [.1] **Capital—Tier 1 Capital—Increase**
- [.2] **Dividends—Restricted**
- [.3] **Assets—Adversely Classified—Reduce or Eliminate**
- [.4] **Loan Loss Reserve—Increase**
- [.5] **Loan Loss Reserve—Policy for Determining Adequacy of**
- [.6] **Consolidated Reports of Condition and Income—Review and Amend**
- [.7] **Management—Qualifications Specified**
- [.8] **Board of Directors—Committee to Review Compliance with Cease and Desist Order**
- [.9] **Loan Policy—Revise, Adopt, and Implement**
- [.10] **Violations of Law—Eliminate or Correct**
- [.11] **Technical Exceptions—Correction Required**
- [.12] **Shareholders—Disclosure—Cease and Desist Order**
- [.13] **Cease and Desist Orders—Compliance Reports**

In the Matter of

**FIRST STATE BANK
MOULTON, TEXAS
(Insured State Nonmember Bank)
ORDER TO CEASE AND DESIST
FDIC-95-162b**

First State Bank, Moulton, Texas ("Bank"), through its board of directors, having been advised of its right to the issuance and service of a NOTICE OF CHARGES AND OF HEARING detailing the unsafe or unsound banking practices and violations of law and/or regulations alleged to have been committed by the Bank and of its right to a hearing on the alleged charges under section 8(b) of the Federal Deposit Insurance Act, 12 U.S.C. § 1818(b), and having waived those rights, entered into a STIPULATION AND CONSENT TO THE ISSUANCE OF AN ORDER TO CEASE AND DESIST ("CONSENT AGREEMENT") with counsel for the Federal Deposit Insurance Corporation ("FDIC") dated April 3, 1996. For the purpose of this proceeding and without admitting or denying the alleged charges of unsafe or unsound banking practices and violations of law and/or regulations, the Bank consented to the issuance of an ORDER TO CEASE AND DESIST ("ORDER") by the FDIC.

The FDIC considered the matter and determined that the Bank had engaged in unsafe or unsound banking practices and had violated laws and/or regulations. The FDIC, therefore, accepted the CONSENT AGREEMENT and issued the following:

ORDER TO CEASE AND DESIST

IT IS ORDERED, that the Bank and institution-affiliated parties of the Bank cease and desist from all of the following unsafe or unsound banking practices and violations of laws and/or regulations:

- (a) Operating the Bank with management whose policies and practices are detrimental {{6-30-96 p.C-4188}}to the Bank and jeopardize the safety of its deposits;
- (b) Operating the Bank without adequate supervision and direction by the board of directors over the management of the Bank;
- (c) Operating with an inadequate level of capital protection;
- (d) Engaging in hazardous lending and/or ineffective and lax collection practices;
- (e) Failing to provide an adequate allowance for loan and lease losses;

- (f) Operating the Bank without adequate written loan policies and procedures;
- (g) Failing to accurately reflect the condition of the Bank in published statements and Consolidated Reports of Condition and Income; and
- (h) Operating the Bank in violation of applicable Federal and State laws and regulations as more fully set forth on pages 8.13 through 8.17 of the Report of Examination of the Bank as of July 17, 1995.

IT IS FURTHER ORDERED, that the Bank take affirmative action as follows:

[.1] 1. (a) Not later than 30 days after the effective date of this ORDER, the Bank shall submit a written plan to the Regional Director of the FDIC's Dallas Regional Office ("Regional Director") and the Banking Commissioner for the State of Texas ("Commissioner") to cause the Bank to achieve and maintain a Tier 1 leverage capital ratio ("leverage ratio") equal to or greater than 6.0%. After the Regional Director and the Commissioner respond to the plan, the board of directors of the Bank shall adopt the plan, including any modifications or amendments requested by the Regional Director and the Commissioner. Thereafter, the Bank shall immediately initiate measures detailed in the plan, to the extent such measures have not previously been initiated, to effect compliance with the plan within 30 days after the Regional Director and the Commissioner respond to the plan. Any increase in Tier 1 capital necessary to meet the ratio required by this ORDER may be accomplished by:

- (i) The sale of common stock;
- (ii) The direct contribution of cash subsequent to July 17, 1995 by the parent Bank holding company; or
- (iii) Any other method approved by the Regional Director and the Commissioner.

(b) If the Bank is found to be in noncompliance with the plan and the leverage ratio is less than 6.0 percent, as determined at an examination by the FDIC or the State banking department, the Board shall, within 30 days after receipt of a written notice of the capital deficiency from the Regional Director or the Commissioner take all of the following actions:

- (i) Develop another plan to bring the ratio to 6.0 percent;
- (ii) Present the plan to the Regional Director and the Commissioner for their review and approval; and
- (iii) Modify the plan as requested by the Regional Director and the Commissioner.

Within 10 days after the Regional Director and the Commissioner approve the plan, the Bank shall adopt it. Thereafter, the Bank shall immediately initiate measures detailed in the plan (unless such measures have already been initiated) to increase the Bank's Tier 1 capital by an amount sufficient to bring the leverage ratio to 6.0 percent within 60 days after the Regional Director and the Commissioner respond to the plan.

(c) If all or part of the increase in Tier 1 capital required by this ORDER is to be accomplished by the sale of new securities, the board of directors of the Bank shall adopt and implement a plan for such sale. The plan shall include soliciting proxies and the voting of any shares or proxies owned or controlled by them in favor of the plan. Should the implementation of the plan involve a public distribution of the Bank's securities (including a distribution limited only to the Bank's existing shareholders), the Bank shall take all of the following actions:

- (i) Prepare offering materials fully describing the securities being offered;
- (ii) Include in the materials an accurate description of the financial condition of the Bank and the circumstances giving rise to the offering;
- (iii) Add any other material disclosures necessary to comply with Federal securities laws; and
- (iv) Submit the capital plan and offering materials to the FDIC's Registration and Disclosure Section, Wash- [6-30-96 p.C-4189](#) ington, D.C. 20429, not less than 20 days prior to dissemination, for review and approval.

Any changes requested to be made in the plan or the materials by the FDIC shall be made prior to their dissemination. If the increase in Tier 1 capital is to be provided by the sale of noncumulative perpetual preferred stock, then all terms and conditions of the issue shall be presented to the Regional Director for prior approval.

(d) In complying with the provisions of this ORDER and until such time as any such public offering is terminated, the Bank shall provide to any subscriber and/or purchaser of the Bank's securities written notice of any planned or existing development or other change which is materially different from the information reflected in any offering materials used in connection with

the sale of the Bank's securities. The written notice required by this paragraph shall be furnished within 10 days after the date such material development or change was planned or occurred, whichever is earlier, and shall be furnished to every purchaser and/or subscriber who received or was tendered the information contained in the Bank's original offering materials.

(e) In addition to the requirements of subparagraphs 1(a) - (b), the Bank shall comply with the FDIC's Statement of Policy on Risk-Based Capital found in Appendix A to Part 325 of the FDIC Rules and Regulations, 12 C.F.R. Part 325, App. A.

(f) For the purposes of this ORDER, the terms *Tier 1 capital*, *leverage ratio*, and *total assets* shall have the meanings ascribed to them in Part 325 of the FDIC's Rules and Regulations.

[.2] 2. While this ORDER is in effect, the Board shall neither declare nor pay, directly or indirectly, any cash dividend to shareholders without the prior written consent of the Regional Director and the Commissioner.

[.3] 3. Upon the effective date of this ORDER, the Bank shall eliminate, by charge-off or collection, all assets classified Loss and one-half of assets classified Doubtful in the Report of Examination as of July 17, 1995 ("Report"). While this ORDER is in effect, the Bank shall ensure the elimination of all assets classified Loss at any subsequent State or FDIC examination on or before the date the examination report is received by the Bank.

[.4] 4. (a) Within 10 days from the effective date of this ORDER, the Bank shall increase the Allowance for Loan and Lease Losses ("ALLL") to an adequate level.

[.5] (b) Within 60 days of this ORDER, the Bank shall establish a comprehensive policy for determining the adequacy of the ALLL. The policy, which shall provide for a review of the ALLL at least quarterly, will focus on the following areas:

- (i) Internal loan review;
- (ii) Loan loss experience;
- (iii) Past due and non-accrual loan trends;
- (iv) Potential loss exposure on significant credits;
- (v) Concentrations of credit; and
- (vi) Present and prospective economic conditions.

Details of these reviews will be recorded in the official Bank minutes, including the methodology for determining any adjustments.

[.6] (c) Within 60 days after the effective date of this ORDER, the Bank shall review Consolidated Reports of Condition and Income filed with the FDIC on or after June 30, 1995, and amend said reports if necessary to properly reflect the financial condition of the Bank as of the date of each such report. In particular, such reports shall contain an adequate allowance for loan and lease losses and properly report loan and lease portfolio losses as charges to this allowance. Reports filed after the effective date of this ORDER shall also accurately reflect the financial condition of the Bank as of the reporting date.

[.7] 5. The Bank shall have and retain qualified management. Each member of management shall possess qualifications and experience commensurate with his or her duties and responsibilities at the Bank. The qualifications of management personnel shall be evaluated on their ability to achieve all of the following:

- (a) Comply with the requirements of the ORDER;
[{{6-30-96 p.C-4190}}](#)
- (b) Operate the Bank in a safe and sound manner;
- (c) Comply with applicable laws and regulations; and
- (d) Restore all aspects of the Bank to a safe and sound condition.

During the life of the ORDER, the Bank shall notify the Regional Director and the Commissioner in writing prior to making any changes in management. The notification must include the name(s) and background(s) of any proposed replacement personnel.

[.8] 6. (a) Within 30 days after the effective date of this ORDER, the Bank shall establish a committee of directors charged with the responsibility of ensuring that the Bank complies with the

provisions of this ORDER. At least two-thirds of the members of such committee shall be independent, outside directors as defined herein. The committee shall report monthly to the entire board of directors. A copy of the report, and any discussion relating to it or the ORDER, shall be included in the minutes of the Board meeting. Nothing contained herein shall diminish the responsibility of the entire Board to ensure compliance with the provisions of this ORDER.

(b) For the purposes of this ORDER, an *outside director* is an individual who meets all of the following criteria:

- (i) Is not employed by the Bank or any of its affiliates other than as a director of the Bank or an affiliate;
- (ii) Does not own or control more than 5 percent of the voting stock of the Bank or its holding company;
- (iii) Is not indebted to the Bank or any of its affiliates in an amount greater than \$100,000;
- (iv) Is not related, by blood or marriage, to any director or principal shareholder of the Bank or any of its affiliates; and
- (v) Is a resident of, or engages in business in, the Bank's trade area.

[.9] 7. Within 60 days after the effective date of this ORDER, the Bank shall revise, adopt, and implement written lending and collection policies and procedures to provide effective guidance and control over the Bank's lending function. Such policies and their implementation shall be in a form and manner acceptable to the Regional Director, as determined at subsequent examinations, and shall include, at a minimum, all of the following:

- (a) A provision that deviations from the written lending policies and procedures require prior approval of the Board;
- (b) Standards setting forth appropriate limitations on concentrations of credit;
- (c) Standards under which unsecured loans may be granted;
- (d) A provision specifically outlining the collection procedures to be taken by the Bank when borrowers fail to make timely payments;
- (e) A provision outlining the documentation required on all purchased mortgage loans, to ensure proper control over original promissory notes; and
- (f) Procedures to be followed to properly control the payoff proceeds of purchased mortgage loans.

[.10] 8. After the effective date of this ORDER, the Bank, consistent with sound banking practices, shall correct all violations of laws and/or regulations set forth on pages 8.13 through 8.17 of the Report. In addition, the Bank shall ensure the Bank's future compliance with all applicable laws and regulations.

[.11] 9. Within 60 days after the effective date of this ORDER, the Bank, to the best of its ability using reasonable effort, shall ensure correction of the technical exceptions listed on pages 3c.1 and 3c.2 of the Report.

[.12] 10. After the effective date of this ORDER, the Bank shall provide to its shareholders a description of this ORDER, (1) in conjunction with the Bank's next shareholder communication, and also (2) in conjunction with its notice or proxy statement preceding the Bank's next shareholder meeting. The description shall fully describe the ORDER in all material respects. The description and any accompanying communication, statement, or notice shall also be sent to the FDIC, Registration and Disclosure Unit, Washington, D.C. 20429, for review at least 20 days prior to dissemination to shareholders. Any changes requested by the FDIC shall be made prior to dissemination of the description, communication, notice, or statement.

[.13] 11. Within 30 days after the end of each calendar quarter following the effective date of this ORDER, the Bank shall furnish written progress reports to the Re- ~~{{6-30-96 p.C-4191}}~~gional Director and the Commissioner detailing the form and manner of any actions to comply with this ORDER and the results thereof. Such reports may be discontinued when the corrections required by this ORDER have been accomplished and the Regional Director and the Commissioner have released the Bank in writing from making additional reports.

12. The effective date of this ORDER shall be 10 days after the date of its issuance. This ORDER shall be binding upon the Bank and all institution-affiliated parties of the Bank. The provisions of this ORDER shall remain effective and enforceable unless modified, terminated, suspended, or set aside by the FDIC.

This ORDER is issued pursuant to delegated authority.

Dated at Dallas, Texas, this 26th day of April, 1996.

