

FEDERAL DEPOSIT INSURANCE CORPORATION  
WASHINGTON, D.C.  
and  
TEXAS DEPARTMENT OF BANKING  
AUSTIN, TEXAS

|                                |   |                                 |
|--------------------------------|---|---------------------------------|
|                                | ) |                                 |
| In the Matter of               | ) | CONSENT ORDER                   |
|                                | ) |                                 |
| LONE STAR BANK                 | ) |                                 |
| HOUSTON, TEXAS                 | ) | FDIC-10-259b                    |
|                                | ) |                                 |
| (Insured State Nonmember Bank) | ) | COMMISSIONER ORDER No. 2010-025 |
|                                | ) |                                 |

The Federal Deposit Insurance Corporation ("FDIC") is the appropriate Federal banking agency for Lone Star Bank, Houston, Texas ("Bank"), under 12 U.S.C. § 1813(q).

The Texas Department of Banking ("Department") is the appropriate state banking agency for the Bank, under Texas Finance Code, Title 3, Subtitle A, §§ 31.001 et seq.

The Bank, by and through its duly elected and acting Board of Directors, has executed a "STIPULATION TO THE ISSUANCE OF A CONSENT ORDER" ("STIPULATION"), dated May 27, 2010, that is accepted by the FDIC and the Banking Commissioner of Texas ("Commissioner"). With the STIPULATION, the Bank has consented, without admitting or denying any charges of unsafe or unsound banking practices or violations of law or regulation, to the issuance of this CONSENT ORDER ("ORDER") by the FDIC and the State Commissioner.

Having determined that the requirements for issuance of an order under 12 U.S.C. § 1818(b) and Texas Finance Code §§ 35.002, have been satisfied, the FDIC and the Commissioner hereby order that:

## **MANAGEMENT PLAN**

1. (a) Within 60 days after the effective date of this ORDER, the Bank shall develop a written analysis and assessment of the Bank's immediate management and staffing needs along with plans to address any deficiencies ("Management Plan") for the purpose of providing qualified management for the Bank on a long-term basis. The Management Plan shall include, at a minimum:

- (1) Identification of both the type and number of officer positions needed to properly manage and supervise the affairs of the Bank;
- (2) Identification and establishment of such Bank committees as are needed to provide guidance and oversight to active management;
- (3) Evaluation of all Bank officers and loan staff members to determine whether these individuals possess the ability, experience and other qualifications required to perform present and anticipated duties, including adherence to established policies and practices, and restoration and maintenance of the Bank in a safe and sound condition; and
- (4) A plan to recruit and hire any additional or replacement personnel with the requisite ability, experience and other qualifications to fill those officer or staff member positions identified in the Management Plan. The qualifications of management personnel shall be evaluated on their ability to:
  - a) Comply with the requirement of the Order;

- 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, including improvement to asset quality, capital adequacy, earnings, management effectiveness, liquidity, and sensitivity to market risk.

(5) A provision that the Bank begin the recruitment process for a new president in the third quarter of 2010.

(b) The Management Plan shall be submitted to the Regional Director and the Commissioner for review and comment upon its completion. Within 30 days from the receipt of any comments from the Regional Director and the Commissioner, and after the adoption of any recommended changes, the Bank shall approve the Management Plan, and record its approval in the minutes of the Board of Directors' meeting. Thereafter, the Bank, its directors, officers, and employees shall implement and follow the Management Plan and/or any subsequent modifications.

(c) In the event the Regional Director and the Commissioner, after review of the Management Plan, at any time determines that it is necessary the Management Plan be modified or supplanted by a consultant, the Bank shall retain a consultant acceptable to the Regional Director and the Commissioner. Within 30 days after notice from Regional Director and the Commissioner, the bank shall engage a consultant to perform a written analysis and assessment of the Bank's management and staffing needs ("Management Study") to be used as the basis for a revised Management Plan. The scope of the Management Study shall include provisions 1(a)(1) through 1(a)(4) above. Within 90 days after notice, the Bank shall submit a revised Management Plan to the Regional Director and the Commissioner.

(d) The Bank shall provide the Regional Director and the Commissioner with a copy of the proposed engagement letter or contract with the consultant for review before it is executed.

The contract or engagement letter, at a minimum, should include:

- (1) A description of the work to be performed under the contract or engagement letter;
- (2) The responsibilities of the consultant;
- (3) An identification of the professional standards covering the work to be performed;
- (4) Identification of the specific procedures to be used when carrying out the work to be performed;
- (5) The qualifications of the employee(s) who are to perform the work;
- (6) The time frame for completion of the work;
- (7) Any restrictions on the use of the reported findings; and
- (8) A provision for unrestricted examiner access to work papers.

### **STRATEGIC PLAN AND BUDGET**

2. (a) Within 60 days after the effective date of this ORDER, the Bank shall revise its strategic plan and budget. The strategic plan and budget required by this paragraph shall contain an assessment of the Bank's current financial condition and market area, and a description of the operating assumptions that form the basis for major projected income and expense components. The written strategic plan and budget shall address, at a minimum:

- (1) Financial goals, including pro forma balance sheets and income statements for the years ending 2010, 2011, and 2012; and

(2) Plans to improve core earnings, maintain adequate capital, enhance the liquidity position, and reduce the reliance on non-core funding.

(b) The Bank shall submit the strategic plan and budget to the Regional Director and the Commissioner for review and comment. After consideration of all such comments, the Bank shall approve the plan, which approval shall be recorded in the minutes of the Bank's Board of Directors' meeting. Thereafter, the Bank shall implement and follow the strategic plan and budget.

(c) Within 30 days after the end of each calendar quarter following the effective date of this ORDER, the Bank's Board of Directors shall evaluate the Bank's performance in relation to the strategic plan and budget required by this paragraph and record the results of the evaluation, and any actions taken by the Bank, in the minutes of the Bank's Board of Directors' meeting at which such evaluation is undertaken.

(d) The strategic plan and budget required by this ORDER shall be revised and submitted to the Regional Director and the Commissioner for review and comment 30 days after the end of each calendar year for which this ORDER is in effect. Within 30 days after receipt of all such comments from the Regional Director and the Commissioner and after consideration of all such comments, the Bank shall approve the revised plan, which approval shall be recorded in the minutes of the Bank's Board of Directors' meeting. Thereafter, the Bank shall implement the revised plan.

### **CAPITAL PLAN**

3. (a) Within 60 days after the effective date of this ORDER, the Bank shall submit a written capital plan to the Regional Director and the Commissioner. The capital plan

shall require the Bank, after establishing an Allowance for Loan and Lease Losses, to achieve and maintain its Tier 1 Leverage Capital ratio equal to or greater than Nine (9) percent of the Bank's Average Total Assets; to achieve and maintain its Total Risk-Based Capital ratio equal to or greater than Thirteen (13) percent of the Bank's Total Risk Weighted Assets.

(b) After the Regional Director and the Commissioner respond to the capital plan, the Bank's Board of Directors shall adopt the capital plan, including any modifications or amendments requested by the Regional Director and the Commissioner. Thereafter, the Bank shall immediately initiate measures detailed in the capital plan, to the extent such measures have not previously been initiated, to effect compliance with the plan.

(c) Such increase in Tier 1 Capital and any increase in Tier 1 Capital necessary to meet the capital ratios required by this ORDER may be accomplished by:

- (1) The sale of securities in the form of common stock, or any other instruments that qualify as Tier 1 Capital; or
- (2) The direct contribution of cash subsequent to January 4, 2010, by the directors and/or shareholders of the Bank or by the Bank's holding company; or
- (3) Receipt of an income tax refund or the capitalization subsequent to January 4, 2010, of a bona fide tax refund certified as being accurate by a certified public accounting firm; or
- (4) Any other method approved by the Regional Director and the Commissioner.

(d) If any such capital ratios are less than required by the ORDER, as determined as of the date of any Report of Condition and Income or at an examination by the FDIC or the Department, the Bank shall, within 30 days after receipt of a written notice of the

capital deficiency from the Regional Director or the Commissioner, present to the Regional Director and the Commissioner a new capital plan to increase the Bank's Tier 1 Capital of the Bank or to take such other measures to bring all the capital ratios to the percentages required by this ORDER. After the Regional Director and the Commissioner respond to the new capital plan, the Bank's Board of Directors shall adopt the new capital plan, including any modifications or amendments requested by the Regional Director and the Commissioner.

(e) Thereafter, the Bank shall immediately initiate measures detailed in the plan, to the extent such measures have not previously been initiated, to increase its Tier 1 Capital by an amount sufficient to bring all the Bank's capital ratios to the percentages required by this ORDER.

(f) In addition, the capital plan must include a contingency plan in the event that the Bank has failed to maintain the minimum capital ratios required; failed to submit an acceptable capital plan as required by this subparagraph; or failed to implement or adhere to a capital plan to which the Supervisory Authorities have taken no written objection. Said contingency plan shall include a plan to sell or merge the Bank. The Bank shall implement the contingency plan upon written notice from the Supervisory authorities.

(g) 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 Bank's Board of Directors shall adopt and implement a plan for the sale of such additional securities, including 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 prepare offering materials fully describing the securities being offered, including an accurate description of the financial condition of the Bank and the circumstances giving rise to the offering, and any other

material disclosures necessary to comply with Federal securities laws and any applicable State law. Prior to the implementation of the plan, and in any event, not less than 20 days prior to the dissemination of such materials, the plan and any materials used in the sale of the securities shall be submitted to the FDIC, Accounting and Securities Disclosure Section, Washington, D.C. 20429, for review. 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 non-cumulative perpetual preferred stock, then all terms and conditions of the issue shall be presented to the Regional Director and the Commissioner for prior approval.

(h) 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 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.

(i) In addition, 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.

(j) For purposes of this ORDER, all terms relating to capital shall be calculated according to the methodology set forth in Part 325 of the FDIC's Rules and Regulations, 12 C.F.R. Part 325.

## **LOAN COMMITTEE AND LOAN REVIEW REQUIREMENTS**

4. (a) Within 30 days of the date of this ORDER, the Bank's board of directors shall establish a Board level loan committee with the responsibility of overseeing the Bank's credit function. At least 25 percent of the members of the committee shall be directors not employed in any capacity by the bank other than as director. The Board loan committee shall also be charged with reviewing and approving significant credit relationships in excess \$500,000 or loans that are experiencing significant deterioration including nonaccrual loans and restructured troubled debts in excess of \$250,000.

(b) The committee shall file a report with the Board of Directors at each Board meeting. This report shall include the following information:

- (1) overall quality of the loan portfolio;
- (2) identification, by type and amount, of each problem or delinquent loan;
- (3) identification of all loans not in conformance with the Bank's lending policy; and
- (4) A list of all loans approved by the Board loan committee.

(c) Within 60 days of the effective date of this Memorandum, the Bank, with Board approval, shall establish a loan review process to accurately and timely identify and categorize problem credits. The Bank shall ensure that all borrowing relationships of \$150,000 and above are reviewed initially and annually thereafter, problem loans are appropriately identified, and internal loan grades are accurate.

(d) The loan review function shall file a report with the Board in conjunction with each review which shall be performed not less frequently than quarterly, that includes, at a

minimum, the following information:

- (1) Summary information on the overall quality of the loan portfolio and comparative trend analysis on the reduction of classified assets;
- (2) The identification, by type and amount, of each problem loan; and
- (3) The identification of all loans not in conformance with the loan policy.

### **ALLOWANCE FOR LOAN AND LEASE LOSSES**

5. (a) Within 30 days after the effective date of this ORDER, the Bank shall ensure provisions to its Allowance for Loan and Lease Losses (“ALLL”) are calculated in accordance with generally accepted accounting standards and ALLL supervisory guidance. The Bank shall maintain a reasonable ALLL. Prior to the end of each calendar quarter, the Bank’s board of directors shall review the adequacy of the ALLL. Such reviews shall include, at a minimum, the Bank’s loan loss experience, an estimate of potential loss exposure in the portfolio, trends of delinquent and non-accrual loans and prevailing and prospective economic conditions. The minutes of the Bank’s Board of Directors’ meetings at which such reviews are undertaken shall include complete details of the reviews and the resulting recommended increases in the ALLL.

(b) Within 30 days after the effective date of this ORDER, the Bank shall ensure Consolidated Reports of Condition and Income filed with the FDIC contain a reasonable ALLL. The Bank must use Financial Accounting Standards Board Statements Numbers 5 and 114 for determining the Bank’s allowance for loan and lease losses reserve adequacy. Provisions for loan losses must be based on the inherent risk in the Bank’s loan portfolio. The directorate must document with written reasons any decision not to require provisions for loan losses in the

board minutes.

**CLASSIFIED ASSETS - PLAN FOR REDUCTION**

6. (a) Within 60 days after the effective date of this ORDER, the Bank shall submit a written plan to the Regional Director and the Commissioner to reduce the remaining assets classified Doubtful and Substandard as of January 4, 2010. The plan shall be based upon a written internal review that addresses each asset so classified with a balance of \$150,000 or greater and provide the following:

- (1) The name under which the asset is carried on the Bank's books;
- (2) Type of asset;
- (3) Actions to be taken in order to reduce the classified asset; and
- (4) Timeframes for accomplishing the proposed actions.

The internal review shall also, at a minimum:

- (1) Review the financial position of each such borrower, including the source of repayment, repayment ability, and alternate repayment sources; and
- (2) Evaluate the available collateral for each such credit, including possible actions to improve the Bank's collateral position.

In addition, the Bank's classified asset reduction plan shall contain a summary schedule detailing the projected reduction of total classified assets on a quarterly basis. Further, the plan shall contain a provision requiring the submission of monthly progress reports to the Bank's Board of Directors and a provision mandating a review by the Bank's Board of Directors.

(b) The Bank shall present the plan to the Regional Director and the Commissioner for review. Within 30 days after the Regional Director's and the Commissioner's

response, the plan, including any requested modifications or amendments shall be adopted by the Bank's Board of Directors which approval shall be recorded in the minutes of the meeting of the Bank's Board of Directors. The Bank shall then immediately initiate measures detailed in the plan to the extent such measures have not been initiated.

(c) For purposes of the plan, the reduction of adversely classified assets shall include adversely classified assets as of January 4, 2010, as well as any newly identified items. The plan shall be detailed using quarterly targets expressed as a percentage of the Bank's Tier 1 Capital plus the Allowance for Loan and Lease Losses and may be accomplished by:

- (1) Charge-off;
- (2) Collection;
- (3) Sufficient improvement in the quality of adversely classified assets so as to warrant removing any adverse classification, as determined by the FDIC or the Department; or
- (4) Increase in the Bank's Tier 1 Capital.

(d) While this ORDER is in effect, the Bank shall eliminate from its books, by charge-off or collection, all assets or portions of assets classified Loss as determined at any future examination conducted by the FDIC or the Department.

#### **CONCENTRATIONS – PLAN FOR REDUCTION**

7. (a) Within 60 days after the effective date of this ORDER, the Bank shall formulate and submit to the Regional Director and the Commissioner for review and comment a written plan to reduce commercial real estate and construction/development loan concentrations of credit identified in the Visitation Report as of January 4, 2010. Such plan shall prohibit any

additional advances that would increase the concentrations or create new concentrations, except where the advancement is pursuant to an existing loan agreement, and shall include, but not be limited to:

- (1) Dollar levels to which the Bank shall reduce each concentration;  
and
- (2) Provisions for the submission of monthly written progress reports to the Bank's Board of Directors for review and notation in minutes of the meetings of the Bank's Board of Directors.

(b) For purposes of the plan, "reduce" means to:

- (1) Charge-off;
- (2) Collect; or
- (3) Increase Tier 1 Capital.

(c) After the Regional Director and the Commissioner have responded to the plan, the Bank's Board of Directors shall adopt the plan as amended or modified by the Regional Director and the Commissioner. The plan shall be implemented immediately to the extent that the provisions of the plan are not already in effect at the Bank.

#### **RESTRICTION ON ADVANCES TO CLASSIFIED BORROWERS**

8. (a) While this ORDER is in effect, the Bank shall not extend, directly or indirectly, any additional credit to or for the benefit of any borrower whose existing credit has been classified Loss by the FDIC or the Department as a result of a Bank examination, either in whole or in part, and is uncollected, or to any borrower who is already obligated in any manner to the Bank on any extension of credit, including any portion thereof, that has been charged off

the books of the Bank and remains uncollected. The requirements of this paragraph shall not prohibit the Bank from renewing credit already extended to a borrower after full collection, in cash, of interest due from the borrower.

(b) While this ORDER is in effect, the Bank shall not extend, directly or indirectly, any additional credit to or for the benefit of any borrower whose extension of credit is classified Doubtful and/or Substandard by the FDIC or the Department as a result of any Bank examination, either in whole or in part, and is uncollected, unless the Bank's Board of Directors has signed a detailed written statement giving reasons why failure to extend such credit would be detrimental to the Bank's best interests. The statement shall be placed in the appropriate loan file and included in the minutes of the applicable Bank's Board of Directors' meeting.

### **INTEREST RATE RISK**

9. Within 60 days after the effective date of the ORDER, the Bank shall develop, adopt, and implement an interest rate risk policy and establish procedures that shall include, at a minimum:

- (1) Measures designed to control the nature and amount of interest rate risk the Bank takes including those that specify risk limits and defines lines of responsibilities and authority for managing risk;
- (2) A system for adequately identifying and measuring interest rate risk;
- (3) A system for monitoring and reporting risk exposures; and
- (4) A system of internal controls, review, and audit to ensure the integrity of the overall risk management process.

### **CORRECTION OF VIOLATIONS**

10. (a) Within 30 days after the effective date of this ORDER, the Bank shall eliminate and/or correct all violations of law and regulation noted in the Visitation.

(b) Within 30 days after the effective date of this ORDER, the Bank shall implement procedures to ensure future compliance with all applicable laws and regulations.

(c) Within 30 days after the effective date of this ORDER, the Bank shall address any contraventions of policy noted in the Visitation.

### **DIVIDEND RESTRICTION**

11. As of the effective date of this ORDER, the Bank shall not declare or pay any cash dividend without the prior written consent of the Regional Director and the Commissioner.

### **SHAREHOLDER NOTIFICATION**

12. After the effective date of this ORDER, the Bank shall send a copy of this ORDER, or otherwise furnish a description of this ORDER, to its shareholders (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 be sent to the FDIC Accounting and Securities Disclosure Section, 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.

## **PROGRESS REPORTS**

13. Within 30 days after the end of the first calendar quarter following the effective date of this ORDER, and within 30 days after the end of each successive calendar quarter, the Bank shall furnish written progress reports to the Regional Director and the Commissioner detailing the form and manner of any actions taken to secure compliance with this ORDER and the results thereof. Such reports may be discontinued when the corrections required by the ORDER have been accomplished and the Regional Director has released the Bank in writing from making additional reports.

The provisions of this ORDER shall not bar, stop, or otherwise prevent the FDIC, the State, or any other federal or state agency or department from taking any other action against the Bank or any of the Bank's current or former institution-affiliated parties.

This ORDER shall be effective on the date of issuance.

The provisions of this ORDER shall be binding upon the Bank, its institution-affiliated parties, and any successors and assigns thereof.

The provisions of this ORDER shall remain effective and enforceable except to the extent that and until such time as any provision has been modified, terminated, suspended, or set aside by the FDIC and the Commissioner.

Issued pursuant to delegated authority this 10<sup>th</sup> day of June, 2010.

/s/  
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Kristie K. Elmquist  
Acting Regional Director  
Dallas Region  
Division of Supervision and Consumer Protection  
Federal Deposit Insurance Corporation

/s/  
\_\_\_\_\_  
Charles G. Cooper  
Banking Commissioner  
Texas Department of Banking