

{{1-31-95 p.C-1766}}

¶10,406] In the Matter of Bay Port State Bank, Bay Port, Michigan, Docket No. FDIC-91-403b (12-12-91).

Bank to cease and desist from such unsafe or unsound practices as following hazardous lending and lax collection practices; operating with inadequate capital; operating in violation of applicable laws or regulations, including Regulation O; operating with excessive volumes of adversely classified assets; operating with inadequate allowance for loan and lease losses; engaging in securities transactions without adequate controls, policies or supervision by board of directors; failing to provide adequate supervision over the Bank's affairs; engaging in practices which produce inadequate operating income; operating with inadequate routine and controls policies; and operating without an adequate audit program. *(This order was terminated by order of the FDIC dated 11-22-94; see ¶ 15,938.)*

- [.1] Management—Qualifications—Review
- [.2] Management—Management Plan—Minimum Requirements
- [.3] Assets—Adversely Classified—Eliminate/Reduce
- [.4] Capital—Tier 1 Capital—Increase/Maintain—Methods
- [.5] Allowance for Loan and Lease Losses—Establish/Maintain
- [.6] Dividends—Restricted
- [.7] Loans—Risk Position—Reduce—Written Plan Required
- [.8] Loans—Special Mention—Correct Deficiencies
- [.9] Technical Exceptions—Eliminate/Correct
- [.10] Loans—Extensions of Credit—Existing Borrowers—Curtail
- [.11] Loan Policy—Written Revision—Minimum Requirements
- [.12] Asset/Liability Management—Written Policy—Minimum Requirements
- [.13] Investment Policy—Securities Policy—Minimum Requirements
- [.14] Profit Plan—Minimum Requirements
- [.15] Violations of Law—Eliminate/Correct
- [.16] Audit—Written Policy Required
- [.17] Assets—Total Assets—Limitation on Increase
- [.18] Bank Operations—Internal Routine and Controls—Written Policy Required
- [.19] Shareholders—Disclosure—Cease and Desist Order
- [.20] Board of Directors—Committee to Review Compliance with Cease and Desist Order
- [.21] Compliance Reports—Frequency

In the Matter of

**BAY PORT STATE BANK
BAY PORT, MICHIGAN
(Insured State Nonmember Bank)
ORDER TO CEASE AND DESIST**

Bay Port State Bank, Bay Port, Michigan ("Bank"), having been advised of its right to a NOTICE OF CHARGES AND OF HEARING detailing the unsafe or unsound banking practices and violations of law or regulation alleged to have been committed by the Bank, and of its right to a hearing on the charges under section 8(b) of the Federal Deposit Insurance Act ("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 December 12, 1991, whereby, solely for the purpose of this proceeding and without admitting or denying the charges of unsafe or unsound banking practices and violations of law or regulation, 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 it had reason to believe that the Bank had engaged in unsafe or unsound banking practices and had violated laws or regulation. The FDIC, therefore, accepted the CONSENT AGREEMENT and issued the following:

ORDER TO CEASE AND DESIST

IT IS HEREBY ORDERED, that the Bank, its institution-affiliated parties, as that term is defined in section 3(u) of the Act, 12 U.S.C. § 1813(u), and its successors and assigns, cease and desist from the following unsafe or unsound banking practices and violations of law and regulation:

- A. Engaging in hazardous lending and lax collection practices, as evidenced by an excessive volume of adversely classified loans;
- B. Operating with an inadequate level of capital protection for the kind and quality of assets held;
- C. Violating the more than the normal risk of repayment, unfavorable features and preferential terms and conditions prohibitions of section 215.4(a) of Regulation O of the Board of Governors of the Federal Reserve System, 12 C.F.R. § 215.4(a); the charge-off requirements for overdrafts of section 239(1) of the Michigan Banking Code of 1969 MICH. COMP. LAWS ANN. § 487.539 (West 1987); and the good faith terms and circumstances requirements of section 23B of the Federal Reserve Act, 12 U.S.C. § 371c-1(a)(1)(A);
- D. Operating with an excessive level of adversely classified and Special Mention assets;
- E. Operating with an inadequate allowance for loans and lease losses for the volume, kind, and quality of loans and leases held;
- F. Engaging in securities transactions without adequate controls, policies, and procedures, and without adequate supervision by the Bank's board of directors;
- G. Operating with management whose policies and practices are detrimental to the Bank and which jeopardize the safety of its deposits;
- H. Operating with a board of directors which has failed to provide adequate supervision over and direction to the management of the Bank;
- I. Engaging in practices which have resulted in an inadequate level of earnings;
- J. Operating with inadequate internal routines and controls; and
- K. Operating with an inadequate audit program.

IT IS FURTHER ORDERED, that the Bank, its institution-affiliated parties, and its successors and assigns, take affirmative action as follows:

[.1]1. (a) Within 60 days from the effective date of this ORDER, the Bank shall have and retain qualified management. At a minimum, such management shall include a chief executive officer with proven ability in managing a bank of comparable size and experience in upgrading a lowquality loan portfolio. Such person shall be provided the necessary written authority to implement the provisions of this ORDER. The qualifications of management shall be assessed on its ability to:

- (i) comply with the requirements of this ORDER;
- (ii) operate the Bank in a safe and sound manner;
- (iii) comply with applicable laws and regulations; and
- (iv) restore all aspects of the Bank to a safe and sound condition, including asset quality, capital adequacy, earnings, management effectiveness, and liquidity.

(b) During the life of this ORDER, the Bank shall notify the Regional Director of the Chicago Regional Office of the FDIC ("Regional Director") in writing of any changes in any of the Bank's management. For purposes of this ORDER, "management" is defined as members of the board of directors and "senior executive officers," as that term is defined in section 32 of the Act ("section 32"), 12 U.S.C. § 1831(i), and section 303.14 of the FDIC Rules and Regulations ("section 303.14"), 12 C.F.R. § 303.14. Prior to the addition of any individual to the board of directors or the employment of any individual as a senior executive officer, the Bank shall comply with the re- [{{2-29-92 p.C-1768}}](#)quirements of section 32 and section 303.14.

[.2] 2. (a) Within 120 days from the effective date of this ORDER, the Bank shall develop a written analysis and assessment of the Bank's management and staffing needs ("Management Plan") for the purpose of providing qualified management for the Bank. The Management Plan shall include, at a minimum:

- (i) identification of both the type and number of officer positions needed to properly manage and supervise the affairs of the Bank;
- (ii) identification and establishment of such Bank committees as are needed to provide guidance and oversight to active management;
- (iii) evaluation of all Bank officers and staff members to determine whether these individuals possess the ability, experience and other qualifications required to perform present and anticipated duties, including adherence to the Bank's established policies and practices, and restoration and maintenance of the Bank in a safe and sound condition; and

(iv) 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 by this paragraph of the ORDER.

(b) The Management Plan and any subsequent modification thereto shall be submitted to the Regional Director for review and comment. Within 30 days from the receipt of any comment from the Regional Director and after consideration of such comment, the Bank shall approve the Management Plan or any subsequent modifications, which approval shall be recorded in the minutes of the board of directors' meeting. Thereafter, the Bank shall implement and follow the Management Plan and any subsequent modification.

(c) The written management plan shall also include the requirement that the board of directors of the Bank, or a committee thereof consisting of not less than 2 individuals who are independent with respect to the Bank, provide supervision over lending, investment and operating policies of the Bank sufficient to ensure that the Bank complies with the provisions of this ORDER. For purposes of this ORDER, a person who is an independent director shall be any individual (a) who is not an officer of the Bank; (b) who does not own more than 5 percent of the outstanding shares of the Bank; (c) who is not related by blood or marriage to an officer or director of the Bank or to any shareholder owning more than 5 percent of the Bank's outstanding shares, and who does not otherwise share a common financial interest with such officer, director or shareholder; and (d) who is not indebted to the Bank directly or indirectly through blood relation, marriage or common financial interest, including the indebtedness of any entity in which the individual has a substantial financial interest in an amount exceeding 10 percent of the Bank's total Tier 1 capital and allowance for loan and lease losses. The addition of any new Bank directors if necessary to comply with this paragraph may be accomplished, to the extent permissible by state statute or the Bank's bylaws, by means of appointment or by election at a regular or special meeting of the Bank's shareholders.

(d) During the life of this ORDER, the Bank's board of directors shall meet at least monthly. The board shall prepare in advance and shall follow a detailed written agenda at each meeting, which shall include consideration of actions of any committees. Nothing in the foregoing sentence shall preclude the board from considering matters other than those contained in the agenda. Detailed written minutes of all meetings shall be maintained and recorded on a timely basis.

[.3] 3. As of the effective date of this ORDER, the Bank shall eliminate from its books, by charge-off or collection, all assets or portions of assets classified "Loss" as of June 17, 1991, that have not been previously collected or charged off. Elimination or reduction of these assets with the proceeds of other Bank extensions of credit is not considered collection for the purpose of this paragraph.

[.4] 4. (a) Within 90 days from the effective date of this ORDER, the Bank shall increase its Tier 1 capital by not less than \$225,000.

(b) Within 30 days of each March 31, June 30, September 30, and December 31 following the date of required compliance with paragraph 4(a) of this ORDER, the [{{2-29-92 p.C-1769}}](#) Bank shall determine from its Report of Condition and Income its level of Tier 1 capital as a percentage of its total assets ("capital ratio") for that calendar quarter. If the capital ratio is less than 7 percent, the Bank shall, within 60 days of the date of the required determination, increase its capital ratio to not less than 7 percent calculated as of the end of that preceding quarterly period. For purposes of this ORDER, Tier 1 capital, the capital ratio, and total assets shall be calculated in accordance with Part 325 of the FDIC's Rules and Regulations ("Part 325"), 12 C.F.R. Part 325 and all appendices thereto.

(c) Any such increase in Tier 1 capital may be accomplished by the following:

- (i) The sale of common stock and noncumulative perpetual preferred stock constituting Tier 1 capital under Part 325; or
- (ii) The elimination of all or part of the assets classified "Loss" as of June 17, 1991 without loss or liability to the Bank, provided any such collection on a partially charged-off asset shall first be applied to that portion of the asset which was not charged off pursuant to this ORDER; or
- (iii) The collection in cash of assets previously charged-off; or
- (iv) The direct contribution of cash by the directors and/or the shareholders of the Bank or its holding company; or
- (v) Any other means acceptable to the Regional Director; or
- (vi) Any combination of the above means.

(d) If all or part of the increase in capital required by this paragraph is to be accomplished by the sale of

new securities, the board of directors of the Bank shall adopt and implement a plan for the sale of such additional securities, including the voting of any shares owned or proxies held by or controlled by them in favor of said plan. Should the implementation of the plan involve public distribution of the Bank securities, including a distribution limited only to the Bank's existing shareholders, the Bank shall prepare detailed 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 the Federal securities laws. Prior to the implementation for the plan and, in any event, not less than 20 days prior to the dissemination of such materials, the materials used in the sale of the securities shall be submitted to the FDIC at Washington, D.C., for its review. Any changes requested to be made in the materials by the FDIC shall be made prior to their dissemination.

(e) In complying with the provisions of paragraph 4(d) of this ORDER, the Bank shall provide to any subscriber and/or purchaser of Bank securities written notice of any planned or existing development or other changes which are materially different from the information reflected in any offering materials used in connection with the sale of Bank securities. The written notice required by this paragraph shall be furnished within 10 calendar days of the date any material development or change was planned or occurred, whichever is earlier, and shall be furnished to every purchaser and/or subscriber of the Bank's original offering materials.

(f) The capital ratio analysis required by this paragraph shall not negate the responsibility of the Bank and its board of directors for maintaining throughout the year an adequate level of capital protection for the kind, quality and degree of market depreciation of assets held by the Bank.

[.5] 5. (a) Within 30 days from the effective date of this ORDER, the Bank shall replenish its allowance for loan and lease losses ("ALLL") in the amount of \$75,000.

(b) Within 30 days from the effective date of this ORDER, the Bank shall make an additional provision for loan and lease losses which, after review and consideration by the board of directors, reflects the potential for further losses in the remaining loans or leases classified "Substandard" and all other loans and leases in its portfolio. In making this determination, the board of directors shall maintain an adequate allowance in accordance with the requirements of the Federal Financial Institutions Examination Council's ("FFIEC's") Instructions for the Reports of Condition and Income.

[\[2-29-92 p.C-1770\]](#)(c) Within 30 days from the effective date of this ORDER, Reports of Condition and Income required by the FDIC and filed by the Bank subsequent to June 17, 1991, shall be amended and refiled if they do not reflect a provision for loan and lease losses and an ALLL which are adequate considering the condition of the Bank's loan portfolio, and which, at a minimum, incorporate the adjustments required by the above paragraphs of this ORDER.

(d) Prior to submission or publication of all Reports of Condition and Income required by the FDIC after the effective date of this ORDER, the board of directors of the Bank shall review the adequacy of the Bank's ALLL and accurately report the same. The minutes of the board meeting at which such review is undertaken shall indicate the findings of the review, the amount of increase in the reserve recommended, if any, and the basis for determination of the amount of reserve provided.

(e) While this ORDER is in effect, the Bank shall submit to the Regional Director the analysis supporting the determination of the adequacy of its ALLL. These submissions shall be made in conjunction with the progress reports required by paragraph 21 of this ORDER.

(f) Provisions to the ALLL required by this paragraph shall be made prior to any determinations of Tier 1 capital calculations required by paragraph 4 of this ORDER.

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

[.7] 7. (a) Within 60 days from the effective date of this ORDER, the Bank shall adopt and implement a written plan to reduce the Bank's risk position in each asset in excess of \$50,000 which is classified "Substandard" in the FDIC's Report of Examination of June 17, 1991 ("Report"). A copy of the written plan shall be submitted to the Regional Director. In developing such plan, the Bank shall, at a minimum:

- (i) review the financial position of each such borrower, including source of repayment, repayment ability, and alternative repayment sources; and
- (ii) evaluate the available collateral for each such credit, including possible actions to improve the Bank's collateral position.

(b) Such plan shall include, but not be limited to, the following:

- (i) dollar levels to which the Bank shall reduce each asset within 6 and 12 months from the effective date of this ORDER; and

(ii) provisions for the submission of monthly written progress reports to the Bank's board of directors for review and notation in the minutes of the meetings of the board of directors.

(c) As used in this paragraph, "reduce" means to (1) collect; (2) charge off; or (3) improve the quality of such assets so as to warrant removal of any adverse classification by the FDIC.

(d) Within 30 days from receipt of any comment from the Regional Director of any written plan required by this ORDER to be submitted for review and comment, and after consideration of all such comments, the Bank shall approve and implement the plan. The approval shall be recorded in the minutes of a board of directors' meeting.

[.8] 8. Within 60 days from the effective date of this ORDER, the Bank shall correct all deficiencies in the loans listed for "Special Mention" in the Report.

[.9] 9. Within 60 days of the effective date of this ORDER, the Bank shall correct the technical exceptions listed in the Report. Excluded from this requirement are the following technical exceptions: financial and/ or operating statements for John Baranic, Jr., Gehring Bros.; Paul Kreh; and James and Betty Miller. The Bank shall take all prudent banking measures to correct the excluded technical exceptions and shall document the measures taken in the minutes of the meetings of the board of directors.

[.10] 10. Effective the date of this ORDER, the Bank shall not extend, directly or indirectly, any additional credit to, or for the benefit of, any borrower who has a loan or other extensions of credit with the Bank that has been charged off or classified, in whole or in part, "Loss", "Doubtful", or "Substandard", and is uncollected, unless a majority of the Bank's board of directors first (1) determines that such advance is in the best interest of the Bank, (2) determines that the Bank has satisfied the requirements set out in paragraph 7 of this ORDER as to such borrower, and (3) approves such advance. A written record of the board of directors' determination and approval of any advance under the terms of this paragraph shall be maintained in the credit file of any affected borrower as well as the minutes of the board of directors. The requirements of this paragraph do not prohibit the Bank from renewing any credit already extended to the borrower.

[.11] 11. (a) Within 60 days from the effective date of this ORDER, and annually thereafter, the board of directors of the Bank shall review the Bank's loan policy and procedures for adequacy and, based upon this review, shall make all appropriate revisions to the policy necessary to strengthen lending procedures and abate additional loan deterioration. The revised written loan policy and any subsequent modifications shall be submitted to the Regional Director for review and comment.

(b) Within 30 days from the receipt of any comments from the Regional Director and after the adoption of any recommended changes, the board of directors shall approve and implement the written loan policy and any subsequent modification thereto. The approvals shall be recorded in the minutes of a board of directors' meeting.

[.12] 12. (a) Within 60 days from the effective date of this ORDER, the Bank shall formulate and submit to the Regional Director for review and comment a written plan addressing liquidity, the Bank's relationship of volatile liabilities to temporary investments, rate sensitivity objectives and asset/liability management policy. Annually thereafter during the life of this ORDER, the Bank shall review this plan for adequacy and, based upon such review, shall make appropriate revisions in the plan that are necessary to strengthen funds management procedures and maintain adequate provisions to meet the Bank's liquidity needs.

(b) Within 30 days from the receipt of all such comments from the Regional Director, and after consideration of all such comments, the Bank shall approve and implement the plan. The approval shall be recorded in the minutes of a board of directors' meeting.

[.13] 13. (a) Within 60 days from the effective date of this ORDER, the Bank shall develop a written policy concerning investment in securities, which shall include:

- (i) goals and strategies for improving the Bank's investment in securities;
- (ii) controls and procedures for the Bank's investment in securities, including trading account activity, which, among other things, shall identify sources of funding for trading account activity and specify individuals authorized to engage in any securities trading and any limitations on their authority to engage in securities trading; and
- (iii) accounting guidelines for all purchases and sales of securities, including trade date

accounting, consistent with the FFIEC's for the Report of Condition and Income.

(b) The policy and any subsequent modification thereto shall be submitted to the Regional Director for review and comment. No more than 30 days from the receipt of any comment from the Regional Director, the board of directors shall approve the policy and any subsequent modification thereto which approval shall be recorded in the minutes of the board. Thereafter, the Bank, its directors, officers and employees shall follow the policy and/or any subsequent modification thereto and shall accurately report all trading account activities in all Reports of Condition and Income.

(c) (i) No more than 60 days from the effective date of this ORDER, the Bank's board of directors shall in writing either authorize or prohibit the Bank from engaging in securities trading, record such authorization or prohibition in the minutes of the Bank's board of directors, and provide a copy of said minutes to the Regional Director. If the Bank's board of directors prohibits the Bank from engaging in securities trading, the Bank need not develop written policies concerning securities trading as part of the written policy concerning investment in securities required by paragraph 13(a), but shall state in the written policy concerning investment in securities that the Bank will not engage in securities trading.

(ii) If while this ORDER is in effect the Bank's board of directors authorizes the Bank to engage in securities trading, at least 30 days prior to engaging in securities trading the Bank shall:

- (1) Provide the Regional Director with notice of its intent to engage in securities trading;
- (2) Revise the Bank's written policy concerning investment in securities to include the information regarding securities trading required by paragraph 13(a) herein; and

(3) Comply with paragraph 13(b).

[.14] 14. (a) Within 90 days from the effective date of this ORDER, the Bank shall formulate and submit to the Regional Director for review and comment a written profit plan and a realistic, comprehensive budget for all categories of income and expense for calendar year 1992. The plan required by this paragraph shall contain formal goals and strategies, consistent with sound banking practices, to reduce discretionary expenses and to improve the Bank's overall earnings and shall contain a description of the operating assumptions that form the basis for major projected income and expense components.

(b) The written profit plan shall address, at a minimum, the following:

- (i) identification of the major areas in, and means by, which the board of directors will seek to improve the Bank's operating performance;
- (ii) realistic and comprehensive budgets;
- (iii) a budget review process to monitor the income and expenses of the Bank to compare actual figures with budgetary projections; and
- (iv) a description of the operating assumptions that form the basis for, and adequately support, major projected income and expense components.

(c) Prior to the end of each calendar quarter, the Bank's board of directors shall evaluate the Bank's actual performance in relation to the 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 board of directors' meeting at which such evaluation is undertaken.

[.15] 15. Within 30 days from the effective date of this ORDER, the Bank shall undertake all prudent banking measures to eliminate and/or correct all violations of law or regulation listed on pages 6 of the Report. In addition, the Bank shall implement procedures to ensure future compliance with all applicable laws and regulations.

[.16] 16. (a) Within 90 days from the effective date of this ORDER, the Bank's board of directors shall formulate and submit to the Regional Director for review and comment a revised written audit policy. The Bank shall thereafter implement and enforce an effective system of internal and external audits. The internal control officer or auditor shall make written quarterly reports of audit findings directly to the Bank's board of directors. The minutes of the meetings of the board of directors shall reflect consideration of these reports and describe any action taken as a result thereof.

(b) Within 30 days from the receipt of any comment from the Regional Director, and after consideration of all such comments, the Bank shall continue to implement this policy. The implementation of any such comments and changes should be recorded in the minutes of the board of directors' meeting.

(c) During the life of this ORDER, the Bank shall forward copies of any external audit reports required by this paragraph to the Regional Director within 10 days from the Bank's receipt of such reports.

[.17] 17. During the life of this ORDER, the Bank shall not increase its total assets by more than 2 percent during any consecutive three-month period without providing, at least 30 days prior to its implementation, a growth plan to the Regional Director. Such growth plan shall include the funding source to support the projected growth, as well as the anticipated use of funds. This growth plan shall not be implemented without the prior written consent of the Regional Director. In no event shall the Bank increase its total assets by more than 6 percent annually. For the purpose of this paragraph, "total assets" shall be defined as in the FFIEC's Instructions for the Reports of Condition and Income.

[.18] 18. Within 60 days from the effective date of this ORDER, the Bank shall correct the deficiencies in internal routines and controls which are listed on page 6-c of the Report. Additionally, policies and procedures shall be established to prevent the recurrence of any deficiency so noted.

[.19] 19. Following the effective date of [9-30-92 p.C-1773](#) this ORDER, the Bank shall send to its shareholders or otherwise furnish a description of this ORDER: (1) in conjunction with the Bank's next shareholder communication; and (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, notice, or statement shall be sent to the FDIC in Washington, D.C. for review at least 20 days prior to dissemination to shareholders. Any changes requested to be made by the FDIC shall be made prior to dissemination of the description, communication, notice, or statement.

[.20] 20. Within 30 days from the effective date of this ORDER, the Bank shall establish a compliance committee comprised of at least 3 directors who are not officers of the Bank. The committee shall monitor compliance with this ORDER, and, within 30 days from the effective date of this ORDER, and every 60 days thereafter, shall submit to the board of directors for consideration at its regular monthly meeting a written report detailing the Bank's compliance with this ORDER. The compliance report shall be incorporated in the minutes of the board of directors' meeting. Establishment of this committee does not in any way diminish the responsibility of the entire board of directors for ensuring that compliance with the provisions of this ORDER is achieved.

[.21] 21. Within 30 days of the end of each calendar quarter following the effective date of this ORDER, the Bank shall furnish to the Regional Director written progress reports signed by each member of the Bank's board of directors, detailing the actions taken to secure compliance with the ORDER and the results thereof. Such reports may be discontinued when the corrections required by this ORDER have been accomplished and the Regional Director has, in writing, released the Bank from making further reports.

The effective date of this ORDER shall be 10 days after its issuance by the FDIC.

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 provisions of this ORDER shall have been modified, terminated, suspended, or set aside by the FDIC.

Dated: December 12, 1991.

Pursuant to delegated authority.