

FEDERAL DEPOSIT INSURANCE CORPORATION
WASHINGTON, D.C.

and

TEXAS DEPARTMENT OF BANKING
AUSTIN, TEXAS

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In the Matter of	)	
	)	
	)	ORDER TO CEASE AND DESIST
	)	
WALLIS STATE BANK	)	
WALLIS, TEXAS	)	FDIC-07-201b
	)	
	)	STATE NUMBER 2007-046
	)	
(INSURED STATE NONMEMBER BANK)	)	
_____	)	

The Wallis State Bank, Wallis, Texas (“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 laws 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)(1) of the Federal Deposit Insurance Act (“Act”), 12 U.S.C. § 1818(b)(1), 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”) and a representative of the Texas Department of Banking (“State”), dated February 21, 2008, whereby, solely for the purpose of this proceeding and without admitting or denying the alleged charges of unsafe or unsound banking practices and violations of laws or regulations, the

Bank consented to the issuance of an ORDER TO CEASE AND DESIST (“ORDER”) by the FDIC and the State.

The FDIC and the State considered the matter and determined that they had reason to believe that the Bank had engaged in unsafe or unsound banking practices and had committed violations of laws or regulations. The FDIC and the State, therefore, accepted the CONSENT AGREEMENT and issued the following:

ORDER TO CEASE AND DESIST

IT IS HEREBY ORDERED that the Bank, its directors, officers, employees, agents, and other 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 laws or regulations:

(a) Operating the Bank in violation of the Currency and Foreign Transactions Reporting Act (31 U.S.C. § 5311 *et seq.*) (the Bank Secrecy Act) (“BSA”), the rules and regulations implementing the BSA issued by the U. S. Department of the Treasury (31 C.F.R. Part 103) (“Financial Recordkeeping”), and the FDIC’s BSA Rules and Procedures Regulations, 12 C.F.R. Part 326; and the FDIC’s Suspicious Activity Reports (“SARs”) regulations, 12 C.F.R. Part 353 (all the rules referred to in this paragraph are referred to hereinafter, collectively, as “BSA Rules”);

(b) Operating the Bank without adequate supervision and direction by the Bank’s board of directors and senior management of the Bank to prevent unsafe and unsound

banking practices and violations of Federal and State laws or regulations and to ensure compliance with the BSA Rules;

(c) Operating the Bank with an ineffective BSA/Anti-Money Laundering (“AML”) Compliance Policy;

(d) Operating the Bank with an ineffective system of internal controls to ensure compliance with the BSA Rules;

(e) Operating the Bank with an ineffective BSA/AML training program to ensure compliance with the BSA Rules;

(f) Operating the Bank with an ineffective Customer Identification Program (“CIP”) for accounts for persons other than individuals;

(g) Operating the Bank with an ineffective Customer Due Diligence Program (“CDD”) to ensure compliance with the BSA Rules;

(h) Operating the Bank without an effective system of independent testing to ensure compliance with the BSA Rules;

(i) Operating the Bank with an ineffective audit policy to ensure compliance with the BSA Rules; and

(j) Engaging in hazardous lending practices, including, but not limited to:

(1) Poor credit administration practices.

(2) Failure to obtain proper loan documentation prior to funding loans.

(3) Failure to maintain current and complete financial information subsequent to funding loans.

(4) Renewing or extending credit without adequate and appropriate supporting documentation.

- (5) Operating the Bank without a comprehensive loan monitoring system.

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

1. (a) Within 60 days after the effective date of this ORDER, the Bank shall amend its written BSA/AML policy to address all BSA recommendations detailed in the FDIC's May 21, 2007 safety and soundness Report of Examination ("ROE") and amend the written BSA/AML Compliance Program ("BSA Compliance Program") as necessary to comply with the BSA Rules.

(b) At a minimum, the Compliance Program, as appropriate for the Bank's size, complexity, and risk profile, shall:

- (i) Establish ongoing CDD procedures;
- (ii) Expand the money service business ("MSB") account guidelines as recommended in the ROE which includes applying uniform minimum account procedures and, as necessary, additional due diligence procedures for higher-risk MSB accounts, with reference to the provisions of the FFIEC Bank Secrecy Act/Anti-Money Laundering Manual (revised August 24, 2007), which incorporates the principles of the April 26, 2005 *Interagency Interpretive Guidance on Providing Banking Services to Money Services Business Operating in the United States* issued by the Financial Crimes Enforcement Network and all Federal Banking Agencies;

- (iii) Establish policies and procedures relating to privately-owned ATMs, professional service providers and trade financing activities;
- (iv) Provide for the ongoing review of the Kite Suspect List;
- (v) Provide for an effective system of internal controls to ensure compliance with the BSA Rules; and
- (vi) Provide for the continued administration of the BSA Compliance Program to ensure and monitor ongoing compliance with the BSA Rules.

(c) The development and maintenance of policies and procedures with respect to wire transfer recordkeeping, including requirements for complete information on beneficiaries and senders, as required by 31 C.F.R. § 103.33.

(d) Upon completion, the BSA Compliance Program shall be submitted to the Regional Director, FDIC, Dallas Regional Office (“Regional Director”), and the Texas Banking Commissioner (“Commissioner”) for review and comment. Any changes requested to the BSA Compliance Program by the Regional Director or the Commissioner shall be made within 30 days from the receipt of all such comments from the Regional Director and the Commissioner. After revising the BSA Compliance Program as necessary and after considering comments received from the Regional Director and the Commissioner, the Bank’s board of directors shall adopt the Compliance Program. Such adoption shall be recorded in the minutes of the Bank’s board of directors’ meeting. The BSA Compliance Program shall be implemented immediately upon adoption by the Bank’s board of directors.

2. (a) Within 60 days after the effective date of this ORDER, the Bank shall identify the knowledge of the BSA Rules each employee shall possess to perform his or her assigned job functions. For each employee that the Bank has determined must have knowledge of the BSA Rules, a comprehensive review will be performed to determine their current BSA knowledge level. The Bank will then develop a timeline to address any identified areas of weaknesses.

(b) Bank personnel shall be evaluated to determine whether these individuals possess the ability, experience, training and other necessary qualifications required to perform present and anticipated duties in all areas related to the BSA Rules, including adherence to the Bank's BSA Compliance Program, the requirements of the BSA Rules, and the provisions of this ORDER.

(c) The review shall be conducted by a qualified party with the requisite ability to perform such an analysis, and a written report shall be presented to the Bank's board of directors. A copy of the written report shall be submitted to the Regional Director and the Commissioner for review and comment.

(d) After receipt of the comments of the Regional Director and the Commissioner, the Bank shall incorporate results and recommendations from the written report into its BSA Compliance Program within 30 days from the receipt of all such comments from the Regional Director and the Commissioner.

3. (a) The Bank shall provide an effective training program for management and staff on all relevant aspects of laws, regulations, and Bank policies and procedures relating to the BSA compliance ("Training Program"). This training shall ensure that all appropriate personnel are aware of, and can comply with, the requirements of the BSA including the currency and

monetary instruments reporting requirements and the reporting requirements associated with Suspicious Activity Reports (“SARs”). The Training Program shall also cover:

- (i) the Bank’s BSA/AML policies and procedures, as well as new rules, regulations, and requirements as they arise; and
- (ii) a requirement that the Bank’s board of directors will fully document the training of all appropriate employees, including the designated BSA compliance officer.

(b) The Bank shall also identify the method of training and source of training materials. The initial training shall be completed within 120 days after the effective date of this ORDER. Thereafter, the Bank shall conduct additional training on a regular basis, but not less than annually.

(c) Employees receiving the initial and subsequent training shall include, but are not limited to, all current or new tellers, new accounts personnel, lending personnel, bookkeeping personnel, wire transfer personnel, senior management and the Bank’s board of directors.

4. (a) Within 30 days after the effective date of this ORDER, the Bank shall develop a policy that specifies and documents the duties and responsibilities of a qualified individual, or individuals, who will function on a daily basis as the designated BSA Officer. The BSA Officer will be charged with coordinating and monitoring the day-to-day compliance with the BSA Rules.

- (b) The BSA Officer shall:
 - (i) have sufficient executive authority to establish BSA compliance procedures, including procedures to monitor ongoing compliance with the BSA;
 - (ii) be responsible for determining the adequacy of the Bank's BSA/AML staffing, given its size and risk profile (based upon the Risk Assessment) and for supervising such staff;
 - (iii) report directly to the Bank's board of directors and/or the board of directors' Compliance Committee;
 - (iv) report to the Bank's Audit Committee on a regular basis, but not less than quarterly, with respect to BSA/AML matters; and
 - (v) be responsible for assuring the proper and timely filing of Currency Transaction Reports, SARs, and any other BSA required reports.

5. (a) Within 180 days after the effective date of this ORDER, the Bank shall establish independent testing programs for compliance with the BSA and Office of Foreign Assets Control ("OFAC") provisions, to be performed on no less than an annual basis. The scope of the testing procedures to be performed and testing results shall be documented in writing and approved by the Bank's board of directors or its designee. The testing programs, at a minimum, should include the following:

- (i) compliance testing for all appropriate business lines conducted by qualified staff independent of the Bank's compliance, BSA/AML and OFAC functions;

- (ii) formal, documented testing programs, including adequately detailed reports and work papers;
- (iii) testing of the adequacy of the Bank's risk assessment;
- (iv) testing of the adequacy of the BSA and OFAC internal controls designed to ensure compliance with both the BSA and OFAC Provisions;
- (v) testing of the adequacy of the Bank's training program;
- (vi) a risk-based approach that includes transactional testing and verification of data for higher risk accounts;
- (vii) review of independent testing results by senior management;
- (viii) procedures to ensure that senior management institutes appropriate actions in response to independent testing results; and,
- (ix) direct lines of reporting between the independent testing function and the Bank's board of directors or its designee.

(b) The results of each independent test, as well as any apparent exceptions noted during the testing, shall be presented to the Bank's board of directors. The Bank's board of directors shall record the steps taken to correct any exceptions noted, address any recommendations made during each independent test, and record its actions in the minutes of the Bank's board of directors' meetings.

6. Within 60 days after the effective date of this ORDER, the Bank shall amend its audit policies, procedures, and practices, to ensure Bank adherence to an independent BSA audit program so that periodic reviews are made of the Bank's compliance with the BSA, Section 326.8 and Part 353 of the FDIC Rules and Regulations, 12 C.F.R. § 326.8 and 12 C.F.R. § 353,

and Treasury Rules and Regulations as part of the Bank's routine auditing. As long as this ORDER shall remain in effect, the Bank's BSA audit program shall include review of these areas, with significant exceptions reported directly to the Bank's board of directors.

7. (a) Within 90 days after the effective date of this ORDER, the Bank shall establish policies and procedures reasonably designed to identify and report suspicious activities ("SAR Policies"). At a minimum, the SAR Policies shall satisfy the requirements of Part 353 of the FDIC Rules and Regulations, 12 C.F.R. Part 353, and shall be reasonably designed to identify misconduct from both internal and external sources.

(b) The Bank shall submit the SAR Policies to the Regional Director and the Commissioner for review and comment. Within 30 days of the receipt of all such comments from the Regional Director and the Commissioner, and after consideration of such comments, the Bank shall approve the SAR Policies, which approval shall be recorded in the minutes of the Bank's board of directors. Thereafter, the Bank shall implement and fully comply with the SAR Policies. The SAR Policies shall be reviewed, revised as appropriate, and approved by the Bank's board of directors on an annual basis or more frequently as appropriate.

8. Within 120 days after the effective date of this ORDER, the Bank shall develop, adopt, and implement an enhanced system of internal controls to ensure compliance with the BSA, including, but not limited to, filing currency transaction reports; approving exemptions; aggregating related customer's transactions; monitoring high risk and suspicious activities for all types of accounts, customers, products, services, and geographic areas. At a minimum, such enhanced system of internal controls shall include:

(a) Procedures for conducting a risk-based assessment of the Bank's customer base to identify the categories of customers whose transactions and banking activities are routine

and usual, and for determining the appropriate level of enhanced due diligence necessary for those categories of customers whose transactions and banking activities are not routine and/or usual (“high-risk accounts”);

(b) Procedures with respect to high-risk accounts and customers identified through the risk assessment conducted pursuant to subparagraph (a), including the adoption of adequate methods for conducting enhanced due diligence on high-risk accounts and customers at account opening and on an ongoing basis, and for monitoring high-risk client relationships on a transaction basis, as well as by account and customer;

(c) Procedures and systems for identifying, evaluating, monitoring, investigating, and reporting suspicious activity in the Bank’s products, accounts, customers, services, and geographic areas, including:

- (i) the establishment of meaningful thresholds for identifying accounts and customers for further monitoring, review, and analyses;
- (ii) the periodic testing and monitoring of such thresholds for their appropriateness to the Bank’s products, customers, accounts, services, and geographic areas;
- (iii) procedures and/or systems for each business area of the Bank to produce periodic reports designed to identify unusual or suspicious activity, to monitor and evaluate unusual or suspicious activity, and to maintain accurate information needed to produce these reports with the following features:

- (A) the Bank's procedures and/or systems should be able to identify related accounts, countries of origin, location of the customer's businesses and residences to evaluate patterns of activity; and
- (B) the periodic reports should cover a broad range of time frames, including individual days, a number of days, and a number of months, as appropriate, and should segregate transactions that pose a greater than normal risk for non-compliance with the BSA;
- (iv) the review of existing systems to ensure adequate referral of information about potentially suspicious activity through appropriate levels of management, including a policy for determining action to be taken in the event of multiple filings of SARs on the same customer, or in the event a correspondent or other customer fails to provide due diligence information. Such procedures shall describe the circumstances under which an account should be closed and the processes and procedures to be followed in doing so;
- (v) documentation of management's decisions to file or not to file a SAR; and
- (vi) systems to ensure the timely, accurate, and complete filing of required SARs and any other similar or related reports required by law; and

9. (a) Within 30 days from the effective date of this ORDER, the Bank shall engage a qualified independent firm (“Consultant”), acceptable to the Regional Director and the Commissioner, to conduct a review of account and transaction activity, for the time period beginning January 1, 2005, and ending on the effective date of this ORDER, to determine whether suspicious activity involving any accounts of, or transactions within or through, the Bank were properly identified and reported in accordance with the applicable suspicious activity reporting requirements (“Look Back Review”).

(b) Within 10 days of the engagement of the Consultant, but prior to the commencement of the Look Back Review, the Bank shall submit to the Regional Director and the Commissioner for approval an engagement letter that sets forth:

- (i) the scope of the Look Back Review, including the types of accounts and transactions to be reviewed which shall, at a minimum, include, but not be limited to, the transactions or accounts identified in the ROE as requiring additional investigation by the Bank;
- (ii) the methodology for conducting the Look Back Review, including any sampling procedures to be followed;
- (iii) the expertise and resources to be dedicated to the Look Back Review; and
- (iv) the anticipated date of the completion of the Look Back Review.

(c) Upon completion of the Look Back Review, the Consultant shall provide a copy of the report detailing its findings to the Regional Director and the Commissioner at the same time the report is provided to the Bank.

(d) Within 30 days of its receipt of the Look Back Review report, the Bank shall ensure that all matters or transactions required to be reported, for which appropriate action has not previously been taken, are addressed in accordance with applicable laws and regulations.

10. (a) Effective with the date of this ORDER, the Bank shall require that all extensions of credit originated or renewed by the Bank have a defined and stated purpose and have a predetermined and realistic repayment source and schedule.

(b) The extension of credit shall be supported by current credit information and collateral documentation. The following documents, as appropriate, must be reviewed and maintained in the loan file throughout the term of the loan:

- (i) title and lien searches;
- (ii) perfected security interests;
- (iii) current financial information;
- (iv) profit and loss statements;
- (v) copies of tax returns;
- (vi) cash flow projections.

11. Within 60 days after the effective date of this ORDER the Bank shall modify its loan review process and ensure that it addresses loans of all sizes and collateral types, including unsecured loans.

12. Within 60 days after the effective date of this ORDER, the Bank shall establish and implement a formal pre-funding analysis and a comprehensive post-funding loan monitoring system to include stress testing and floor plan lending.

13. Within 60 days after the effective date of this ORDER, the Bank shall eliminate and/or correct all technical exceptions as to loan documentation as set forth in the ROE. Where

efforts to correct technical exceptions are unsuccessful, the loan file shall document the corrective efforts.

14. Within 60 days from the effective date of this ORDER, the Bank shall enhance its loan policy to include more specific guidelines regarding the allowance for loan and lease losses (“ALLL”) methodology and the documentation method. The Bank shall take the steps necessary to ensure full compliance with the 2006 *Interagency Policy Statement on the Allowance for Loan and Lease Losses*.

15. Within 60 days after the effective date of this ORDER, the Bank shall, consistent with safe and sound banking practices, eliminate and/or correct all violations of laws and regulations cited in the May 21, 2007 FDIC ROE and not corrected as of the date of this ORDER. Furthermore, the Bank shall adopt and implement procedures to ensure future compliance with all such applicable laws and regulations.

16. Within 90 days after the effective date of this ORDER, the Bank shall adopt and implement all policy recommendations included in the ROE.

17. Within 30 days after the effective date of this ORDER, the Bank’s board of directors shall establish a committee of the board of directors of the Bank (“Compliance Committee”) charged with the responsibility of ensuring that the Bank complies with the provisions of this ORDER. At least half of the members of such committee shall be directors who are not employees of the Bank other than as a director. Bank directors already serving on the audit committee of the Board may also serve as members of the Compliance Committee, so long as doing so would be consistent with the foregoing limitation. The Compliance Committee shall report monthly to the full board of directors of the Bank, and a copy of the report and any discussion relating to the report or the ORDER shall be noted in the minutes of the Bank’s board

of directors' meetings. The establishment of this committee shall not diminish the responsibility or liability of the entire board of directors of the Bank to ensure compliance with the provisions of this ORDER.

18. 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.

19. 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 and the Commissioner have released the Bank in writing from making additional reports.

This ORDER shall be binding upon the Bank, its successors and assigns, and all institution-affiliated parties of the Bank.

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

This ORDER will become effective upon its issuance by the FDIC.

Pursuant to delegated authority.

Dated this 26th day of February, 2008.

Thomas J. Dujenski
Regional Director
Dallas Regional Office
Division of Supervision and Consumer Protection
Federal Deposit Insurance Corporation

Randall S. James
Commissioner
Texas Department of Banking
Austin, Texas