

{{10-31-01 p.C-4994}}

[¶11,737] **In the Matter of Craig M. Horsch, Dewey State Bank, Dewey, Illinois**, Docket No. 00-067b (9-19-00).

A cease and desist order was issued, based on findings by the FDIC that it had reason to believe that respondent had engaged in unsafe and unsound practices. (*This order was terminated by order of the FDIC dated 8-22-01; see ¶16,290.*)

[.1] **Capital—Increase Required**

[.2] **Management—Qualifications Specified**
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[.3] **Extension of Credit—Restricted**

[.4] **Board of Directors—Review Specific Individuals' Salaries**

[.5] **Board of Directors—Outside Directors Added to Board**

[.6] **Dividends—Dividends Restricted**

[.7] **Assets—Adversely Classified Assets—Reduction Required**

[.8] **Loan Loss Reserve—Establishment of or Increase Required**

[.9] **Loans—Risk Position—Written Plan Required**

[.10] **Board of Directors—Review Bank Affairs**

[.11] **Technical Exceptions—Correction of Technical Exceptions Required**

[.12] **Loans—Collections, Written Policy Required**

[.13] **Board of Directors—Review Life Insurance Policies**

[.14] **Funds Management and Liquidity—Preparation or Revision of Funds Management Policy Required**

[.15] **Violations of Law—Correction of Violations Required**

[.16] **Profit Plan—Preparation of Plan Required**

[.17] **Bank Operations—New Lines of Business Restricted**

[.18] **Shareholders—Disclosure of Cease and Desist Order Required**

**In the Matter of
CRAIG M. HORSCH,
individually, and as an officer, director, person participating in the conduct of the affairs, and
institution-affiliated party of
Dewey State Bank Dewey, Illinois
and
DEWEY STATE BANK
DEWEY, ILLINOIS
(Insured State Nonmember Bank)
ORDER TO CEASE AND DESIST**

FDIC-00-067b

Dewey State Bank ("Bank"), and Craig M. Horsch ("Individual Respondent"), as an officer, director, person participating in the conduct of the affairs, and institution-affiliated party of the Bank, having been advised of their 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 Individual Respondent and of their right to a hearing on the 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 the Assistant Commissioner of the Illinois Office of Banks and Real Estate ("Assistant Commissioner"), dated September 19, 2000, 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 and Individual Respondent consented to the issuance of an ORDER TO CEASE AND DESIST ("ORDER") by the FDIC.

The FDIC and Assistant Commissioner considered the matter and determined that there was reason to believe that the Bank and Individual Respondent had engaged in unsafe or unsound banking practices and had committed violations of law 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), its successors and assigns, and Craig M. Horsch, individually, as an officer, director, person participating in the conduct of the affairs, and as an institution-affiliated [{{11-30-00 p.C-4996}}](#) party of the Bank, cease and desist from the following unsafe or unsound banking practices and violations of law or regulation:

A. Engaging in hazardous lending and lax collection practices, including, but not limited to the following:

- The failure to obtain proper loan documentation;
- The failure to obtain adequate collateral;
- The failure to establish and monitor collateral margins of secured borrowers;
- The failure to establish and enforce adequate loan repayment programs;
- The failure to obtain current and complete financial information;
- The failure to obtain and review appraisals; and
- The failure to enforce loan policy guidelines and officer lending limits.

B. Operating with an inadequate level of capital protection for the kind and quality of assets held.

C. Violating laws or regulations, including:

- The State of Illinois legal lending limit restrictions as set forth in section 32 of the Illinois Banking Act, 205 ILCS 5/32;
- The terms and creditworthiness prohibitions of section 215.4(a)(1) of Regulation O of the Board of Governors of the Federal Reserve System, 12 C.F.R. § 215.4(a)(1);
- The documentation requirements of section 206.5(b) of Regulation F of the Board of Governors of the Federal Reserve System, 12 C.F.R. § 206.5(b);
- The prohibitions on activities and investments of insured state banks of section 362.3(b) of the FDIC Rules and Regulations, 12 C.F.R. § 362.3(b); and
- The annual security program reporting requirements of section 326.4 of the FDIC Rules and Regulations, 12 C.F.R. § 326.4

D. Operating with excessive levels of adversely classified assets, assets listed for "Special Mention,"

delinquent loans, and nonaccrual loans.

E. Operating with inadequate liquidity in light of the Bank's asset and liability mix.

F. Operating with an inadequate allowance for loans and lease losses for the volume, kind, and quality of loans and leases held.

G. Operating with excessive overhead expenses.

H. Operating with inadequate policies to monitor and control asset growth.

I. Operating with management whose policies and practices are detrimental to the Bank and which jeopardize the safety of its deposits.

J. Operating with a board of directors which has failed to provide adequate supervision over and direction to the management of the Bank to prevent unsafe or unsound banking practices and violations of laws or regulations.

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

[.1] 1. (a) The Bank shall increase its Tier 1 capital by not less than \$400,000. This requirement may be satisfied if, by September 30, 2000, the Bank enters into a letter of intent for a sale or merger, the terms of which provide for this capital increase not later than January 31, 2001. Should the Bank fail to enter into such a letter of intent for a sale or merger, the increase in the Bank's Tier 1 capital required by this subparagraph shall be accomplished by November 15, 2000.

(b) Within 30 days from the last day of each calendar quarter following the date that the Bank is required to enter into a letter of intent for a sale or merger, or alternatively, should the Bank fail to enter into such a letter of intent within the allocated period, within 30 days from the last day of each calendar quarter following November 15, 2000, the 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 8 percent, the Bank shall, within 60 days of the date of the required determination, increase its capital ratio to not less than 8 percent calculated as of the end of that preceding quarterly period. For purposes of this ORDER, Tier 1 capital and total assets shall be calculated in accordance with Part 325 of the FDIC Rules and Regulations ("Part 325"), 12 C.F.R. Part 325.

(c) Any such increase in Tier 1 capital may be accomplished by the following:
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(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 February 22, 2000, 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's 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 and State securities laws. Prior to the implementation of the plan and, in any event, not less than 20 days prior to the dissemination of such materials, the materials to be used in the sale of the securities shall be submitted to the FDIC Registration and Disclosure Section, 550 17th Street, N.W., Washington, D.C. 20429, and to the Assistant Commissioner for review. Any changes requested to be made in the materials by the FDIC and the Assistant Commissioner shall be made prior to their dissemination.

(e) In complying with the provisions of this paragraph, 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 that 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.

[.2] 2. (a) The Bank shall have and retain qualified management. This requirement may be satisfied if, by September 30, 2000, the Bank enters into a letter of intent for a sale or merger, the terms of which provide for the retention of qualified management as specified in this subparagraph not later than January 31, 2001. Should the Bank fail to enter into such a letter of intent for a sale or merger, the Bank shall retain qualified management as specified in this subparagraph by December 1, 2000. At a minimum, such management shall include: (i) a chief executive officer with proven ability in managing a bank of comparable size and with experience in upgrading a low quality loan portfolio; and (ii) a senior lending officer with an appropriate level of lending, collection, and loan supervision experience for the type and quality of the Bank's loan portfolio. The qualified chief executive officer and senior lending officer required by this paragraph may be the same individual. Such person(s) 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.

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(b) During the life of this ORDER, pursuant to section 32 of the Act, 12 U.S.C. § 1831(i), the Bank shall notify the Regional Director of the Chicago Regional Office of the FDIC ("Regional Director") and Assistant Commissioner in writing when it proposes to add any individual to its board of directors or employ any individual as a senior executive officer. This notification must be received at least 30 days before such addition or employment is intended to become effective, must include a description of the background and experience of the individual(s) to be added or employed, and in all respects must comply with Subpart F of Part 303 of the FDIC Rules and Regulations.

[.3] 3. (a) As of the effective date of this ORDER, the Individual Respondent shall not approve any extension of credit to any customer of the Bank in excess of \$25,000 without the prior review and written approval of the senior lending officer appointed pursuant to this ORDER, or the bank's board of directors. For purposes of this paragraph, the term "extension of credit" includes all newly originated loans, loans renewed or extended beyond the original contractual maturity date, advances of additional funds to loan customers beyond the terms of the original extension of credit, and capitalization of interest owing on any extension of credit, when the resulting extension of credit is in excess of \$25,000.

(b) Within 120 days from the effective date of this ORDER, the Bank shall submit to the Regional Director and Assistant Commissioner, an educational plan for the Individual Respondent focusing on the

areas of lending, operations, and compliance with laws, rules, and regulations applicable to FDIC-insured depository institutions. After adoption of any recommended changes by the Regional Director and Assistant Commissioner, the Bank shall ensure that the Individual Respondent implements and follows the educational plan.

(c) As of the effective date of this ORDER, the Individual Respondent shall not approve the purchase by the Bank of any extension of credit or brokered loan from any third party or financial institution until the completion of the educational plan implemented pursuant to this paragraph.

(d) Nothing in this ORDER is intended to restrict the Individual Respondent's loan collection efforts or prohibit the Individual Respondent from voting on loans in his capacity as a director.

[.4] 4. Within 30 days from the effective date of this ORDER and annually thereafter, the board of directors shall conduct a review of the salary and benefit packages of both the Individual Respondent and Bank Chairman of the Board Kay J. Horsch, to determine their reasonableness in light of each individual's duties and responsibilities, with such review noted in the minutes of the Bank's board of directors' meeting at which such review was made. Immediately thereafter, the board of directors shall take action to implement the findings of this review.

[.5] 5. The Bank shall add to its board of directors two new members who are independent directors. This requirement may be satisfied if, by September 30, 2000, the Bank enters into a letter of intent for a sale or merger, the terms of which provide for the addition of two new board members who are independent directors not later than January 31, 2001. Should the Bank fail to enter into such a letter of intent for a sale or merger, the addition of two new independent board members shall be accomplished by December 1, 2000. 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 by blood, marriage or common financial interest, including the indebtedness of any entity in which the individual has a substantial financial interest, in an amount exceeding 5 percent of the Bank's total Tier 1 capital and allowance for loan and lease losses. The addition of any new Bank directors required by 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.

[.6] 6. 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 Assistant Commissioner.

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[.7] 7. 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" in the FDIC's Report of Examination as of February 22, 2000 ("Report") that have not been previously collected or charged off. Any such charged-off asset shall not be rebooked. 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.

[.8] 8. (a) Within 5 days from the effective date of this ORDER, the Bank shall replenish its allowance for loan and lease losses ("ALLL") in the amount of not less than \$188,000.

(b) Within 45 days from the effective date of this ORDER, Reports of Condition and Income required by the FDIC and filed by the Bank subsequent to February 22, 2000, shall be amended and re-filed 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 adjustment required by this paragraph.

(c) 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, provide for an adequate 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 ALLL provided. In making these determinations, the board of directors shall consider the Federal Financial Institutions Examination Council's Instructions for the Reports of Condition and Income and any analysis

of the Bank's ALLL provided by the FDIC.

(d) ALLL entries required by this paragraph shall be made prior to the calculation of the Tier 1 capital levels required by this ORDER.

[.9] 9. (a) Within 60 days from the effective date of this ORDER, the Bank shall formulate and submit to the Regional Director and Assistant Commissioner, for review and comment, a written plan to reduce the Bank's risk position in each asset in excess of \$25,000 which is classified "Substandard" in the Report. 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 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 the receipt of any comment from the Regional Director and Assistant Commissioner, and after the adoption of any recommended changes, the Bank shall approve the written plan, which approval shall be recorded in the minutes of a board of directors' meeting. Thereafter, the Bank shall implement and follow this written plan.

[.10] 10. Within 30 days from the effective date of this ORDER, and annually thereafter, the board of directors of the Bank shall review the Bank's underwriting and credit administration practices and, based upon this review, shall strengthen lending procedures and abate additional loan deterioration. At a minimum, the Bank shall correct the weaknesses set forth on pages 33 through 36 of the Report.

11. Within 30 days from the effective date of this ORDER, the Bank shall correct all deficiencies in the loans listed for "Special Mention" in the Report.

[.11] 12. Within 30 days from the effective date of this ORDER, the Bank shall correct the technical exceptions listed in the Report.

[.12] 13. Within 30 days from the effective date of this ORDER, the Bank shall adopt and implement a written plan for the reduction and collection of delinquent loans. A copy of the written plan shall be submitted to the Regional Director and Assistant Commissioner upon its completion. Said plan shall include, but not be limited to the following:

(a) Dollar levels to which the Bank shall reduce delinquencies within 6 and 12 months from the effective date of this ORDER; and

(b) 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 board of directors. Reductions of delinquent loans with the proceeds of other Bank extensions of credit, or through the granting of unsupported payment extensions or credit renewals will not be considered appropriate for the purpose of this paragraph.

[.13] 14. (a) Within 45 days from the effective date of this ORDER, the board of directors of the Bank shall review the key person life insurance issues discussed in the Report. At a minimum, the board of directors of the Bank shall:

(i) review each key person whole life insurance policy for which the Bank is paying or has paid a premium to determine if: (A) the size of the policy is appropriate in terms of the insured's value to

the Bank; and (B) the Bank is the owner and beneficiary of each policy, as appropriate;

(ii) require all assets and accounting entries arising from the key person insurance policies be reflected on the Bank's books in accordance with generally accepted accounting principles;

(iii) document that each key person life insurance policy fully complies with the guidelines established in the Office of the Comptroller of the Currency's Bulletin 96-51, dated September 20, 1996;

(iv) take appropriate measures, based on the determination made in provisions (i) through (iii) of this paragraph, to correct any deficiencies arising from the key person life insurance policies.

(b) Within 90 days from the effective date of this ORDER, the board of directors of the Bank shall submit to the Regional Director and Assistant Commissioner a written report of the review required by this paragraph of this ORDER.

[.14] 15. Within 60 days from the effective date of this ORDER, the Bank shall adopt and implement a written plan addressing liquidity and the Bank's relationship of volatile liabilities to temporary investments and rate sensitivity objectives. A copy of the plan shall be submitted to the Regional Director and Assistant Commissioner upon its completion. 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. The initial plan shall, at a minimum:

(i) Establish recordkeeping systems to identify and track the volume of core deposits and volatile deposits;

(ii) Establish a desirable range for net non-core funding dependency ratio ("dependency ratio") as computed by the FDIC.

(iii) Require that monthly calculations of the liquidity ratio (following the format utilized by the Illinois Office of Banks and Real Estate in regulatory reports of examination), and the dependency ratio be provided to the board of directors for review, with such review noted in the board minutes;

(iv) Identify the source and use of borrowed and/or volatile funds;

(v) Establish an acceptable range for the relationship between rate sensitive assets and rate sensitive liabilities;

(vi) Establish appropriate lines of credit at correspondent banks that would allow the Bank to borrow funds to meet depositor demands if the Bank's other provisions for liquidity are inadequate;

(vii) Require the retention of securities and/or other identified categories of investments that can be liquidated within one day in amounts sufficient (as a percentage of the Bank's total assets) to ensure the maintenance of the Bank's liquidity posture at a level consistent with short- and long-term liquidity objectives;

(viii) Establish contingency plans to improve liquidity to the level established in the Bank's liquidity policy.

[.15] 16. (a) Within 10 days from the effective date of this ORDER, the Bank shall [{{1-31-02 p.C-5001}}](#)eliminate and/or correct all violations of law and/or regulations listed on pages 42 through 44 of the Report.

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

[.16] 17. (a) Within 90 days from the effective date of this ORDER, the Bank shall adopt and implement a written profit plan and a realistic, comprehensive budget for all categories of income and expense. The plan required by this paragraph shall contain formal goals and strategies, consistent with sound banking practices, to reduce discretionary expenses and to improve and sustain earnings of the Bank. The plan shall include a description of the operating assumptions that form the basis for major projected income and expense components. Thereafter, the Bank shall formulate such a plan and budget by November 30

of each subsequent year.

(b) The plans and budgets required by this paragraph, upon completion, shall be submitted to the Regional Director and Assistant Commissioner for review and the opportunity for comment.

(c) Following 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.

[.17] 18. The Bank shall provide 30 days' prior written notice to the Regional Director and Assistant Commissioner before engaging in any new line of business, including but not limited to: mortgage banking operations, subprime lending, high loan-to-value lending, out-of-territory lending (outside Champaign, DeWitt, Ford and McLean counties) in excess of 20% of Tier 1 capital, and transactional internet banking activities. Such notice shall include a detailed business plan which describes the nature and scope of the Bank's planned activities and includes pro-forma financial projections for the first three years of operation.

[.18] 19. Following the effective date of this ORDER, the Bank shall send to its shareholders or otherwise furnish a description of this ORDER in conjunction with the Bank's next shareholder communication; and also 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 Registration and Disclosure Section, 550 17th Street, N.W., Washington, D.C. 20429, 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. Within 30 days from the end of each calendar quarter, the Bank shall furnish written progress reports, signed by each member of the Bank's board of directors, to the Regional Director and the Assistant 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 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, any successors and assigns thereof, and Craig M. Horsch, individually.

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.

Pursuant to delegated authority.

Dated this 19th day of September, 2000.