

*Quarterly
Journal*

**SPECIAL SUPERVISION AND
ENFORCEMENT ACTIVITIES**

SPECIAL SUPERVISION AND ENFORCEMENT ACTIVITIES

The Special Supervision Division of the Midsize and Community Bank Supervision department supervises critical problem banks through rehabilitation or through other resolution processes such as orderly failure management or the sale, merger, or liquidation of such institutions. The Special Supervision Division monitors the supervision of delegated problem banks, coordinates safety and soundness examinations, provides training, analyzes and disseminates information, and supports OCC supervisory objectives as an advisor and liaison to OCC management and field staff on emerging problem bank related issues.

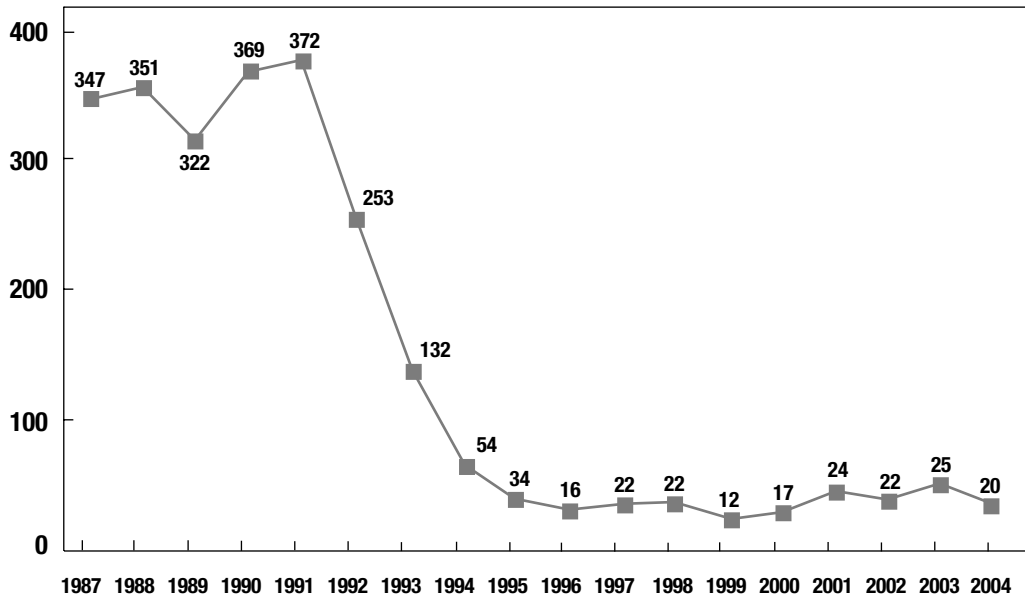
This section includes information on problem national banks, national bank failures, and enforcement actions. Data on problem banks and bank failures is provided by OCC's Special Supervision department and the FDIC's Department of Resolutions in Washington. Information on enforcement actions is provided by the Enforcement and Compliance Division (E&C) of the law department. The latter is principally responsible for presenting and litigating administrative actions on the OCC's behalf against banks requiring special supervision.

Problem National Banks and National Bank Failures

Problem banks represented approximately 1 percent of the national bank population as of December 31, 2004. The volume of problem banks, those with a CAMELS rating of 4 or 5, has been relatively stable for several years. The CAMELS rating is the composite bank rating based on examiner assessment of capital, asset quality, management, earnings, liquidity, and sensitivity to market risk. The total number of problem banks is 20 at December 31, 2004, and declined 20 percent from the number reported at December 31, 2003. This low volume of problem banks reflects the stable economy and generally favorable economic conditions enjoyed for the past several years. One national bank failure occurred during 2004 out of the four commercial bank/savings bank failures.

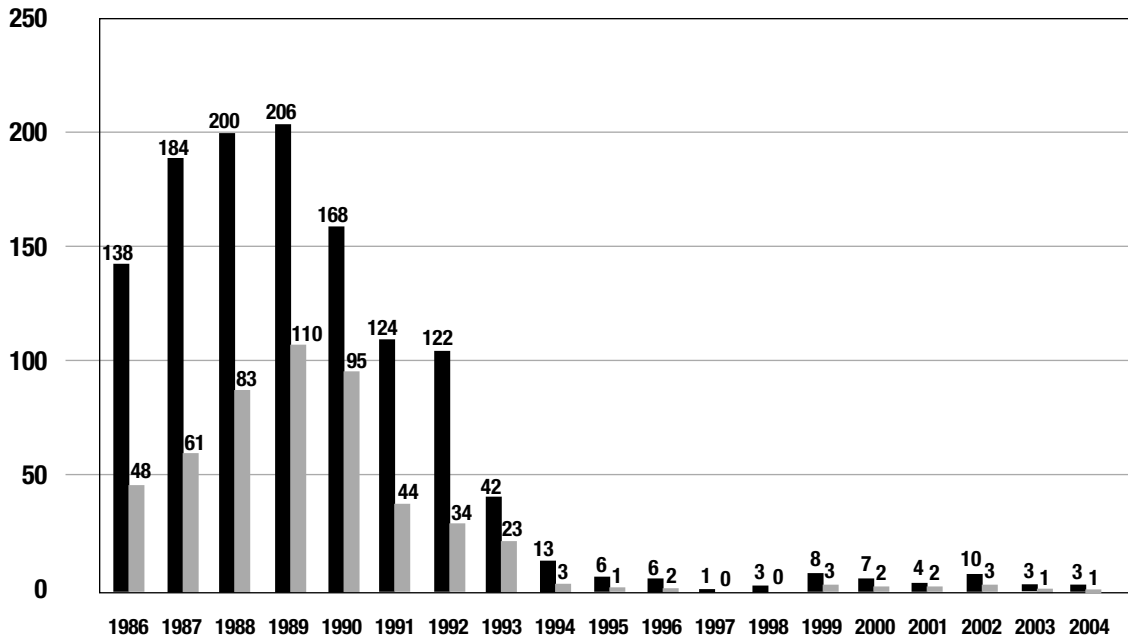
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Figure 1—Total number of banks rated 4 or 5 as of year-end



Source: OCC FINDRS

Figure 2—Total bank failures compared to OCC failures



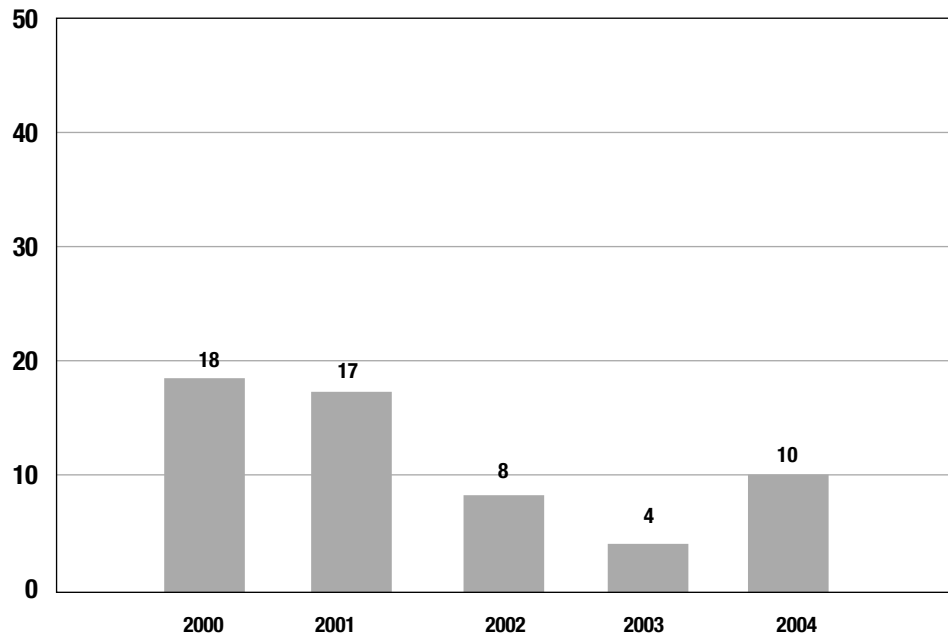
Source: Federal Deposit Insurance Corporation

Enforcement Actions

The OCC has a number of remedies with which to carry out its supervisory responsibilities. When it identifies safety and soundness or compliance problems, these remedies range from advice and moral suasion to informal and formal enforcement actions. These mechanisms are designed to achieve expeditious corrective and remedial action to return the bank to a safe and sound condition.

The OCC takes enforcement actions against national banks, parties affiliated with national banks, and servicing companies that provide data processing and other services to national banks. The OCC's informal enforcement actions against banks include commitment letters and memorandums of understanding (MOUs). Informal enforcement actions are meant to handle less serious supervisory problems identified by the OCC in its supervision of national banks. Failure to honor informal enforcement actions will provide strong evidence of the need for the OCC to take formal enforcement action. The charts below show total numbers of the various types of informal enforcement actions completed by the OCC against banks in the last several years.

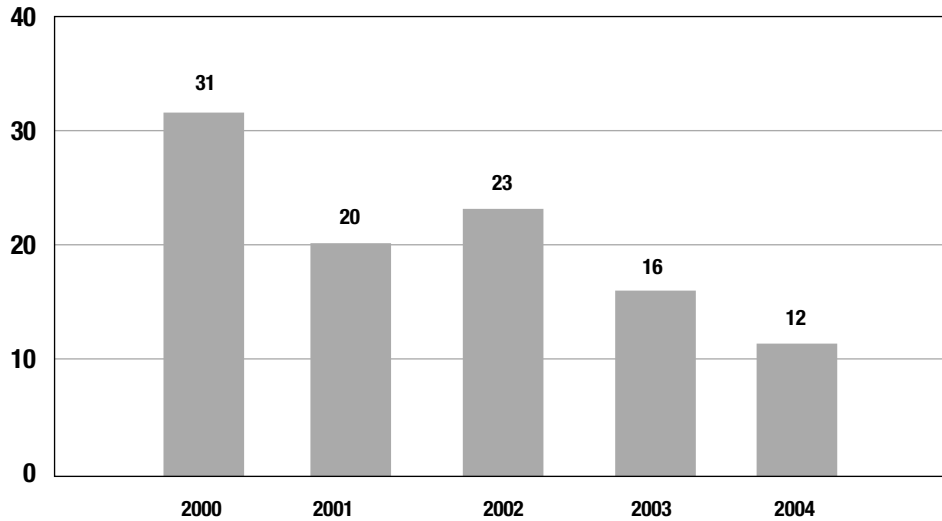
Figure 3—Commitment letters



Source: OCC Systems. Note that totals for previous years' completed enforcement actions may be adjusted to reflect revised aggregates.

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Figure 4—Memorandums of understanding

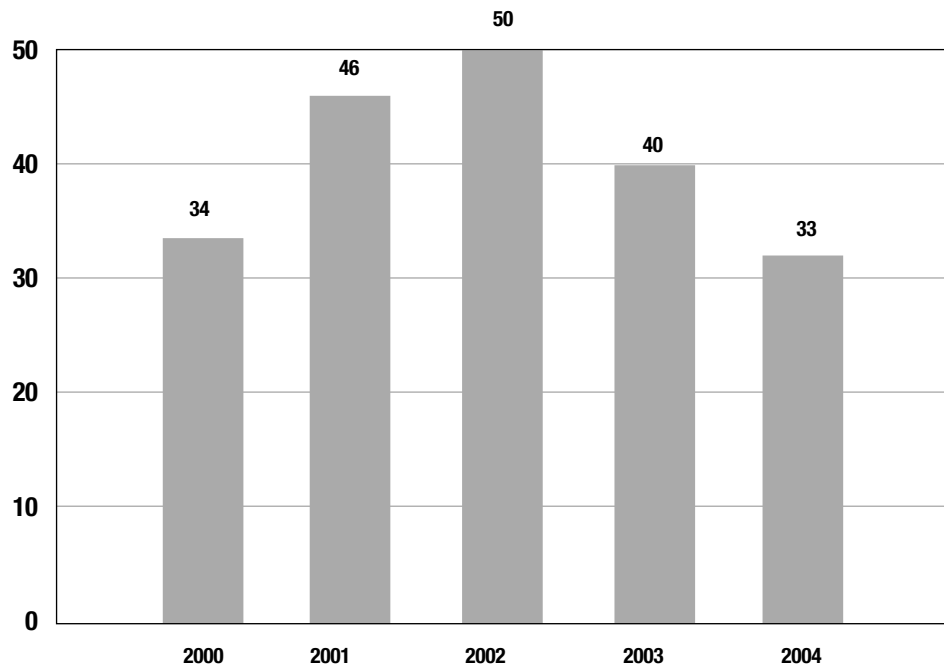


Source: OCC Systems. Note that totals for previous years' completed enforcement actions may be adjusted to reflect revised aggregates.

The most common types of formal enforcement actions issued by the OCC against banks over the past several years have been formal agreements and cease-and-desist orders. Formal agreements are documents signed by a national bank's board of directors and the OCC in which specific corrective and remedial measures are enumerated as necessary to return the bank to a safe and sound condition. Cease-and-desist orders (C&Ds), sometimes issued as consent orders, are similar in content to formal agreements, but may be enforced either through assessment of civil money penalties (CMPs) or by an action for injunctive relief in federal district court. The OCC may also assess CMPs against banks, and in 2004, the OCC assessed CMPs against six banks.

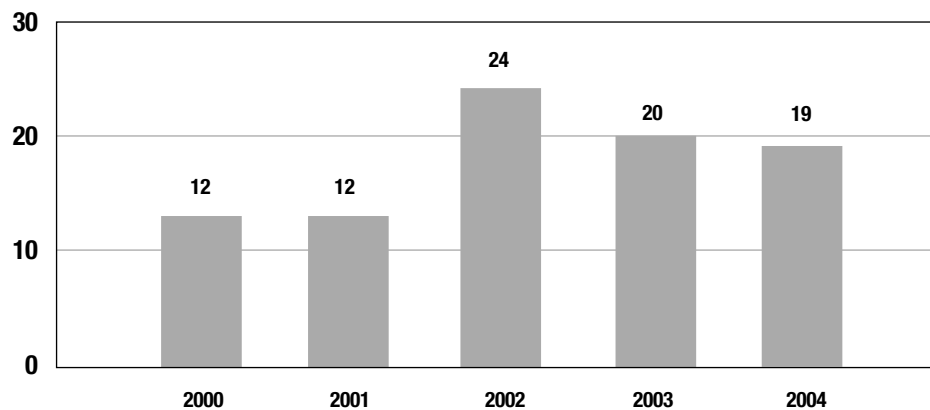
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Figure 5—Formal agreements



Source: OCC Systems. Note that totals for previous years' completed enforcement actions may be adjusted to reflect revised aggregates.

Figure 6—Cease-and-desist orders against banks

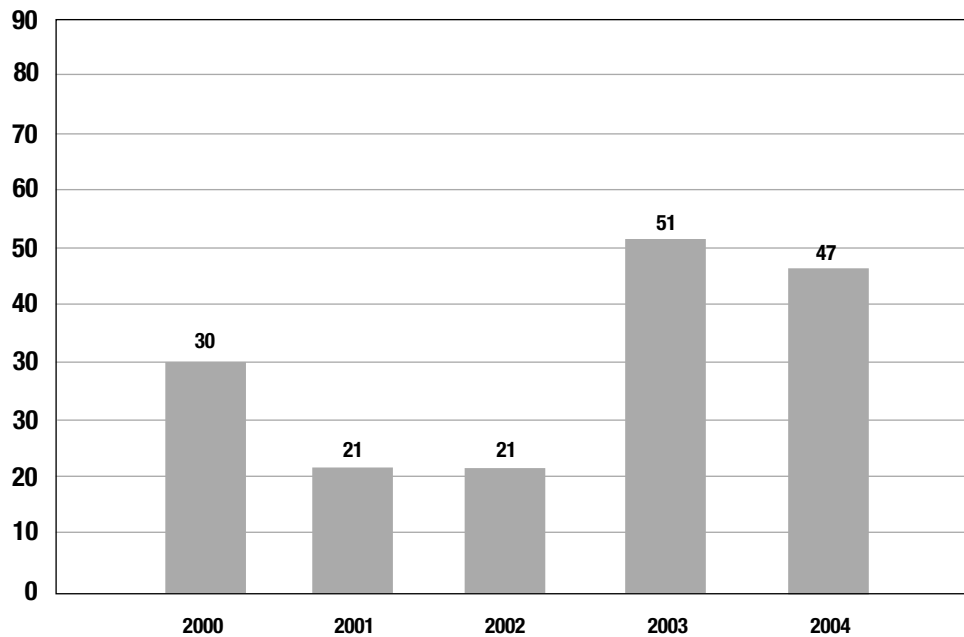


Source: OCC Systems. Note that totals for previous years' completed enforcement actions may be adjusted to reflect revised aggregates.

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The most common enforcement actions against individuals and other institution-affiliated parties are CMPs, personal C&Ds, and removal and prohibition orders. CMPs are authorized for violations of laws, rules, regulations, formal written agreements, final orders, conditions imposed in writing, unsafe or unsound banking practices, and breaches of fiduciary duty. Personal C&Ds may be used to restrict activities, order payment of restitution, or require institution-affiliated parties to take other affirmative action to correct the results of past conduct. Removal and prohibition actions, which are used in the most serious cases, result in lifetime bans from the banking industry.

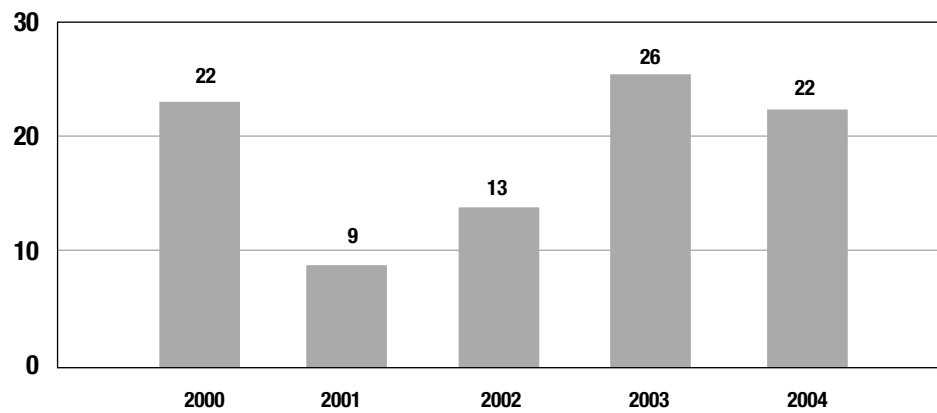
Figure 7—Civil money penalties against institution-affiliated parties



Source: OCC Systems. Note that totals for previous years' completed enforcement actions may be adjusted to reflect revised aggregates.

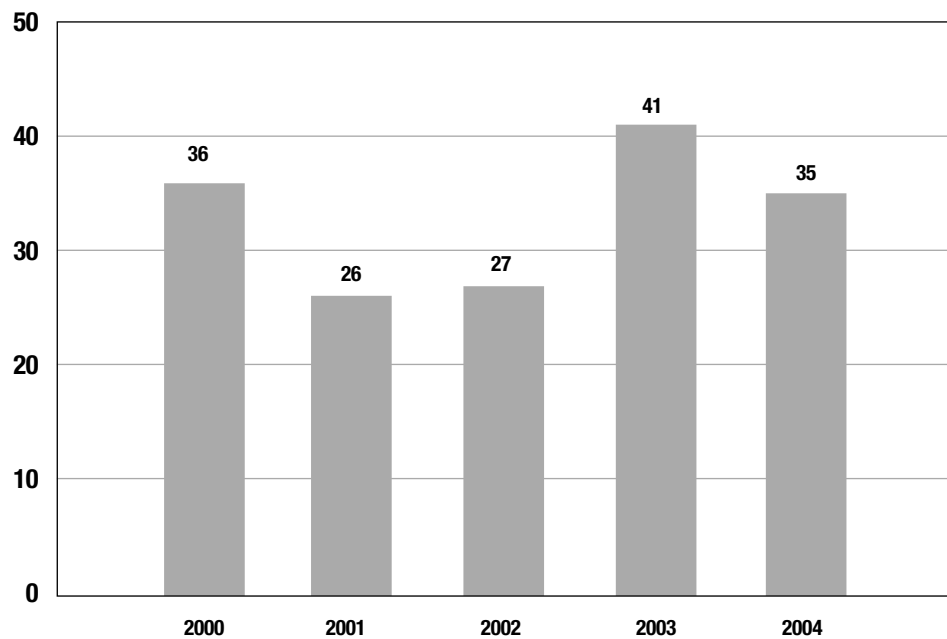
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Figure 8—Cease-and-desist orders against institution-affiliated parties



Source: OCC Systems. Note that totals for previous years' completed enforcement actions may be adjusted to reflect revised aggregates.

Figure 9—Removal and prohibition orders



Source: OCC Systems. Note that totals for previous years' completed enforcement actions may be adjusted to reflect revised aggregates.

Recent Enforcement Cases

Below are summaries of the significant cases completed between July 1 and December 31, 2004:

A. Actions Involving Bank Secrecy Act/Anti-Money-Laundering Compliance

Banks ordered to comply with Bank Secrecy Act/Anti-Money-Laundering (BSA/AML) provisions. The OCC brought enforcement actions against banks for failing to maintain adequate BSA/AML compliance programs and ordered those banks to provide for internal controls, auditing, and employee training, and to designate a BSA compliance officer. *In the Matter of Fullerton National Bank, Fullerton, NE*, Enforcement Action No. 2004-121 (September 21, 2004); *Formal Agreement: First National Bank, Graford, TX*, Enforcement Action No. 2004-115 (October 1, 2004); *In the Matter of International Bank of Miami, N.A., Coral Gables, FL*, Enforcement Action No. 2004-119 (October 18, 2004); *In the Matter of The Upstate National Bank, Lisbon, NY*, Enforcement Action No. 2004-154 (November 4, 2004); *In the Matter of The First National Bank of Paonia, Paonia, CO*, Enforcement Action No. 2004-131 (November 18, 2004); *In the Matter of Metropolitan Bank & Trust Co (Federal branch), New York, NY*, Enforcement Action No. 2004-155 (December 15, 2004); *In the Matter of Asia Bank, N.A., New York, NY*, Enforcement Action No. 2004-153 (December 17, 2004); *In the Matter of Eagle National Bank of Miami, Doral, FL*, Enforcement Action No. 2004-138 (December 21, 2004).

B. Early Intervention for Problem Banks

Enforcement actions against bank officer and directors for suspicious loan transaction. The OCC continued to pursue enforcement actions against the president and directors of a national bank that had engaged in a questionable loan transaction with The Central Bank of the Gambia (CBG). Seven of the bank's directors consented to the OCC's assessments of civil money penalties for varying levels of alleged culpability for the loan transaction and other deficiencies in the bank's operations. The OCC also initiated a cease and desist action and assessed a \$100,000 civil money penalty against the bank's former president, which actions are currently in litigation. *In the Matter of Arthur Mason, First Liberty National Bank, Washington, DC*, Enforcement Action No. 2004-104 (September 22, 2004); *In the Matter of Madhu Mohan*, Enforcement Action No. 2004-105 (September 22, 2004); *In the Matter of Patrick M. Donahue*, Enforcement Action No. 2004-99 (September 22, 2004); *In the Matter of John J. Mahoney*, Enforcement Action No. 2004-103 (September 22, 2004); *In the Matter of Shailendra Kumar*, Enforcement Action No. 2004-102 (September 22, 2004); *In the Matter of Kailash C. Goel*, Enforcement Action No. 2004-100 (September 22, 2004); *In the Matter of John M. Jacquemin*, Enforcement Action No. 2004-101 (September 22, 2004); *OCC v. Richard Dean*, OCC Docket No. AA-EC-04-25.

Bank ordered to close lending division, increase capital levels, and enhance BSA/AML procedures. A bank permitted one of its departments to engage in unsafe and unsound banking practices. In addition, the OCC found significant deficiencies in board of directors oversight and management of the day-to-day operations of that department, exposing the bank to substantial

reputation, transaction, and litigation risk. The OCC issued a cease and desist order by consent that formalized the shut-down of the lending department. The order also required the bank to address deficiencies in the bank's compliance with BSA and USA PATRIOT Act; to increase capital levels, in view of increased risks; and to correct problems with the bank's books and records. *In the Matter of International Bank of Miami, N.A., Coral Gables, FL*, Enforcement Action No. 2004-119 (October 18, 2004).

C. Actions Involving Third-Party Institution-Affiliated Parties

Enforcement actions against a bank's outside legal counsel. As a result of its formal investigation into irregularities in the operations of a national bank, the OCC brought enforcement actions against the law firm that principally represented both the bank and the bank's service provider, and against the individual law firm partner who principally represented the bank. The law firm consented to the OCC's cease and desist order to pay \$90,000 to reimburse the bank for certain legal fees alleged to have been improperly billed and paid, and to observe restrictions on the firm's representation of insured depository institutions. The law firm partner consented to the OCC's assessment of a \$10,000 civil money penalty. *In the Matter of Wolf Haldenstein Adler Freeman & Herz, LLP, New York, NY (former counsel for Sinclair National Bank, Grayette, AR)*, Enforcement Action No. 2004-140 (November 30, 2004); *In the Matter of Helen Davis Chaitman*, Enforcement Action No. 2004-98 (September 22, 2004).

Enforcement actions against officers of failed bank's independent service organization. A national bank failed as a result of excessive charge-backs in its merchant processing portfolio, due to fraud by several merchants. The bank had contracted with several independent service organizations (ISO) to conduct the underwriting function for merchants, including ISO Cashgate, Inc., which allegedly was responsible for underwriting virtually all of the merchants who had engaged in fraudulent activity. The OCC initiated enforcement actions against the president and the chairman/CEO of Cashgate, Inc. The two officers consented to the OCC's cease and desist orders prohibiting them from providing goods or services to any insured depository institutions, and each consented to the assessment of a \$2,500 civil money penalty. *In the Matter of Bernard P. Kenneally, Cashgate, Inc. (former independent contractor of National State Bank of Metropolis, Metropolis, IL)*, Enforcement Action No. 2004-19 (April 2, 2004); *In the Matter of Gregory P. Healey, Cashgate, Inc.*, Enforcement Action No. 2004-156 (October 19, 2004).

Enforcement action against a failed bank's external auditor. The OCC conducted a public hearing before an administrative law judge, commencing November 10, 2004, concerning an enforcement proceeding against Grant Thornton LLP, former external auditor for the failed First National Bank of Keystone, Keystone, WV. The OCC alleges that Grant Thornton should have but failed to discover that the bank had overstated its assets by more than \$500 million. The OCC subsequently closed the bank. The OCC is seeking a cease and desist order that would require Grant Thornton to perform various enhanced auditing practices and procedures whenever it audits insured depository institutions. The agency also seeks the assessment of a \$300,000 civil money

penalty against Grant Thornton. The matter is under review by the administrative law judge. *OCC v. Grant Thornton, LLP* (OCC Docket Nos. AA-EC-04-02, AA-EC-04-03).

D. Actions Involving Institution-Affiliated Parties of Resolved Problem Banks

Enforcement actions against officers and directors for unsafe and unsound lending practices and breaches of fiduciary duty. A national bank with declining capital and increasing credit risks elected, under the terms of a consent order, to close the bank by selling its deposits and pursuing voluntary dissolution under 12 USC 181, which was completed with the merger of the bank into a nonbank subsidiary under 12 USC 215c. The bank's president subsequently consented to the OCC's prohibition order and assessment of a \$100,000 civil money penalty, for allegedly engaging in a pattern of originating loans without conducting prudent underwriting procedures, receiving the proceeds of loans, diverting loan proceeds to past-due loans, and under-reporting levels of past-due loans in regulatory reports. The OCC also assessed civil money penalties against the bank's vice president (\$40,000) and against two outside directors (\$2,500 each). *In the Matter of Joseph E. Johnson, First National Bank of Sumner, Olney, IL*, Enforcement Action No. 2004-123 (October 21, 2004); *In the Matter of Lyle Puzey*, Enforcement Action No. 2004-84 (July 29, 2004); *In the Matter of Christina Puzey*, Enforcement Action No. 2004-83 (July 29, 2004); *In the Matter of A. Melinda Meyer*, Enforcement Action No. 2004-82 (July 29, 2004).

Enforcement actions against officers and directors for unsafe or unsound lending practices, uncorrected violations of law, and breaches of fiduciary duty. The OCC continued to pursue enforcement actions against the officers and directors of a national bank that had been sold to prevent the bank's failure. The bank, which had been operating under a formal agreement since 2001, allegedly failed to correct deficiencies in lending practices, asset quality, and internal controls, and allegedly failed to correct violations of law, including suspected violations of the legal lending limit. The bank's four outside directors consented to assessments of civil money penalties in amounts ranging from \$18,000 down to \$5,000. Three of those directors consented to cease and desist orders and the fourth consented to a prohibition order. Actions against the former president and one inside director are in litigation. *In the Matter of Kim Morris, First National Bank, Lubbock, TX*, Enforcement Action No. 2004-111 (September 3, 2004); *In the Matter of Darrell Hobgood*, Enforcement Action No. 2004-110 (September 28, 2004); *In the Matter of Brian Burns*, Enforcement Action No. 2004-125 (October 13, 2004); *In the Matter of Johnny Bob Carruth*, Enforcement Action No. 2004-109 (September 22, 2004).

Enforcement actions against a former bank president for insider abuses. A bank was merged into another bank to avoid bank failure. The OCC obtained consent orders against many of the former officers, directors, and employees of the bank who were allegedly responsible for the bank's failure to comply with a formal agreement with the OCC and for allegedly engaging in activities that caused the increased risks and deteriorating financial condition that led to the closing of the bank. The former president/COB/majority shareholder had also allegedly engaged in insider abuse for

his personal benefit, including the issuance of money orders for his own benefit without contemporaneous payment, overdraft abuse, and illegal extensions of credit. He also allegedly caused the bank to pay personal expenses for himself and his family. The former president consented to the OCC's order of prohibition and the assessment of a \$100,000 civil money penalty. *In the Matter of Nelson D. Hogg, First National Bank of O'Donnell, O'Donnell, TX*, Enforcement Actions Nos. 2003-72 (June 25, 2003) and 2004-90 (September 2, 2004).

E. Actions to Combat Bank Insider Abuse

Enforcement actions against loan officers for insider abuses. Two loan officers, one of whom is suspected to have engaged in misconduct at two successive banks, allegedly received payments and other benefit for making several million dollars' worth of loans to non-creditworthy borrowers for the benefit of a third party and to the detriment of the banks issuing the loans. One of the loan officers consented to the OCC's prohibition order and assessment of a \$130,000 civil money penalty. Action against the second loan officer is proceeding, and the investigation into misconduct continues. *In the Matter of David A. Ranostaj, Whitney National Bank, New Orleans, LA*, Enforcement Action No. 2004-152 (December 23, 2004).

Enforcement action against loan officer for improper lending practices. A loan officer allegedly made loans to a business partner, who was known to be experiencing financial difficulties, in violation of the bank's loan policy and in contravention of explicit instructions not to make further loans to the borrower. As a result of the loan officer's actions, the bank suffered a loss in excess of \$30,000. The loan officer allegedly received some of the proceeds of the new loans. The loan officer consented to the OCC's order for prohibition and for restitution payments of \$38,000 to the bank, and the assessment of a \$25,000 civil money penalty. *In the Matter of Brian Stull, Integra Bank, N.A., Evansville, IN*, Enforcement Action No. 2004-66 (June 7, 2004).

F. Fast Track Enforcement Cases

The OCC continued its Fast Track Enforcement program, initiated in 1996, which ensures that bank insiders who have engaged in criminal acts in banks, but who are not being criminally prosecuted, are prohibited from working in the banking industry. As part of the Fast Track Enforcement program, the OCC secured 22 consent prohibition orders against institution-affiliated parties during 2004. Eight of these orders incorporated restitution to the appropriate bank for losses incurred, and two of the orders incorporated civil money penalties. During the same period, the OCC sent out notifications to 231 former bank employees who were convicted of crimes of dishonesty, informing them that under federal law they are prohibited from working again in a federally insured depository institution.