Failed Bank Review

The Enloe State Bank | Cooper, Texas

September 2019 **FBR-19-001**

☆☆☆☆☆☆☆☆

Federal Deposit Insurance Corporation
Office of Inspector General
Office of Program Audits and Evaluations

Date: September 23, 2019

Memorandum To: Doreen R. Eberley
Director, Division of Risk Management Supervision

/Signed/

From: Terry L. Gibson
Assistant Inspector General for Program Audits and Evaluations

Subject **Failed Bank Review Memorandum** | The Enloe State Bank | Cooper, Texas | FBR-19-001

Background

On May 31, 2019, the Texas Department of Banking (TDB) closed The Enloe State Bank (Enloe or Bank) and appointed the Federal Deposit Insurance Corporation (FDIC) as receiver. According to the FDIC's Division of Finance, the estimated loss to the Deposit Insurance Fund (DIF) at the time of failure was $27.6 million, or 75 percent of the Bank's $37.0 million in total assets. According to TDB's Closing Order, the Enloe Board of Directors resolved to voluntarily close the Bank and place it with TDB for liquidation consistent with state law.[1]

Enloe was a $37.0 million, state-chartered nonmember institution that operated in a single location in Cooper, Texas. The Bank had been FDIC-insured since 1934 and historically focused on agricultural lending and residential mortgages. Enloe was wholly-owned by Entex Bancshares, Inc. a shell, one-bank holding company.

This Memorandum examines whether the subject bank failure warrants an in-depth review.[2]

Causes of Failure

According to the May 31, 2019, TDB Press Release, it was forced to close the Bank due to insider abuse and fraud by former officers. Based on our review of key FDIC documents, the Bank's Board of Directors' (Board) failed to establish adequate corporate governance to monitor and control

[1] Tex. Fin. Code. Ann. § 36.201(b) (2007).
[2] When the DIF incurs a loss under $50 million, the Federal Deposit Insurance Act requires the Inspector General of the appropriate federal banking agency to determine the grounds upon which the state or federal banking agency appointed the FDIC as receiver and whether any unusual circumstances exist that might warrant an in-depth review of the loss. 12 U.S.C. § 1831*o*(k) (2010).

management's activities, including those of a dominant bank President.[3] The inadequate governance structure resulted in the origination of a large number of irregular loans (allegedly fraudulent and fictitious). The losses associated with these loans depleted Enloe's capital levels and the Board was unable to obtain additional capital to restore the Bank to health.

FDIC Supervision

Historically, Enloe received satisfactory ratings. In April 2018, examiners downgraded Enloe from a composite "1" to a "2" based on a "3" component **Management** rating.[4] The April 2018 FDIC examination report included Matters Requiring Board Attention (MRBA). MRBAs are supervisory recommendations involving an issue or risk of significant importance and that would typically require more effort to address than those correctable in the normal course of business. The MRBAs included in the examination report noted that the Bank was not in conformance with established safety and soundness standards in the areas of internal controls, management information systems, and internal audit. For instance, the Board was expected to ensure that the external audit scheduled for 2018 be a full financial statement audit with an attestation of the Bank's internal routines and controls. Following the April 2018 examination, the FDIC followed up regularly with Enloe to monitor the Board's efforts to address the outstanding MRBAs.

Enloe failed to respond adequately to the MRBAs related to external audit and internal control matters, causing supervisory activity to escalate from March to May 2019. Specifically, in March 2019, the Bank had not provided the FDIC Dallas Regional Office with an external audit report of the Bank's financial statements, including an attestation of the Bank's internal controls, or an IT audit report as required by the MRBAs. On May 8, 2019, the TDB provided the FDIC a draft of the Bank's audit. The draft document only provided an independent review of certain internal controls as well as a reconciliation of certain general ledger accounts rather than a full financial statement audit as required. The TDB was scheduled to start a state-only examination of Enloe on May 13, 2019, but a suspicious fire occurred the preceding weekend, resulting in the Bank's temporary closure due to fire damage. Given the unfolding circumstances, the FDIC informed TDB that it would like to participate on the examination, which began on May 16, 2019. TBD welcomed the FDIC's participation. On May 24, 2019, examiners downgraded the Bank to a "5" and designated it a troubled institution based on the ongoing examination, which identified significant losses associated with over 100 fraudulent and/or fictitious loans. The FDIC and TDB also notified Enloe that it had become *Critically Undercapitalized*.[5] Given the Board was unable to recapitalize the Bank, it voluntarily agreed to close on May 31, 2019.

---

[3] In conducting this review we assessed key documents related to Enloe's failure, including the Division of Risk Management Supervision's (RMS) *Supervisory History* and the Division of Resolutions and Receiverships' *Failing Bank Case*. This review does not constitute an audit conducted in accordance with Generally Accepted Government Auditing Standards.

[4] Financial institution regulators evaluate a bank's performance in six components represented by the CAMELS acronym: **C**apital adequacy, **A**sset quality, **M**anagement practices, **E**arnings performance, **L**iquidity position, and **S**ensitivity to market risk. Examiners assign each CAMELS component and an overall, composite score, a rating of "1" (strong) through "5" (critically deficient), with "1" having the least regulatory concern and "5" having the greatest concern.

[5] FDIC regulation specifies five capital levels for banks ranging from *Well Capitalized* to *Critically Undercapitalized*. 12 C.F.R. Part 324 (2018).

Conclusion

We have determined that proceeding with an in-depth review of the loss is warranted given the extent of irregular loans and the extraordinarily high estimated loss rate (75 percent). Performing an in-depth review will provide an opportunity to further evaluate the cause of failure and the FDIC's supervision of the Bank to determine whether there are any lessons to be learned from this failure. We plan to complete the in-depth review within 6 months of announcing that engagement.