

FEDERAL DEPOSIT INSURANCE CORPORATION  
WASHINGTON, D.C.

and

TEXAS DEPARTMENT OF BANKING  
AUSTIN, TEXAS

_____ )	
In the Matter of )	CONSENT ORDER
FIRST STATE BANK )	
MESQUITE, TEXAS )	FDIC-10-814b
(Insured State Nonmember Bank) )	COMMISSIONER ORDER No. 2010-062
_____ )	

The Federal Deposit Insurance Corporation (“FDIC”) is the appropriate Federal banking agency for First State Bank, Mesquite, Texas (“Bank”), under 12 U.S.C. § 1813(q).

The Texas Department of Banking (“Department”) is the appropriate state banking agency for the Bank under Texas Finance Code, Title 3, Subtitle A §§ 31.001 et. seq.

The Bank, by and through its duly elected and acting board of directors (“Board”), has executed a “STIPULATION TO THE ISSUANCE OF A CONSENT ORDER” (“STIPULATION”), dated December 15, 2010, that is accepted by the FDIC and the Banking Commissioner of Texas (“Commissioner”).

With the Stipulation, the Bank has consented, without admitting or denying any charges of unsafe or unsound banking practices and violations of law or regulation relating to loan administration, excessive levels of low quality assets, deficient earnings, and inadequate levels and methodology of the allowance for loan and lease losses (“ALLL”), to the issuance of this CONSENT ORDER (“ORDER”) by the Acting Regional Director of the FDIC’s Dallas Regional Office (“Regional Director”) and the Commissioner.

Having determined that the requirements for issuance of an order under 12 U.S.C. § 1818(b) and Texas Finance Code § 35.002 have been satisfied, the FDIC and the Commissioner hereby order that:

**MANAGEMENT – BOARD SUPERVISION**

1. Within 30 days after the effective date of this ORDER, the Bank’s Board shall increase its participation in the affairs of the Bank by assuming full responsibility for the approval of the Bank’s policies and objectives and for the supervision of the Bank’s management, including all the Bank’s activities. The Board’s participation in the Bank’s affairs shall include, at a minimum, monthly meetings in which the following areas shall be reviewed and approved by the Board: reports of income and expenses; new, overdue, renewed, insider, charged-off, delinquent, nonaccrued, and recovered loans; investment activities; operating policies; and individual committee actions. The Bank’s Board minutes shall document the Board’s reviews and approvals, including the names of any dissenting directors.

**MANAGEMENT CLAUSE – STAFFING STUDY**

2. (a) Within 30 days after the effective date of this ORDER, the Bank shall retain a bank consultant acceptable to the Regional Director and the Commissioner. The consultant 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.

(b) The Bank shall provide the Regional Director and the Commissioner with a copy of the proposed engagement letter or contract with the consultant for review before it is executed. The contract or engagement letter, at a minimum, should include:

- (1) A description of the work to be performed under the contract or engagement letter;
- (2) The responsibilities of the consultant;
- (3) An identification of the professional standards covering the work to be performed;
- (4) Identification of the specific procedures to be used when carrying out the work to be performed;
- (5) The qualifications of the employee(s) who are to perform the work;
- (6) The time frame for completion of the work;
- (7) Any restrictions on the use of the reported findings; and
- (8) A provision for unrestricted examiner access to work papers.

(c) The Management Plan shall be developed within 90 days after the effective date of this ORDER. The Management Plan shall include, at a minimum:

- (1) Identification of both the type and number of officer positions needed to properly manage and supervise the affairs of the Bank;
- (2) Identification and establishment of such Bank committees as are needed to provide guidance and oversight to active management;
- (3) 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

- (4) 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 in the Management Plan.

(d) The Management Plan shall be submitted to the Regional Director and the Commissioner for review and comment upon its completion. Within 30 days from the receipt of any comments from the Regional Director and the Commissioner, and after the adoption of any recommended changes, the Bank shall approve the Management Plan and record its approval in the Board's meeting minutes. Thereafter, the Bank, its directors, officers, and employees shall implement and follow the Management Plan and/or any subsequent modification.

### **LOAN UNDERWRITING AND ADMINISTRATION**

3. (a) Within 90 days of the issuance of this ORDER, the Bank shall employ and retain a qualified executive officer with loan collection, loan administration and loan workout expertise. The executive officer must be acceptable to the Texas Department of Banking and the FDIC pursuant to Section 32 of the Federal Deposit Insurance Act, 12 U.S.C § 1831i and Part 303, subpart F, of the FDIC Rules and Regulations, 12 C.F.R. Part 303, Subpart F.

(b) Within 10 days after the effective date of this ORDER, the Bank shall improve loan underwriting and administration practices by ensuring adherence to the Bank's

Loan Policy. Pursuant to the Bank's Loan Policy the Board will take all necessary steps, including but not limited to:

- (1) Ensuring that collateral valuations are prepared pursuant to Uniform Standards of Professional Appraisal practice and are current;
- (2) Ensuring that problems are recognized in a timely manner, evidenced by proper loan grading and timely charge-offs as appropriate;
- (3) The cessation of converting overdrawn deposit accounts into loan renewals without proper approval;
- (4) Ensuring effective financial monitoring by receipt of complete and current financial information and collateral inspections;
- (5) Implementing a formal process to evaluate loans for troubled debt restructuring status;
- (6) Ensuring an effective independent loan review which results in appropriate and timely loan grading;
- (7) Establishing a formal loan workout and collections structure which is led by an executive officer dedicated to that purpose whose function is to develop and implement workout strategies on larger commercial and commercial real estate credits. The Board should closely monitor this function monthly and ensure that appropriate resources are available.

## **CLASSIFIED ASSETS - CHARGE-OFF AND PLAN FOR REDUCTION**

4. (a) Within 10 days after the effective date of this ORDER, the Bank shall, to the extent that it has not previously done so, eliminate from its books, by charge-off or collection, all assets or portions of assets classified Loss by the FDIC or the Department as a result of its examination of the Bank as of July 26, 2010. Elimination or reduction of these assets through proceeds of loans made by the Bank shall not be considered "collection" for the purpose of this paragraph.

(b) Within 90 days after the effective date of this ORDER, the Bank shall submit a written plan to the Regional Director and the Commissioner to reduce the remaining assets classified Doubtful and Substandard as of July 26, 2010. The plan shall address each asset so classified with a balance of \$250,000 or greater and provide the following:

- (1) The name under which the asset is carried on the books of the Bank;
- (2) Type of asset;
- (3) Actions to be taken in order to reduce the classified asset; and
- (4) Time frames for accomplishing the proposed actions.

The plan shall also include, at a minimum:

- (1) Review of the financial position of each such borrower, including the source of repayment, repayment ability, and alternate repayment sources; and
- (2) Evaluation of the available collateral for each such credit, including possible actions to improve the Bank's collateral position.

In addition, the Bank's plan shall contain a schedule detailing the projected reduction of total classified assets on a quarterly basis. Further, the plan shall contain a provision requiring the submission of monthly progress reports to the Bank's Board and a provision mandating a review by the Bank's Board.

(c) The Bank shall present the plan to the Regional Director and the Commissioner for review. Within 30 days after the Regional Director's and the Commissioner's response, the plan, including any requested modifications or amendments, shall be adopted by the Bank's Board, which approval shall be recorded in the Bank's Board meeting minutes. The Bank shall then immediately initiate measures detailed in the plan to the extent such measures have not been initiated.

(d) For purposes of the plan, the reduction of adversely classified assets as of July 26, 2010 shall be detailed using quarterly targets expressed as a percentage of the Bank's Tier 1 Capital plus the Bank's ALLL and may be accomplished by:

- (1) Charge-off;
- (2) Collection;
- (3) Sufficient improvement in the quality of adversely classified assets so as to warrant removing any adverse classification, as determined by the FDIC or the Department; or
- (4) Increase in the Bank's Tier 1 Capital.

(e) While this ORDER is in effect, the Bank shall eliminate from its books, by charge-off or collection, all assets or portions of assets classified Loss as determined at any future examination conducted by the FDIC or the Department.

**ALLOWANCE FOR LOAN AND LEASE LOSSES**  
**AND**  
**AMENDED CONSOLIDATED REPORTS OF CONDITIONS AND INCOME**

5. (a) Within 30 days after the effective date of this ORDER, the Bank shall make provisions to its ALLL in an amount of at least \$1,753,000 if not already provided. The allowance should be funded by charges to current operating income and should be calculated in accordance with generally accepted accounting standards and ALLL supervisory guidance. After the initial provision is made, the Bank shall thereafter maintain a reasonable ALLL. Prior to the end of each calendar quarter, the Bank's Board shall review the adequacy of the Bank's ALLL. Such reviews shall include, at a minimum, the Bank's loan loss experience, an estimate of potential loss exposure in the portfolio, trends of delinquent and non-accrual loans and prevailing and prospective economic conditions. The minutes of the Bank's Board meetings at which such reviews are undertaken shall include complete details of the reviews and the resulting recommended increases in the ALLL.

(b) Within 30 days after the effective date of this ORDER, the Bank shall review Consolidated Reports of Condition and Income ("Call Reports") filed with the FDIC on or after December 31, 2009, and amend said reports, if necessary, to accurately reflect the financial condition of the Bank as of the date of each such report. In particular, such reports shall contain a reasonable ALLL. Reports filed after the effective date of this ORDER shall also accurately reflect the financial condition of the Bank as of the reporting date.

(c) The Bank must use Financial Accounting Standards Board Statements Numbers 5 and 114 for determining the Bank's ALLL reserve adequacy. Provisions for loan losses must be based on the inherent risk in the Bank's loan portfolio. The Board must document with written reasons any decision not to require provisions for loan losses in the Board minutes.

## **OVERDRAFT POLICY**

6. (a) Within 30 days after the effective date of this ORDER, the Bank's Board shall establish a written policy governing extensions of credit in the form of customer deposit account overdrafts. The overdraft policy shall, at a minimum, prohibit converting overdrawn deposit accounts into loan renewals without proper approval and establish a dollar amount and a time period for extending such credit without the prior approval of the Bank's loan committee or the Bank's Board.

(b) The Bank shall submit the foregoing overdraft policy to the Regional Director and the Commissioner for comment. After the Regional Director and the Commissioner have responded to the overdraft policy, the Bank's Board shall adopt the overdraft policy as amended or modified by the Regional Director and the Commissioner. The overdraft policy will be implemented immediately to the extent that it is not already in effect at the Bank.

## **BUDGET AND PROFIT PLAN**

7. (a) Within 45 days after the effective date of this ORDER, the Bank shall formulate and submit to the Regional Director and the Commissioner for review and comment a written profit plan and a realistic, comprehensive budget for all categories of income and expense for calendar year 2011. The plan required by this paragraph shall contain formal goals and strategies, be consistent with sound banking practices, reduce discretionary expenses, improve the Bank's overall earnings and net interest income, and shall contain a description of the operating assumptions that form the basis for major projected income and expense

components. The written profit plan shall also address an analysis of the Bank's pricing structure.

(b) Within 30 days after the end of each calendar quarter following completion of the profit plan and budget required by this paragraph, the Bank's Board shall evaluate the Bank's actual performance in relation to the written profit plan and budget, record the results of the evaluation, and note any actions taken by the Bank in the minutes of the Board meeting when such evaluation is undertaken.

(c) A written profit plan and budget shall be prepared for each calendar year for which this ORDER is in effect and shall be submitted to the Regional Director and the Commissioner for review and comment within 30 days after the end of each year. Within 30 days after receipt of all such comments from the Regional Director and the Commissioner and after adoption of any recommended changes, the Bank shall approve the written profit plan and budget, which approval shall be recorded in the minutes of a Board meeting. Thereafter, the Bank shall implement and follow the plan.

### **STRATEGIC PLAN**

8. (a) Within 90 days after the effective date of this ORDER, the Bank shall prepare and adopt a comprehensive strategic plan. The strategic plan required by this paragraph shall contain an assessment of the Bank's current financial condition and market area, and a description of the operating assumptions that form the basis for major projected income and expense components.

- (b) The written strategic plan shall address, at a minimum:
- (1) Strategies for pricing policies and asset/liability management;
  - (2) Plans for sustaining adequate liquidity, including back-up lines of credit to meet any unanticipated deposit withdrawals;
  - (3) Goals for reducing problem loans;
  - (4) Plans for attracting and retaining qualified individuals to fill vacancies in the lending and accounting functions;
  - (5) Financial goals, including pro forma statements for asset growth, capital adequacy, and earnings; and
  - (6) Formulation of a mission statement and the development of a strategy to carry out that mission.

(c) The Bank shall submit the strategic plan to the Regional Director and the Commissioner for review and comment. After consideration of all such comments, the Bank shall approve the plan, which approval shall be recorded in the minutes of the Bank's Board meeting. Thereafter, the Bank shall implement and follow the strategic plan.

(d) Within 30 days after the end of each calendar quarter following the effective date of this ORDER, the Bank's Board shall evaluate the Bank's performance in relation to the strategic plan required by this paragraph and record the results of the evaluation, and any actions taken by the Bank, in the minutes of the Bank's Board meeting at which such evaluation is undertaken.

(e) The strategic plan required by this ORDER shall be revised and submitted to the Regional Director and the Commissioner for review and comment 30 days after the end of each calendar year for which this ORDER is in effect. Within 30 days after receipt of all such

comments from the Regional Director and the Commissioner, and after consideration of all such comments, the Bank shall approve the revised plan, which approval shall be recorded in the minutes of the Bank's Board meeting. Thereafter, the Bank shall implement the revised plan.

### **CAPITAL MAINTENANCE**

9. (a) Within 30 days after the effective date of this ORDER and while this ORDER is in effect, the Bank, after establishing an ALLL, shall maintain its Tier 1 Leverage Capital ratio equal to or greater than 9 percent of the Bank's Average Total Assets; shall maintain its Tier 1 Risk-Based Capital ratio equal to or greater than 11 percent of the Bank's Total Risk-Weighted Assets; and shall maintain its Total Risk-Based Capital ratio equal to or greater than 13 percent of the Bank's Total Risk Weighted Assets.

(b) If any such capital ratios are less than required by the ORDER, as determined as of the date of any Call Report or at an examination by the FDIC or the Department, the Bank shall, within 30 days after receipt of a written notice of the capital deficiency from the Regional Director or the Commissioner, present to the Regional Director and the Commissioner a plan to increase the Bank's Tier 1 Capital or to take such other measures to bring all the capital ratios to the percentages required by this ORDER. After the Regional Director and the Commissioner respond to the plan, the Bank's Board shall adopt the plan, including any modifications or amendments requested by the Regional Director and the Commissioner.

Part of the capital plan must include a contingency plan in the event that the Bank (i) fails to maintain the minimum capital ratios required by the ORDER, (ii) fails to submit an acceptable capital plan or (iii) fails to implement or adhere to a capital plan to which no written

objection was provided by the Regional Director or Commissioner. Said contingency plan shall include a plan to sell or merge the Bank. The Bank shall implement the contingency plan upon written notice from the Regional Director and the Commissioner.

(c) Thereafter, to the extent such measures have not previously been initiated, the Bank shall immediately initiate measures detailed in the plan, to increase its Tier 1 Capital by an amount sufficient to bring all the Bank's capital ratios to the percentages required by this ORDER within 30 days after the Regional Director and the Commissioner respond to the plan. Such increase in Tier 1 Capital and any increase in Tier 1 Capital necessary to meet the capital ratios required by this ORDER may be accomplished by:

- (1) The sale of securities in the form of common stock; or
- (2) The direct contribution of cash subsequent to July 26, 2010, by the directors and/or shareholders of the Bank or by the Bank's holding company; or
- (3) Receipt of an income tax refund or the capitalization subsequent to July 26, 2010, of a bona fide tax refund certified as being accurate by a certified public accounting firm; or
- (4) Any other method approved by the Regional Director and the Commissioner.

(d) If all or part of the increase in Tier 1 Capital required by this ORDER is to be accomplished by the sale of new securities, the Bank's Board shall adopt and implement a plan for the sale of such additional securities, including soliciting proxies and the voting of any shares or proxies owned or controlled by them in favor of the plan. Should the implementation of the plan involve a public distribution of the Bank's securities (including a distribution limited

only to the Bank's existing shareholders), the Bank shall prepare 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 Federal 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 plan and any materials used in the sale of the securities shall be submitted to the FDIC, Accounting and Securities Disclosure Section, Washington, D.C. 20429, for review. Any changes requested to be made in the plan or the materials by the FDIC shall be made prior to their dissemination. If the increase in Tier 1 Capital is to be provided by the sale of non-cumulative perpetual preferred stock, then all terms and conditions of the issue shall be presented to the Regional Director and the Commissioner for prior approval.

(e) In complying with the provisions of this ORDER and until such time as any such public offering is terminated, the Bank shall provide to any subscriber and/or purchaser of the Bank's securities written notice of any planned or existing development or other change which is materially different from the information reflected in any offering materials used in connection with the sale of the Bank's securities. The written notice required by this paragraph shall be furnished within 10 days after the date such material development or change was planned or occurred, whichever is earlier, and shall be furnished to every purchaser and/or subscriber who received or was tendered the information contained in the Bank's original offering materials.

(f) In addition, the Bank shall comply with the FDIC's Statement of Policy on Risk-Based Capital found in Appendix A to Part 325 of the FDIC's Rules and Regulations, 12 C.F.R. Part 325, App. A.

(g) For purposes of this ORDER, all terms relating to capital shall be calculated according to the methodology set forth in Part 325 of the FDIC's Rules and Regulations, 12 C.F.R. Part 325.

### **DIVIDEND RESTRICTION**

10. 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 the Commissioner.

### **CORRECTION OF VIOLATIONS**

11. (a) Within 30 days after the effective date of this ORDER, the Bank shall initiate action to eliminate and/or correct all violations of law and regulation noted in the Report of Examination.

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

(c) Within 30 days after the effective date of this ORDER, the Bank shall address any contraventions of policy noted in the Report of Examination.

### **COMPLIANCE COMMITTEE**

12. Within 30 days after the effective date of this ORDER, the Bank's Board shall establish a committee of the board of directors charged with the responsibility of ensuring that the Bank complies with the provisions of this ORDER. At least two of the members of such committee shall be directors not employed in any capacity by the Bank other than as a director.

The committee shall report monthly to the entire Bank's Board, and a copy of the report and any discussion related to the report or the ORDER shall be included in the Bank's Board meeting minutes. The establishment of this committee shall not diminish the responsibility or liability of the entire Bank's Board to ensure compliance with the provisions of this ORDER.

### **SHAREHOLDER NOTIFICATION**

13. 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.

### **PROGRESS REPORTS**

14. 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.

The provisions of this ORDER shall not bar, stop, or otherwise prevent the FDIC, the Department, or any other federal or state agency or department from taking any other action against the Bank or any of the Bank's current or former institution-affiliated parties.

This ORDER shall be effective on the date of issuance.

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 provision has been modified, terminated, suspended, or set aside by the FDIC and the Commissioner.

This ORDER is signed by the FDIC Dallas Regional Director, pursuant to delegated authority.

Issued and made effective this 15th day of December 2010.

/s/ \_\_\_\_\_  
Kristie K. Elmquist  
Acting Regional Director  
Dallas Region  
Division of Supervision and Consumer Protection  
Federal Deposit Insurance Corporation

/s/ \_\_\_\_\_  
Charles G. Cooper  
Commissioner  
Texas Department of Banking