



Audit Report



OIG-12-059

SAFETY AND SOUNDNESS: Failed Bank Review of Charter
National Bank and Trust, Hoffman Estates, Illinois

July 20, 2012

**Office of
Inspector General**

DEPARTMENT OF THE TREASURY



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

OFFICE OF
INSPECTOR GENERAL

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MEMORANDUM FOR THOMAS J. CURRY
COMPTROLLER OF THE CURRENCY

FROM: Jeffrey Dye /s/
Director, Banking Audits

SUBJECT: Failed Bank Review of Charter National Bank and Trust

This memorandum presents the results of our review of the failure of Charter National Bank and Trust (Charter) located in Hoffman Estates, Illinois. Charter opened in July 1980 and operated a main office and a branch office in Hoffman Estates. The bank was wholly owned by Hanover Bank Corporation, Hanover Park, Illinois, a one-bank holding company. The Office of the Comptroller of the Currency (OCC) closed Charter and appointed the Federal Deposit Insurance Corporation (FDIC) as receiver on February 10, 2012. As of December 31, 2011, the bank had \$93.9 million in total assets. As of June 30, 2012, FDIC estimated that the loss to the Deposit Insurance Fund is \$20.4 million.

Because the loss to the Deposit Insurance Fund is less than \$150 million, as set forth by section 38(k) of the Federal Deposit Insurance Act (FDIA), we conducted a review of the failure of Charter that was limited to (1) ascertaining the grounds identified by OCC for appointing FDIC as receiver and (2) determining whether any unusual circumstances exist that might warrant a more in-depth review of the loss. In performing our review we (1) examined documentation related to the appointment of FDIC as receiver and (2) interviewed an OCC problem bank specialist. We performed our fieldwork from February to April 2012.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Causes of Charter National Bank and Trust's Failure

OCC appointed FDIC receiver primarily on the following grounds: (1) Charter was in an unsafe or unsound condition to transact business, (2) the bank had experienced substantial dissipation of assets or earnings due to unsafe or unsound practices, (3) the bank had incurred or was likely to incur losses that would deplete all or substantially all of its capital and there was no reasonable prospect for it to become adequately capitalized without federal assistance, (4) the bank's unsafe or unsound practices or condition were likely to seriously prejudice the interests of the Deposit Insurance Fund and (5) the bank was critically undercapitalized.

The primary cause of Charter's failure was its focus on commercial lending which, when combined with weak credit risk management practices, led to a concentration of commercial real estate loans in the bank's market area. Credit risk management weaknesses included inadequate monitoring of credit concentrations, poor underwriting, and poor problem loan identification practices. The underwriting and subsequent poor performance of commercial loan participations purchased from Western Springs National Bank and Trust (Western Springs) were particular concerns. Western Springs was a failed institution¹ where Charter's Chairman and his family had a significant financial interest and where the Chairman and members of his family, including Charter's President, served as directors. Beginning in 2007, economic deterioration within the markets that Charter served resulted in the deterioration of Charter's asset quality. This led to increased credit losses, declining capital levels and, ultimately, failure.

During our review, we noted that OCC had opened an Order of Investigation into certain questionable activities by Charter's management. We referred these matters to the Treasury Inspector General's Office of Investigation.

¹ OCC closed Western Springs National Bank and Trust and appointed FDIC as receiver on April 8, 2011. As of June 30, 2012, FDIC estimated the loss to the Deposit Insurance Fund from the failure of Western Springs to be \$44.5 million. Treasury OIG conducted a failed bank review of Western Springs and issued audit report on September 14, 2011 (*Safety and Soundness: Failed Bank Review of Western Springs National Bank and Trust, Western Springs, Illinois*, OIG-11-099). We reported that the primary cause of Western Spring's failure was its pursuit of a growth strategy that resulted in significant commercial real estate concentrations, combined with poor credit administration and risk management practices. Deficiencies included very liberal underwriting practices, ineffective problem loan identification and loan review processes, and weaknesses in the collateral valuation process. The poor performance of loan participations purchased from Mutual Bank, Harvey, Illinois, a failed institution where Western Spring's Chairman served as Vice Chairman, was also a factor in the bank's failure.

Conclusion

Based on our review of the causes of Charter's failure and the grounds identified by OCC for appointing FDIC as receiver, we determined that there were no unusual circumstances surrounding the bank's failure that would necessitate an in-depth review. We provided a draft of this memorandum to OCC management for comment. In its response, OCC stated that it agreed with our conclusion as to the causes of failure of Charter and that it had no concerns with our determination that an in-depth review of the bank's failure is not warranted. The response is provided as Attachment 1. A list of the recipients of this memorandum is provided as Attachment 2.

We appreciate the courtesies and cooperation provided to our staff during the audit. If you have any questions, you may contact me at (202) 927-0384 or James Lisle, Audit Manager, at (202) 927-6345.

Attachments

Attachment 1
Management Response

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MEMORANDUM

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

To: Jeffrey Dye, Banking Audits

From: Thomas J. Curry, Comptroller of the Currency /s/

Date: July 17, 2012

Subject: Response to Failed Bank Review of Charter National Bank and Trust

We have received and reviewed your draft report titled “Failed Bank Review of Charter National Bank and Trust” (Charter) located in Hoffman Estates, Illinois. The loss to the Deposit Insurance Fund is less than \$150 million, therefore, as set forth by section 38(k) of the Federal Deposit Insurance Act, you conducted a review of the failure of Charter that was limited to: (1) ascertaining the grounds identified by the OCC for appointing the FDIC as receiver and, (2) determining whether any unusual circumstances exist that might warrant a more in-depth review of the loss. In performing your review you (1) examined documentation related to the appointment of FDIC as receiver, and (2) interviewed an OCC problem bank specialist.

You conducted your audit during February to April 2012 in accordance with generally accepted government auditing standards. Those standards require that you plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for your findings and conclusions. You believe that the evidence obtained provides a reasonable basis for your findings and conclusions.

You concluded that the primary cause of Charter’s failure was its focus on commercial lending which, when combined with weak credit management practices, led to a concentration of commercial real estate loans in the bank’s market area. We agree.

You determined that there were no unusual circumstances surrounding the bank’s failure. As a result, you determined that a more in-depth review of the bank’s failure by the OIG is not warranted. We have no concerns with your determination.

Thank you for the opportunity to review and comment on your draft report. If you need additional information, please contact Jennifer Kelly, Senior Deputy Comptroller for Midsize and Community Bank Supervision, at 202-874-5020.

Department of the Treasury

Deputy Secretary
Office of Strategic Planning and Performance Management
Office of the Deputy Chief Financial Officer, Risk and Control
Group

Office of the Comptroller of the Currency

Comptroller of the Currency
Liaison Officer

Office of Management and Budget

OIG Budget Examiner