Audit Report

OIG-10-044

SAFETY AND SOUNDNESS: Material Loss Review of Vineyard Bank, National Association

July 13, 2010

Office of Inspector General

Department of the Treasury

Contents

Abbreviations

ALLL	allowance for loan and lease losses
CEO	chief executive officer
CRA	Community Reinvestment Act

CRE	commercial real estate
DFI	California Department of Financial Institutions
FHLB	Federal Home Loan Bank
FDIC	Federal Deposit Insurance Corporation
IT	information technology
MOU	memorandum of understanding
MRA	matter requiring attention
OCC	Office of the Comptroller of the Currency
OIG	Office of Inspector General
PCA	prompt corrective action
ROE	report of examination

OIG

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Comptroller of the Currency

This report presents the results of our review of the failure of Vineyard Bank, N.A. (Vineyard), headquartered in Corona, California, and of the Office of the Comptroller of the Currency's (OCC) supervision of the institution. OCC approved Vineyard's conversion from a state-chartered bank to a national bank in May 2006. OCC closed Vineyard and appointed the Federal Deposit Insurance Corporation (FDIC) as receiver just over 3 years later on July 17, 2009. Section 38(k) of the Federal Deposit Insurance Act mandated this review because of the magnitude of the loss to the Deposit Insurance Fund resulting from Vineyard's failure.[1] As of December 31, 2009, FDIC estimated that the loss to the Deposit Insurance Fund would be $597 million.

Our objectives were to determine the causes of Vineyard's failure and assess OCC's supervision of the bank, including implementation of the prompt corrective action (PCA) provisions of section 38(k). To accomplish these objectives, we reviewed the supervisory files and interviewed key OCC and FDIC officials. We conducted our fieldwork from August 2009 through February 2010. Appendix 1 contains a more detailed description of our material loss review objectives, scope, and methodology.

We have also included several other appendices to this report. Appendix 2 contains background information on Vineyard and OCC's supervision and enforcement processes. Appendix 3 is a glossary of terms used in this report. These terms are underlined and, in the electronic version of the report on our Web site,

[1] Section 38(k) defines a loss as material if it exceeds the greater of $25 million or 2 percent of the institution's total assets.

hyperlinked to the glossary. Appendix 4 contains a chronology of significant events related to the bank's history and OCC's supervision of the institution. Appendix 5 provides bank examination results and information on enforcement actions. Appendix 6 shows recommendations by the Treasury Office of Inspector General (OIG) from material loss reviews of failed OCC-regulated institutions completed since November 2008.

Results in Brief

Vineyard failed because of significant losses in its commercial real estate (CRE) loan portfolio, which included loans for CRE mortgages, residential tract construction, land development, and commercial building. Vineyard reported that its net operating losses exceeded $31 million in 2007 and $127 million in 2008.

Vineyard pursued an aggressive growth strategy beginning in 2001. Its total assets grew by more than $1.9 billion from 2001 through 2007. Vineyard's rapid growth during this time was largely attributable to an increase and high concentration in CRE mortgages, and construction and land development loans. While pursuing this rapid growth, Vineyard's board and management did not adequately control concentration risk or ensure that credit underwriting and administrative controls were adequate. The weak controls led to deterioration in underwriting standards, including the failure to perform adequate financial analysis of borrowers, and the origination of high-risk loans, such as nonrecourse loans, and loans with high loan-to-value ratios. These deficiencies were made worse by the decline in the real estate market and borrowers' inability to pay off loans as they matured. A majority of these loans were for properties located in southern California, which experienced a significant decline in real estate values during this period.

OCC's supervision of Vineyard did not prevent a material loss to the Deposit Insurance Fund. In May 2006, OCC approved Vineyard's conversion to a nationally chartered bank after OCC conducted a preconversion examination to determine if the bank's application for charter conversion should be approved. During the examination, OCC examiners identified significant concerns with Vineyard's high concentration in CRE loans. Because of the significant weaknesses identified by OCC examiners during the preconversion examination, we believe that OCC should have deferred approval of Vineyard's conversion to a nationally chartered bank until those weaknesses had been addressed.

In April 2007, during OCC's first full scope examination after conversion, OCC again identified concerns with Vineyard's large concentration in CRE loans but did not include any matters requiring attention (MRA) instructing the bank to reduce its high-risk concentration. In its reports of examination (ROE) for the 2006 preconversion examination and the 2007 full scope examination, OCC assigned Vineyard a CAMELS composite rating of 2. OCC did not take forceful action until July 2008, when it downgraded Vineyard's CAMELS composite rating to a 4 and entered into a consent order with the bank. By that time, however, Vineyard's problems had become too large and too severe for the bank to resolve.

We concluded that as Vineyard's capital levels fell due to the significant losses in its CRE loan portfolio, OCC imposed the required restrictions and directives under the PCA provisions. The PCAs, however, did not prevent Vineyard's failure or a material loss to the Deposit Insurance Fund.

Vineyard is the second OCC failed bank we reviewed where the bank failed within a relatively short timeframe after it was converted to a nationally chartered bank.[2] Based on our review of the Vineyard charter conversion process, we reaffirm our prior recommendations that OCC (1) determine that banks seeking conversions satisfactorily address significant deficiencies before approval and (2) formalize its process for second level reviews of charter conversions. We are not making any new recommendations from our material loss review of Vineyard.

In a written response, OCC acknowledged our reaffirmation of the two prior recommendations relating to the charter conversion process. OCC also stated that appropriate steps have been taken to

[2] The first failed bank where we reported on charter conversion issues was Silverton Bank, N.A. (OIG, *Safety and Soundness: Material Loss Review of Silverton Bank, N.A.,* OIG-10-033 (Jan. 22, 2010)).

address the recommendations. OCC's full response is provided as Appendix 7.

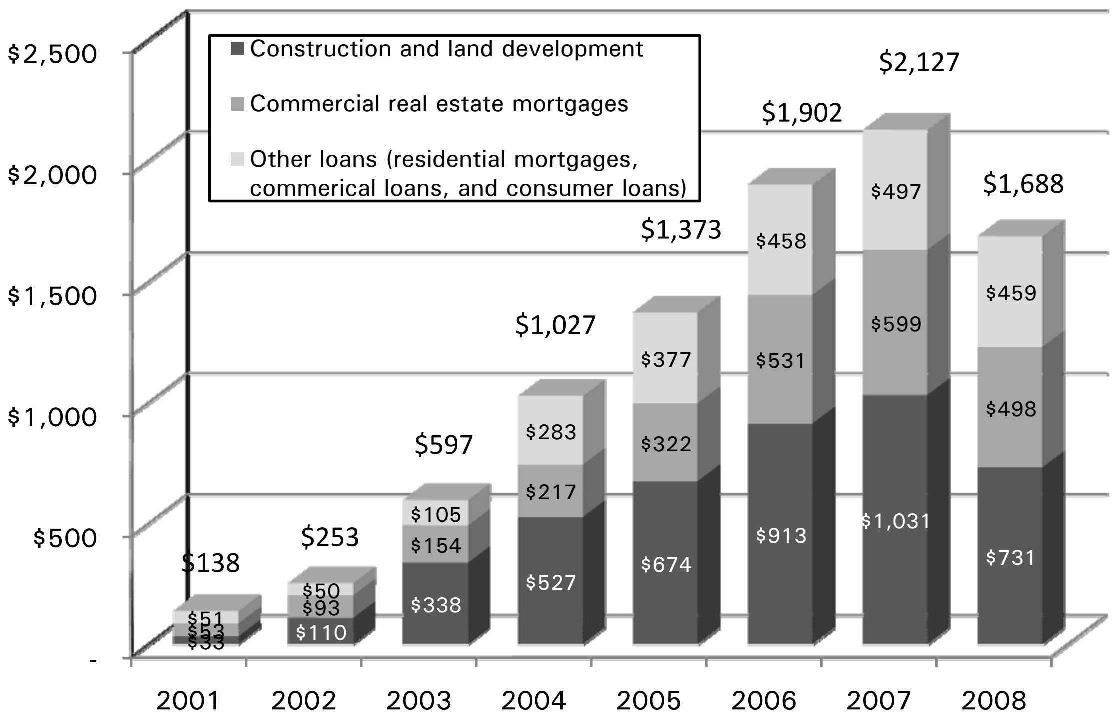
Causes of Vineyard's Failure

Vineyard's failure resulted primarily from significant losses in its CRE loan portfolio. The bank's operating losses exceeded $31 million in 2007 and $127 million in 2008. Beginning in 2001, Vineyard's board and management pursued an aggressive growth strategy designed to increase the bank's assets but, ultimately did not sufficiently control concentration risk or ensure that adequate controls were implemented for CRE lending, including controls over credit underwriting and administration. The effects of Vineyard's inadequate controls over concentration risk, credit underwriting, and administration were made worse by the decline in the real estate market. The majority of Vineyard's CRE loans during the period of its aggressive growth were for properties located in southern California, which experienced a significant decline in real estate values.

Vineyard Pursued an Aggressive Growth Strategy and Was Highly Concentrated in CRE Loans

Vineyard's board and management embarked on an aggressive growth strategy for the bank in 2001, primarily by originating CRE loans in southern California. From 2001 through 2007, Vineyard increased its CRE loans (consisting of land and development loans and CRE mortgages) from $86 million to $1.6 billion and its total loan portfolio from $138 million to $2.1 billion. In 2008, however, its loan portfolio declined when Vineyard's board and management ceased lending in response to the economic downturn. Figure 1 illustrates the rapid growth and composition of Vineyard's overall loan portfolio from 2001 through 2007, and its subsequent decline during 2008.

Figure 1. Growth and Composition of Vineyard's Loan Portfolio, 2001-2008 (in millions)

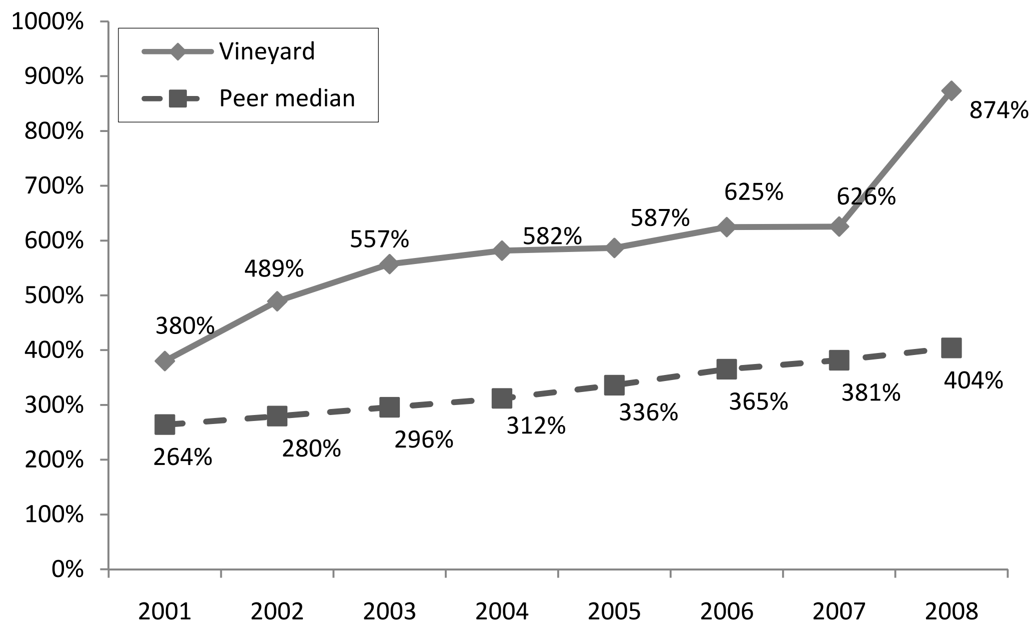


Source: OIG analysis of Vineyard's Call Reports.

Vineyard's excessive concentration in CRE loans, coupled with the poor underwriting of loans resulted in substantial losses for the bank when conditions in the southern California real estate market deteriorated. The poor quality of the CRE loans also led to diminished capital and strained liquidity for the bank.

In OCC's 2008 ROE, examiners criticized Vineyard's chief executive officer (CEO) for allowing the bank's CRE loan concentrations to reach unsafe and unsound levels. Examiners also criticized Vineyard's board for not reacting quickly enough to restrict the bank's growth and concentrations. From 2001 through 2007, Vineyard's CRE loans as a percentage of the bank's total capital increased from an already risky 380 percent to 626 percent. As shown in figure 2, Vineyard's CRE loans as a percentage of its total capital greatly exceeded that of its peer banks. (It should be noted that the dramatic increase in the gap from 2007 to 2008 was due to a 49 percent decline in Vineyard's Tier I Capital level as losses mounted; by then its loan portfolio was shrinking.)

Figure 2. CRE Loans as a Percentage of Total Capital, 2001-2008



Source: OIG analysis of Vineyard's Uniform Bank Performance Reports.

In November 2007, with the deteriorating conditions of the real estate market and increasing problem loans, Vineyard's board directed the bank to cease originating CRE loans and to reduce the number of CRE loans in its portfolio. Despite the board's effort, the concentration of CRE loans as percentage of capital continued to increase as losses began to erode Vineyard's capital.

Vineyard Relied on Costly and Volatile Funding to Fuel Growth

To finance its rapid growth, Vineyard relied heavily on more costly certificates of deposits and wholesale funding, which included brokered deposits and Federal Home Loan Bank (FHLB) loans. The bank reduced its size in 2008, but brokered deposits and FHLB loans increased in order to replace other funding sources. Certificates of deposit and brokered deposits together represented approximately 46 percent of total deposits in December 2007 and 78 percent in December 2008.

In July 2008, OCC entered into a consent order with Vineyard to address the bank's deficiencies in management, capital, asset quality, earnings, and liquidity. The consent order resulted in the reclassification of Vineyard's capital level from well-capitalized to adequately capitalized, which prevented it from accepting, renewing, or rolling over brokered deposits without a waiver from FDIC. This PCA-driven restriction on the use of brokered deposits significantly impacted Vineyard's liquidity.

In an OCC report on its August 2008 quarterly review of Vineyard, examiners wrote that Vineyard's liquidity levels and funds management practices were so critically deficient that the bank's continued viability was threatened. In its 2009 examination, which started in April 2009, OCC examiners wrote in their workpapers that they had serious doubts about Vineyard's ability to repay $182 million in brokered deposits scheduled to mature later in 2009, approximately $180 million in outstanding FHLB loans with maturities of less than 1 year, and $394 million in certificates of deposit scheduled to mature in mid-2009.

Vineyard's core deposit base also was extremely volatile because of negative publicity brought on by both the failure of IndyMac Bank and a proxy contest that publicized Vineyard's financial and management problems. From June 2008 to June 2009, Vineyard's core deposits decreased by $470 million. To attract and replace the deposits, Vineyard offered interest rates above prevailing market rates, in violation of the PCA restrictions imposed by the July 2008 consent order.[3] On August 26, 2008, OCC ordered Vineyard to cease offering those high interest rates. (Vineyard complied with OCC's order.)

Vineyard's Underwriting and Credit Risk Management Were Unsound

In the 2006 through 2008 examinations, OCC examiners found that Vineyard did not consistently obtain sufficient information about the financial condition of borrowers, principals, and

[3] Under 12 C.F.R. § 337.6, banks falling below the well-capitalized level may not accept, renew, or roll over any brokered deposit or solicit deposits with an effective yield more than 75 basis points above the prevailing market rate.

guarantors when underwriting loans. In its 2007 and 2008 ROEs, OCC directed Vineyard to improve its financial analyses during the loan underwriting process. Inadequate financial analysis increased Vineyard's credit risk because the ability of the bank's borrowers to repay their loans was contingent on their ability to sell or otherwise derive income from property that served as collateral for those loans. Despite OCC's directions, Vineyard failed to improve its financial analyses.

Vineyard's credit risk significantly increased and its underwriting became even more liberal during the tenure of a chief lending officer that Vineyard hired in March 2007 and terminated in May 2008. The chief lending officer generated a significant volume of poorly underwritten CRE loans (some examples are more fully described below). During the same time, Vineyard's board noted concern with the decline in the real estate market and the need to reduce the risk level of the bank's loan portfolio, culminating in its November 2007 directive to cease CRE loan originations and reduce the loan portfolio.

As an example of poor loan quality noted by OCC, the chief lending officer made four separate loans to one borrower totaling $22.5 million in September 2007. The loans were to finance the purchase and rehabilitation of 4 apartment complexes in states far from Vineyard's normal geographic lending area. Additionally, 3 of the 4 apartment complexes were underperforming, with high vacancies and poor property management, when the loans were approved. OCC had the following concerns about the loans:

- They were referred to the bank by a broker with whom Vineyard lacked prior experience. The chief lending officer waived bank policy prohibiting this practice.
- Three of the four loans had loan-to-value ratios exceeding Vineyard's policy limit of 75 percent.
- Vineyard's cash flow analysis of the borrowers' financial strength at the time of the loans' origination was weak.

By April 27, 2009, Vineyard had charged off $3.3 million in losses involving these loans and determined that losses could increase to as much as $10 million. It should also be noted that the four loans had been approved by Vineyard's loan committee, indicating a weakness in loan committee's review of the loans.[4]

In OCC's 2008 ROE, examiners noted that many of the loans originated by the chief lending officer were partial- or nonrecourse, without strong mitigating factors to offset the lack of guarantees. Many of those loans had high loan-to-value ratios, and approximately half of the loans had been referred by brokers with whom the bank lacked prior experience. The examiners concluded that Vineyard's credit risk management practices were weak and that the bank needed to

- manage concentrations of credit to ensure prudent risk diversification;
- establish appropriate underwriting for granting nonrecourse loans, including higher debt service ratios, lower loan-to-value ratios, larger cash equity requirements, and financially capable sponsors with incentives to support the debt;
- ensure accurate and timely loan grading in all portfolio segments;
- improve financial and cash flow analysis;
- provide meaningful problem loan reports; and
- improve the allowance for loan and lease loss (ALLL) analysis.

Vineyard's Board Did Not Exercise Its Authority Until It Was Too Late

As Vineyard grew, OCC and the Federal Reserve Bank of San Francisco (FRB San Francisco) became increasingly concerned about the capabilities and competencies of the boards of Vineyard and its holding company, which consisted of the same individuals.[5] Several board members had been directors since before 2000, when Vineyard was a relatively small community bank. By 2005, Vineyard had grown into a larger, more complex, highly concentrated institution. In 2005 and 2006, FRB San Francisco questioned the ability of Vineyard's board to effectively direct a

[4] The loan committee was comprised of senior managers and experienced loan officers. The loan committee normally only considers loans that exceed the lending authority of the loan officer, or loans that require special attention due to the applicant's credit history or other factors.
[5] Vineyard is wholly owned by its holding company. Vineyard's holding company was regulated and annually examined by FRB San Francisco.

bank of Vineyard's size, scope, and complexity. To address these concerns, FRB San Francisco required Vineyard's board to identify and address gaps in its directors' skills and competencies through continuing education or recruitment of individuals with the specialized skills and competencies needed. Vineyard's board adopted a resolution in May 2005 to seek a new outside director. A new director was added in September 2006. OCC examiners, still concerned about the board qualifications, recommended in the 2007 ROE that the board continue its efforts to improve its qualifications for overseeing Vineyard given the bank's size, scope, and direction.

During most of its aggressive growth period, Vineyard's board supported the CEO's growth strategy. Despite the declining real estate market, the CEO planned to continue the bank's original goal of increasing commercial construction loans, with the aim of becoming a $3 billion regional bank by 2010. In late 2007, however, the board became increasingly concerned about Vineyard's overall risk level and sought to restrict growth and reduce risk by tightening underwriting standards, ending construction and land development lending, and reducing its asset base and concentration limits. The CEO did not support the board's plan to limit growth, which ultimately led the board to force the CEO's resignation in January 2008.

In February 2008, the now former CEO and one shareholder of the bank's holding company initiated a proxy contest to gain control of Vineyard by nominating an alternate slate of seven directors to replace the existing board and return the former CEO to his previously held position. Five of the seven directors from the alternate slate and two incumbent directors were elected. OCC, however, informed the board in a letter dated July 31, 2008, that the former CEO could not return to his previous position.

OCC officials told us that the proxy contest consumed valuable time that the board could have used to address the mounting loan losses and capital adequacy, and it complicated efforts to fill important management vacancies, such as the position of CEO. In addition, the proxy contest, along with the July 2008 consent order and failure of IndyMac Bank (also located in southern California), resulted in negative publicity for Vineyard. This negative publicity, in turn, led to significant deposit withdrawals and hindered the bank's efforts to raise capital. Although Vineyard's new directors were more experienced than the members they replaced, they were unable to save Vineyard because of the rapid depletion of the bank's capital. While the significant losses in Vineyard's CRE loan portfolio were the primary cause of its failure, the bank became nearly insolvent in terms of liquidity as a result of deposit outflows in mid-2008.

OCC's Supervision of Vineyard

During the approximately 3 years, 2 months that it supervised Vineyard, OCC was unable to prevent a material loss to the Deposit Insurance Fund. OCC identified Vineyard's growth and high-risk concentration in CRE loans before approving Vineyard's conversion to a national bank charter in May 2006 but believed that management and the board were well aware of the risks and had implemented adequate control systems. OCC also identified concerns with the CRE concentration in 2007 during its first full-scope examination. Despite its concerns, however, OCC assigned Vineyard a CAMELS composite rating of 2 and did not require the bank to reduce its high-risk concentration. OCC did take forceful action in July 2008 by downgrading Vineyard's CAMELS composite rating to 4 and entering into a consent order with the bank. By then, the bank's problems had become too large and too severe to resolve.

We also noted a weakness in the scope of OCC's preconversion examination. Specifically, OCC approved Vineyard's charter conversion application despite the significant concerns regarding the CRE concentration identified by OCC examiners during the preconversion examination. Additionally, OCC was unaware that FDIC, Vineyard's federal banking regulator at the time, had in 2005 directed the bank to adopt a board resolution to restrict asset growth.

Once OCC concluded that strong action was needed to address Vineyard's problems, it imposed PCA-required restrictions on Vineyard through a July 2008 consent order. Among other things, OCC classified the bank's capital level to adequately capitalized and imposed restrictions consistent with that classification. Table 1 summarizes the results of OCC's full-scope safety and soundness examinations of Vineyard and enforcement actions taken.[6] Appendix 5 provides details of MRAs, corrective actions, and other issues noted during the examinations.

Table 1. Summary of OCC's Vineyard National Bank Examinations and Enforcement Actions

		Examination Results			
Date started	**Assets (millions)**	**CAMELS rating**	**Number of MRAs**	**Number of corrective actions**	**Enforcement actions**
3/6/2006[a] (preconversion)	$1,705	2/222222	N/A	3	None
4/2/2007 (full scope)	$2,251	2/222222	2	1	None
3/31/2008 (full scope)	$2,340	4/444432	9	4	Consent order, effective 7/22/2008
7/23/2008[b]	$2,340	5/455553	N/A	N/A	Consent order remains in place
11/03/2008[b]	$2,089	5/545554	N/A	N/A	Consent order remains in place
4/27/2009 [b]	$2,015	5/555555	N/A	N/A	Consent order remains in place

Source: OCC ROEs and Vineyard call reports.

[a] The scope of the preconversion examination of Vineyard was similar to the requirements of a full-scope examination. The report on the preconversion examination identified corrective actions that Vineyard was to take; however, these actions were not identified as MRAs as OCC does not use such a designation in preconversion examination documents.

[b] OCC performed a periodic monitoring review. MRAs are generally not made in such reviews.

[6] We concluded that OCC conducted its examinations of Vineyard and provided oversight through off-site monitoring in accordance with the timeframes specified in its examination policy. The scope of OCC's examinations were comprehensive. However, the workpapers supporting the examinations generally lacked clarity, specificity, and support for many of the examination procedures performed and many of the conclusions reached. We made similar observations about OCC examination workpapers in our material loss reviews of the failed National Bank of Commerce, First National Bank of Nevada, and First Heritage Bank, N.A.

OCC's Process to Approve Vineyard's 2006 Conversion to a National Bank Charter Was Flawed

During the preconversion examination, OCC examiners were concerned with the bank's aggressive growth and high concentration, but determined that management and the board had implemented reasonable underwriting standards and satisfactory risk management practices to address the high concentration. OCC also determined that board and management oversight was satisfactory, financial performance was good, liquidity was adequate, and capital was sufficient to support the projected growth and risk profile. As a result, OCC approved the conversion. We believe that OCC should have deferred approval until the weaknesses identified had been satisfactorily addressed and their resolution validated. At the very least, OCC should have imposed conditions to restrict Vineyard's growth and concentration when OCC approved the bank's conversion. Furthermore, OCC's preconversion examination failed to identify the existence of a 2005 board resolution that restricted the bank's continued growth.

<u>OCC's Charter Conversion Policies and Procedures</u>

OCC guidance outlines the application process and decision criteria for approval of the conversion of institutions to nationally chartered banks.[7] In determining whether to approve an application for conversion, OCC considers the applying institution's

- condition and management, including compliance with regulatory capital requirements;
- conformance with statutory criteria;
- adequacy of policies, practices, and procedures that parallel OCC's minimum policies and procedures; and
- Community Reinvestment Act (CRA) record of performance.

OCC may deny an institution's conversion application because of

- safety and soundness issues;
- inadequate capital;
- financial condition concerns;

[7] Comptroller's Licensing Manual, Conversions (April 2004).

- significant CRA or compliance concerns;
- ownership issues;
- inconsistency with applicable laws, regulations, or OCC policy;
- attempted circumvention of supervisory action by the applicant's current regulator; or
- failure by the applicant to provide requested information that would allow OCC to make an informed decision.

The guidance also states that if significant weaknesses exist in financial and managerial factors, the conversion normally will be denied.

OCC may also impose special conditions for approvals to

- protect the safety and soundness of the bank;
- prevent conflicts of interest;
- provide customer protections;
- ensure that approval is consistent with the statutes and regulations; or
- provide for other supervisory or policy considerations.

OCC Identified Significant Concentration Concerns at Vineyard But Its Preconversion Examination Missed Certain Critical Information About the Bank's Operations

From 1981 to 2001, Vineyard was chartered as a national bank and supervised by OCC. In late 2000, Vineyard, while under a different management team, entered into a memorandum of understanding (MOU) with OCC to address its poor credit administration at the time.[8] While still under the MOU with OCC, Vineyard switched to a state charter in 2001 that placed it under the regulatory purview of the California Department of Financial Institutions (DFI) and the FDIC. In December 2005, Vineyard applied with OCC to convert back to a national bank charter. Vineyard's board believed that many of the bank's strategic endeavors were better suited to a national charter.

OCC conducted a preconversion examination of Vineyard in March 2006 to determine if the bank's application for charter conversion

[8] An MOU is an informal enforcement action. As such, it is not made public by OCC.

should be approved. Because the last full-scope examination conducted by DFI and FDIC was in April 2005, OCC examiners expanded the preconversion examination to meet the requirements of a full-scope examination.[9]

OCC examiners noted that Vineyard was pursuing an aggressive growth strategy and projected growth of 33 percent, 25 percent, and 20 percent, respectively over the next 3 years, but determined that growth projections were reasonable in light of the overall satisfactory risk management systems. Examiners also determined that the Vineyard's CRE loan portfolio at 587 percent of capital was high. In the preconversion examination report, the examiners cautioned Vineyard that the high concentration could negatively affect the bank's asset quality and liquidity if the real estate market declined. They also stated that management's ability to react to potential declines in real estate and the resulting problem loans was unproven. Examiners identified concerns about the real estate appraisal and CRE stress testing process and a compliance issue on foreign wire activity that warranted attention and obtained written representations from management to address those issues. As noted previously, OCC determined that board and management oversight of the lending area was satisfactory and that capital levels supported the risk profile. As a result, OCC assigned Vineyard a CAMELS composite rating of 2 and upgraded the management component rating to 2 from 3.

While the preconversion examination revealed troubling information about Vineyard, it did not identify a DFI/FDIC-required board resolution placing limits on the bank's growth. In 2004, DFI and FDIC entered into an MOU (an informal enforcement action) with Vineyard. The purpose of the MOU was to address the regulators' concerns about the bank's aggressive growth, high concentration in CRE loans, inadequate risk management, and questionable credit administration. DFI and FDIC's joint 2005 ROE stated that while Vineyard had made much needed improvements, the bank was only in partial compliance with the provisions of the MOU; that the bank had significant asset growth, concentration risk, and credit

[9] The Comptroller's Handbook, Bank Supervision Process, states that a converted national bank must receive a full-scope, on-site examination within 12 months from the date of its last full-scope examination by the prior federal banking agency.

administration practices that remained of concern; and that Vineyard needed to take additional measures to address deficiencies in those areas. FDIC assigned Vineyard a management component rating of 3 but upgraded Vineyard's CAMELS composite rating to a 2 from a 3.

At this point, Vineyard's CEO vigorously opposed continuation of the MOU as well as the assigned CAMELS management component rating of 3 for the examination. DFI and FDIC later terminated the MOU in May 2005, even though Vineyard had only partially complied with its provisions. In its place, DFI and FDIC allowed the bank to adopt a board resolution in May 2005 that contained many of the same provisions contained in the MOU.

Although OCC examiners were aware of the 2004 MOU and its subsequent termination, they were not aware of the board resolution that replaced the MOU. This was surprising in that there were at least three separate mentions of the resolution in the minutes of board meetings. Additionally, the inspection report issued by FRB San Francisco for its 2005 examination of Vineyard's holding company stated that the MOU was replaced with a board resolution. These materials were available to the OCC examiners during their preconversion examination.

According to an OCC official, it was his understanding that DFI and FDIC terminated the MOU because Vineyard's condition had improved as evidenced by the composite rating of 2. The official told us that if he had been aware of the board resolution and the fact that the bank had only partially complied with both the MOU and board resolution, this information may have affected the CAMELS ratings OCC assigned from its preconversion examination.

OCC approved Vineyard's conversion in May 2006. As a condition of the conversion, OCC required that the bank provide advance written notice and obtain OCC's written approval of any intent to significantly deviate from or change its current business plan. OCC did not impose conditions restricting the bank's planned growth and concentration.[10]

Given the examiners findings and concerns, we believe that it was a mistake for OCC to approve Vineyard's charter conversion before the bank's weaknesses had been satisfactorily addressed and their resolution validated. At the very least, OCC should have imposed conditions to restrict the bank's growth and concentration when OCC approved the bank's conversion.

OCC's 2007 Examination Identified Increased Concentration But No Forceful Action Was Taken

In the 2007 ROE for OCC's first full-scope examination of Vineyard after conversion, OCC examiners again expressed concern about asset quality because of the bank's high concentration in CRE loans and the weakening real estate market. At the time of the examination, the bank's combined CRE loans had grown from 587 percent of capital to 628 percent of capital. Nevertheless, OCC examiners determined that Vineyard's credit administration practices largely conformed to interagency guidance on CRE concentration issued in December 2006.[11] While this guidance did not set specific concentration limits, it did provide a number of high-level indicators to identify institutions potentially exposed to concentration risk, including:

- total reported loans for construction, land development, and other land representing 100 percent or more of an institution's total capital; or
- total CRE loans representing 300 percent or more of the institution's total capital, and the outstanding balance of the

[10] One of the provisions of the May 2005 board resolution that carried over from the terminated MOU with DFI and FDIC limited Vineyard's future asset growth to 25 percent a year. Vineyard's business plan submitted to OCC projected growth rates in its total assets of 33 percent, 25 percent, and 20 percent for 2006, 2007, and 2008, respectively. OCC accepted Vineyard's business plan during its 2006 pre-conversion examination and while the growth rate for 2006 (33 percent) varied from the 25 percent called for in the board resolution, we did not consider this variance significant. Nevertheless, we believe that the existence of the board resolution was still a critical piece of information that OCC should have considered in approving the conversion.
[11] OCC, Federal Reserve, and FDIC, "Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices" (Dec. 12, 2006).

institution's CRE loan portfolio has increased by 50 percent or more during the prior 36 months.

From 2006 through 2007, Vineyard's CRE loan assets as a percentage of capital significantly exceeded these supervisory benchmarks. Although OCC examiners identified Vineyard's concentration risk in those years, they deemed the bank's practices to be safe and sound and assigned Vineyard a CAMELS composite rating of 2. OCC also did not direct Vineyard to limit its exposure by decreasing its growth and concentration in CRE loans.

When asked why not, an OCC official told us that—based on the information reviewed at the time—OCC examiners concluded that the bank had satisfactory credit risk management, as indicated in the 2007 ROE. Furthermore, the OCC official said the guidelines were only indicators, and that if a bank exceeded the guidelines it could do so as long as it had stronger risk management controls. In this regard, OCC considered Vineyard to have the necessary risk management controls in place to handle the high concentration. During the examination, examiners found that Vineyard had established concentration limits, monitored market conditions to manage concentration risk, and were sending detailed lending reports to the board. The examiners did identify several matters requiring attention to further improve the bank's credit risk management processes.

We believe that OCC should have reached a different conclusion by 2007 about the adequacy of Vineyard's risk management controls based on our review of the supervisory record and on the fact that Vineyard's failure resulted primarily from loan losses stemming from its high concentration in CRE loans. In the 2007 ROE, OCC concluded that credit administration was satisfactory, yet identified some credit risk management practices as MRAs. Specifically, OCC criticized Vineyard for its failure to obtain sufficient information about the financial condition of borrowers, principals, and guarantors, and warned that if not addressed the bank could be exposed to additional credit risk and asset problems, especially if home sales remained slow or worsened. OCC ended up repeating the MRA in its 2008 ROE, in which examiners wrote that Vineyard's concentration levels were unsafe and unsound. The examiners concluded that bank management did not adequately manage concentration risk, given its slowness to reduce the high concentration levels when the real estate market began weakening in mid-2006.

OCC's enforcement action policy states that problems or weaknesses should be dealt with early, before they develop into more serious supervisory issues or adversely affect a bank's performance and viability. We believe OCC should have considered an enforcement action as a result of its 2007 examination, when examiners identified continued concerns with Vineyard's high-risk concentration first noted in its 2006 preconversion examination and warned that the weakening real estate market could lead to substantial increases in problem assets.

OCC Took Enforcement Action in July 2008

OCC began a full-scope examination of Vineyard in March 2008. In the 2008 ROE, OCC took a much stronger stance toward Vineyard than in the prior examination after the examiners found that credit underwriting had become more liberal, previously identified credit risk management weaknesses had not been addressed, the bank's asset quality had deteriorated significantly, and its overall condition had become unsatisfactory. OCC downgraded Vineyard's CAMELS composite rating to 4 from 2 and initiated a consent order. The examiners attributed Vineyard's deterioration to its rapid growth and excessive concentration in CRE loans, which OCC had not previously required the bank to reduce until the 2008 examination. They also determined that Vineyard's board and former CEO had been deficient in their oversight of the bank's direction and allowed weak credit risk management practices during the bank's rapid growth. In summary, although the examination record did not document a material change in the way the bank operated from the prior examination, the examiners reached different, and we believe well-supported, conclusions about the bank's condition.

On May 5, 2008, OCC designated Vineyard in troubled condition and entered into a consent order (a formal enforcement action) with the bank on July 22, 2008. The purpose of the consent order was to address Vineyard's deficiencies in management, capital, asset quality, earnings, and liquidity within specified timeframes. The consent order required Vineyard to appoint a permanent CEO and chief credit officer, maintain certain capital ratios, develop a 3-year capital plan, revise its ALLL methodology, address concentrations of credit, adhere to its own underwriting policy, adequately risk-rate loans, establish a loan review system, and take prompt action to protect its interest in criticized assets.

On July 28, 2008, OCC transferred supervision of Vineyard to its Special Supervision Division in Washington, D.C., which directed overall supervision of the bank until it was closed on July 17, 2009.[12] Because conditions at Vineyard had already begun to deteriorate rapidly before the transfer, there was little the Special Supervision Division could do to rehabilitate the bank.

Vineyard ultimately did not comply with many of the consent order's requirements. The bank's problems were too large and too severe to resolve without substantial additional capital. On August 27, 2008, OCC downgraded Vineyard's overall CAMELS rating to 5. The component ratings for asset quality, management, earnings, liquidity, and sensitivity to market risk were also downgraded to 5. OCC examiners concluded that Vineyard's financial condition was critically deficient, as evidenced by Vineyard's deteriorated asset quality, significant losses, diminished earnings, eroded capital, and strained liquidity. They notified Vineyard that its failure was highly probable without outside financial assistance. Vineyard was unsuccessful in finding investors to inject capital into the bank.

OCC Began PCA After Vineyard's Capital Levels Fell

The purpose of PCA is to resolve the problems of insured depository institutions with the least possible long-term loss to the Deposit Insurance Fund. PCA requires federal banking agencies to take certain actions when an institution's capital drops to certain levels. PCA also gives regulators flexibility to discipline institutions based on criteria other than capital levels to help reduce deposit insurance losses caused by unsafe and unsound practices.

[12] The role of the Special Supervision Division is to supervise problem banks through rehabilitation or through other resolution processes such as the sale, merger, or liquidation of such institutions.

OCC implemented PCA as described below.

- As authorized by PCA, OCC's July 2008 consent order with Vineyard, among other things, resulted in the reclassification of the bank's capital category from well capitalized to adequately capitalized based on its June 30, 2008, call report. Because of the adequately capitalized designation, OCC prohibited Vineyard from accepting or renewing brokered deposits without a waiver from FDIC and from offering excessive interest rates on deposits. In August 2008, OCC examiners found that Vineyard had violated this regulation by offering interest rates above prevailing market rates and ordered the bank to stop. Vineyard complied with OCC's demand.

- On May 1, 2009, OCC timely notified Vineyard that it had fallen into the significantly undercapitalized PCA category based on the bank's March 31, 2009, call report. The PCA required Vineyard to file a capital restoration plan with OCC no later than May 18, 2009. Vineyard, however, never submitted a capital restoration plan. On May 15, 2009, Vineyard informed OCC that neither the bank nor its holding company could raise sufficient capital to become adequately capitalized within a realistic timeframe.

- On June 18, 2009, OCC notified Vineyard that it was critically undercapitalized based on the bank's May 31, 2009, financial information. Vineyard had incurred losses that depleted all of its capital. PCA mandates that a critically undercapitalized bank be put into receivership or conservatorship with the concurrence of FDIC within 90 days after it becomes critically undercapitalized. OCC appointed FDIC as receiver for Vineyard on July 17, 2009.

OCC Lessons-Learned Review Is Not Yet Complete

According to OCC headquarters officials, an internal lessons-learned review of Vineyard's failure had not been completed at the time of our review. The purpose of the review is to assess both the causes of the failure and OCC's supervision of the bank.

Conclusions and Recommendations

Our material loss review of Vineyard is the 11th such review we have performed of a failed OCC-regulated financial institution during the current financial crisis. Appendix 6 lists the other 10 material loss reviews and our associated recommendations. With one exception noted in the appendix, OCC management agreed with the prior recommendations and has taken action or is taking corrective actions to address them.

Vineyard is the second OCC-regulated failed bank we have reviewed where the bank failed within a relatively short timeframe after it was converted to a nationally chartered bank. In our January 2010 material loss review of the failed Silverton Bank, N.A. (Silverton), we found OCC approved Silverton's conversion to a nationally chartered bank in August 2007, despite significant weaknesses identified by OCC examiners during a preconversion examination and the declining housing market.[13] In our Silverton report, we recommended that OCC promptly assign an examiner-in-charge and ensure continuous supervisory coverage of converted institutions, to include the timely initiation of the first full-scope examination after conversion. This recommendation was made in response to a gap in supervision identified with Silverton. In contrast, the supervision of Vineyard was continuous before and after conversion.

We also recommended in the report on Silverton that OCC should ensure that appropriate actions are taken to amend or reinforce OCC guidance in response to the lessons learned review of the Silverton failure. In particular, OCC should (1) determine that banks seeking conversion to a national charter satisfactorily address significant deficiencies identified by OCC or prior regulators before approval and (2) formalize the process for second level reviews of charter conversions. In its response, OCC acknowledged that stronger controls are needed to ensure the clarity of its charter conversion process. Based on our review of the Vineyard charter conversion process, we reaffirm our prior recommendations and the

[13] OIG, *Safety and Soundness: Material Loss Review of Silverton Bank, N.A.,* OIG-10-033 (Jan. 22, 2010).

need for OCC to take corrective action. We are not making any new recommendations from our material loss review of Vineyard.

OCC acknowledged our reaffirmation of the two prior recommendations relating to the charter conversion process. OCC also stated that appropriate steps have been taken to address the recommendations.

* * * * * *

We appreciate the courtesies and cooperation provided to our staff during the audit. If you wish to discuss the report, you may contact me at (617) 223-8640 or Mark Ossinger, Audit Manager, at (617) 223-8643. Major contributors to this report are listed in appendix 8.

/s/
Donald P. Benson
Audit Director

We conducted this material loss review of Vineyard Bank, N.A. (Vineyard), Corona, California, in response to our mandate under section 38(k) of the Federal Deposit Insurance Act.[14] This section provides that if a deposit insurance fund incurs a material loss with respect to an insured depository institution, the inspector general for the appropriate federal banking agency is to prepare a report to the agency, which shall

- ascertain why the institution's problems resulted in a material loss to the insurance fund;
- review the agency's supervision of the institution, including implementation of the prompt corrective action provisions of section 38; and
- make recommendations for preventing any such loss in the future.

Section 38(k) defines a loss as material if it exceeds the greater of $25 million or 2 percent of the institution's total assets. The law also requires the inspector general to complete the report within 6 months after it becomes apparent that a material loss has been incurred.

We initiated a material loss review of Vineyard based on the loss estimate by the Federal Deposit Insurance Corporation (FDIC). As of August 7, 2009, FDIC estimated that Vineyard's failure would cost the Deposit Insurance Fund $572.8 million. As of December 31, 2009, FDIC estimated that the loss to the Deposit Insurance Fund would be $597 million.

Our objectives were to determine the cause of Vineyard's failure and assess the bank's supervision by the Office of the Comptroller of the Currency (OCC). To accomplish our review, we conducted fieldwork at OCC headquarters in Washington, D.C., its district office in Denver, Colorado, and its field office in Carlsbad, California. We also performed work and interviewed officials at FDIC's Division of Resolutions and Receiverships in Irvine, California.

To assess the adequacy of OCC's supervision of Vineyard, we determined (1) when OCC first identified safety and soundness

[14] 12 U.S.C. § 1831o(k).

problems at Vineyard, (2) the gravity of the problems, and (3) the supervisory response OCC took to get the bank to correct the problems. We also determined whether OCC (1) might have discovered problems earlier; (2) identified and reported all the problems; and (3) issued comprehensive, timely, and effective enforcement actions that dealt with any unsafe or unsound activities. We performed the following work:

- We determined that the time period relating to OCC's supervision of Vineyard covered by our audit would be May 2006 through Vineyard's failure on July 17, 2009. This period included a preconversion examination prior to Vineyard's conversion from a state-chartered institution to a national banking association, two full-scope safety and soundness examinations, and two targeted safety and soundness examinations performed subsequent to becoming a national banking association.

- We reviewed OCC's preconversion examination report, supporting documentation, and related correspondence. We performed this review to gain an understanding of any issues identified and the approach and methodology OCC used to assess the bank's condition and subsequent approval of the bank for a national charter.

- We analyzed OCC's postconversion reports of examination, supporting workpapers, and related supervisory and enforcement correspondence. We performed these analyses to gain an understanding of the problems identified, the approach and methodology OCC used to assess the bank's condition, and the regulatory action OCC used to compel bank management to address deficient conditions. We did not conduct an independent or separate detailed review of the external auditor's work or associated workpapers other than those incidentally available through the supervisory files.

- We interviewed and discussed various aspects of OCC's supervision of Vineyard with OCC officials, examiners, and attorneys to obtain their perspectives on the bank's condition and the scope of the examinations.

- We interviewed an official from the California Department of Financial Institutions (DFI) and FDIC's Division of Supervision and Consumer Protection responsible for supervision of the bank before its conversion to a national banking association in 2006. We also reviewed reports of examination prepared by FDIC and DFI for Vineyard prior to its conversion to a national charter, to gain an understanding of its assessment of the bank's condition.

- We interviewed personnel with FDIC's Division of Resolutions and Receiverships who were involved in the receivership process, which was conducted after Vineyard's closure and FDIC's appointment as receiver.

- We reviewed reports of bank holding company inspection prepared by the Federal Reserve Bank of San Francisco (FRB) to gain an understanding of its assessment of the condition of Vineyard's holding company. We did not interview FRB officials.

We conducted our fieldwork from August 2009 through January 2010. 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.

History of Vineyard Bank, N.A.

Vineyard Bank, N.A. (Vineyard), Corona, California, was established in September 1981. Vineyard converted to a state-chartered bank in August 2001 and converted back to a nationally chartered bank in May 2006. From September 2006 through March 2009, OCC collected fees from national banks totaling $2.1 billion, of which Vineyard paid $1.4 million. At the time of its failure, on July 17, 2009, Vineyard had approximately $1.7 billion in assets and 18 banking locations, including its main office. It had offices in the inland and coastal areas of southern California, as well as one banking location in the San Francisco area.

Vineyard was the principal asset and a wholly owned subsidiary of Vineyard National Bancorp, a financial holding company. Vineyard National Bancorp was also the sole stockholder of 1031 Exchange Advantage, Inc., and 1031 Funding & Reverse Corp. (collectively, the Exchange Companies) and 10 unconsolidated statutory business trust subsidiaries created to raise capital for the bank. Vineyard National Bancorp's common stock was listed on NASDAQ, and its Series D preferred stock was listed on the NYSE Amex. The company was delisted from both exchanges in April 2009.

Appendix 4 contains a chronology of significant events regarding Vineyard.

Types of Examinations Conducted by OCC

OCC conducts various types of examinations, including full-scope on-site examinations. A full-scope examination is a combined examination of the institution's safety and soundness, compliance with regulations, and information technology (IT) systems.

The safety and soundness portion of the examination includes a review and evaluation of the six CAMELS components: Capital adequacy, Asset quality, Management administration, Earnings, Liquidity, and Sensitivity to market risk. OCC assigns the bank a rating for each component and a composite rating based on its assessment of the overall condition of the bank and its level of supervisory concern. The compliance portion of the examination includes an assessment of how well the bank manages compliance with various consumer protection laws and related regulations, such as the Truth in Lending Act, the Truth in Savings Act, and the Bank Secrecy Act. The IT portion of the examination evaluates the overall performance of IT within the institution and the institution's ability to identify, measure, monitor, and control technology-related risks.

OCC also conducts targeted examinations. A targeted examination is any examination that does not fulfill all the statutory requirements of a full-scope examination.

OCC must schedule full-scope, on-site examinations of insured banks once during either a 12-month or 18-month cycle. OCC is to conduct examinations on a 12-month cycle until a bank's management has demonstrated its ability to operate the institution in a safe and sound manner and satisfied all conditions imposed at the time of approval of its charter. Once a bank meets these criteria, OCC may use an 18-month examination cycle if the bank

- has total assets of less than $500 million;
- is well-capitalized;
- at its most recent examination received a:
  - Management component rating of 1 or 2, and
  - Composite rating of 1 or 2; and
- is not currently subject to a formal enforcement proceeding or order by the Federal Deposit Insurance Corporation, OCC, or the Federal Reserve Board; and
- has not undergone a change in control during the 12-month period since completion of the last full-scope, on-site examination.

Enforcement Actions Available to OCC

OCC examinations of banks result in the issuance of reports of examinations (ROE) that identify any areas of concern. OCC uses informal and formal enforcement actions to address violations of laws and regulations and to address unsafe and unsound practices.

Informal Enforcement Actions

OCC may use informal enforcement actions when a bank's overall condition is sound, but it is necessary to obtain written commitments from a bank's board of directors or management to ensure that it will correct problems and weaknesses. Informal enforcement actions provide a bank with more explicit guidance and direction than a ROE normally contains but are generally not legally binding. Informal enforcement actions include commitment letters and memoranda of understanding. Also included are safety and soundness plans authorized by 12 C.F.R. Part 30. Informal enforcement actions are not disclosed to the public.

Formal Enforcement Actions

Formal enforcement actions are authorized by statute, generally more severe than informal actions, and disclosed to the public. Formal enforcement actions are enforceable under the Federal Deposit Insurance Act. They are appropriate when a bank has significant problems, especially when there is a threat of harm to the bank, depositors, or the public. OCC is to use formal enforcement actions when informal actions are considered inadequate, ineffective, or otherwise unlikely to influence bank management and board members to correct identified problems and concerns in the bank's operations. Because formal actions are enforceable, OCC can assess civil money penalties against banks and individuals for noncompliance with a formal agreement or final order. OCC can also request a federal court to require the bank to comply with an order. Formal enforcement actions include consent orders, cease and desist orders, formal written agreements, and prompt corrective action directives.

OCC Enforcement Guidelines

Factors used in determining whether to use informal action or formal action include the following:

- the overall condition of the bank;
- the nature, extent, and severity of the bank's problems and weaknesses;
- the commitment and ability of bank management to correct the identified deficiencies; and
- the existence of previously identified but unaddressed problems or weaknesses.[15]

[15] OCC Policies and Procedures Manual 5310-3 (Rev).

Allowance for loan and lease losses	An estimate of uncollectible amounts that is used to reduce the book value of loans and leases to the amount that is expected to be collected. It is established in recognition that some loans in the institution's overall loan and lease portfolio will not be repaid.
Brokered deposit	Any deposit that is obtained, directly or indirectly, from a deposit broker. The bank solicits deposits by offering rates of interest that are significantly higher than the rates offered by other insured depository institutions in its normal market area. Use of brokered deposits is limited to well-capitalized insured depository institutions and, with a waiver from the Federal Deposit Insurance Corporation (FDIC), to adequately capitalized institutions. Undercapitalized institutions are not permitted to accept brokered deposits. (See 12 U.S.C. § 1831(f) and 12 C.F.R. 337.6.)
Call report	A quarterly report of income and financial condition that banks file with their regulatory agency. The contents of a call report include consolidated detailed financial information on assets, liabilities, capital, and loans to executive officers, as well as income, expenses, and changes in capital accounts.
CAMELS	An acronym for performance rating components for financial institutions: capital adequacy, asset quality, management, earnings, liquidity, and sensitivity to market risk. Numerical values range from 1 to 5, with 1 being the best rating and 5 being the worst.
Capital restoration plan	A plan submitted to the appropriate federal banking agency by an undercapitalized insured depository institution. A capital restoration plan specifies the steps the insured depository institution is to take to become adequately capitalized, the levels of capital to be attained during each year in which the plan is in effect, how the institution is to comply with the restrictions or requirements then in effect, the types and levels of activities in which the institution is to

	engage, and any other information that the federal banking agency may require.
Commercial real estate loans	Loans for real property where the primary or significant source of repayment is from rental income associated with the property or the proceeds of the sale, refinancing, or permanent financing of the property. Commercial real estate loans include loans for construction and real estate development, land development, and commercial properties such as office buildings and shopping centers.
Concentration (of credit)	A situation where direct, indirect, or contingent obligations exceed 25 percent of a bank's capital structure.
Concentration risk	Risk in a loan portfolio that arises when a disproportionate number of an institution's loans are concentrated in one or a small number of financial sectors, geographical areas, or borrowers.
Consent order	The title given by the Office of the Comptroller of the Currency (OCC) to a cease and desist order that is entered into and becomes final through the board of directors' execution, on behalf of the bank, of a stipulation and consent document. Its provisions are set out in article-by-article form, and it prescribes restrictions and remedial measures necessary to correct deficiencies or violations in the bank in order to return it to a safe and sound condition.
Division of Resolutions and Receiverships	A division within FDIC that is charged with resolving failing and failed financial institutions, including ensuring that depositors have prompt access to their insured funds.
Federal Home Loan Bank	A bank within the Federal Home Loan Bank (FHLB) System, which consists of 12 regional banks from which local member institutions borrow funds to finance housing, economic development, infrastructure, and jobs. The system provides liquidity to member institutions that hold mortgages in their

	portfolios and facilitates the financing of mortgages by making low-cost loans, called advances, to members. Advances are available to members with a wide variety of terms to maturity, from overnight to long term, and are collateralized. Advances are designed to prevent any possible loss to FHLBs, which also have a super lien (a lien senior or superior to all current and future liens on a property or asset) when institutions fail. To protect their position, FHLBs have a claim on any of the additional eligible collateral in the failed bank. In addition, FDIC has a regulation that reaffirms FHLB priority, and FHLBs can demand prepayment of advances when institutions fail.
Full-scope examination	Examination activities performed during the supervisory cycle that (1) are sufficient in scope to assign or confirm a bank's CAMELS composite and component ratings; (2) satisfy core assessment requirements; (3) result in conclusions about a bank's risk profile; (4) include onsite supervisory activities; and (5) generally conclude with the issuance of a report of examination.
Loan-to-value ratio	A ratio for a single loan and property calculated by dividing the total loan amount at origination by the market value of the property securing the credit plus any readily marketable collateral or other acceptable collateral. In accordance with Interagency Guidelines for Real Estate Lending Policies, institutions' internal loan-to-value limits should not exceed the legal lending limit: (1) 65 percent for raw land; (2) 75 percent for land development; (3) 80 percent for commercial, multifamily, and other nonresidential loans; and (4) 85 percent for one-family to four-family residential loans The guidelines do not specify a limit for owner-occupied one-family to four-family properties and home equity loans. However, when the loan-to-value ratio on such a loan equals or exceeds 90 percent at the time of origination, the guidelines state that the bank should require mortgage insurance or readily marketable collateral.

Matter requiring attention	A bank practice noted during an examination that deviates from sound governance, internal control, and risk management principles, which may adversely affect the bank's earnings or capital, risk profile, or reputation if not addressed. It may also result in substantive noncompliance with laws and regulations, internal policies or processes, OCC supervisory guidance, or conditions imposed in writing in connection with the approval of any application or other request by a bank. Matters requiring attention are not enforcement actions, but failure by a bank's board and management to address a matter requiring attention could lead to an enforcement action.
Nonrecourse loan	A loan that is secured by collateral (e.g., a home or building), but for which the borrower is not held personally liable. If the lender seizes the property and the sale does not cover the loan, the borrower is not responsible for the shortfall.
Prompt corrective action	A framework of supervisory actions for insured banks that are not adequately capitalized. It was intended to ensure that action is taken when an institution becomes financially troubled in order to prevent a failure or minimize resulting losses. These actions become increasingly severe as a bank falls into lower capital categories. The capital categories are well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized. (See 12 U.S.C. § 1831o.) The prompt corrective action minimum capital requirements are as follows:

Capital category	Total risk-based		Tier 1/ risk-based		Tier 1/ leverage
Well-capitalized[a]	10% or greater	and	6% or greater	and	5% or greater
Adequately capitalized	8% or greater	and	4% or greater	and	4% or greater (3% for 1-rated)
Undercapitalized	Less than 8%	or	Less than 4%	or	Less than 4% (except for 1-rated)
Significantly undercapitalized	Less than 6%	or	Less than 3%	or	Less than 3%
Critically undercapitalized	Has a ratio of tangible equity to total assets that is equal to or less than 2 percent. Tangible equity is defined in 12 C.F.R. § 565.2(f).				

[a] To be well-capitalized, a bank also cannot be subject to a higher capital requirement imposed by OCC.

Proxy contest — A shareholder challenge to an action or the control of corporate management accomplished through the solicitation of proxies from other shareholders.

Risk-rate — A bank's internal rating that summarizes the risk of loss due to failure by a given borrower to pay as promised.

Safety and soundness examination — The part of an examination that includes a review and evaluation of each CAMELS component rating (see explanation of CAMELS above).

Tier 1 capital — Common shareholder's equity (common stock, surplus, and retained earnings), noncumulative perpetual preferred stock, and minority interests in the equity accounts of consolidated subsidiaries.

Troubled condition — A national bank is in troubled condition if it (1) has a composite CAMELS rating of 4 or 5; (2) is subject to a cease and desist order, a consent order, or a formal written agreement, unless otherwise informed in writing by the OCC; or (3) has been informed by the OCC that, as a result of an examination, it has been designated in troubled condition.

Risk-based capital — A measure of a bank's financial strength, taking into account capital reserves for loans, investments, and

	certain other items off the balance sheet. In general, assets with higher credit risk require more capital in reserve than low-risk assets. The aim of risk-based capital is to (1) encourage banks to keep a sufficient cushion of equity capital, including common stock, to support balance sheet assets; (2) include off-balance sheet items in the computation of capital adequacy; (3) eliminate disincentives to holding low-risk, liquid assets; and (4) set uniform international guidelines for bank capital adequacy.
Uniform Bank Performance Report	An analytical tool created by the Federal Financial Institutions Examinations Council to help supervise and examine financial institutions. A Uniform Bank Performance Report is produced quarterly for each commercial bank that is supervised by the Board of Governors of the Federal Reserve System, FDIC, or OCC. The performance and composition data in the report are presented in the form of ratios, percentages, and dollar amounts and are computed mainly from call reports submitted by the bank. The Uniform Bank Performance Report also compares a bank’s performance and balance sheet structure with those of similarly sized banks.
Wholesale funding	Funding obtained by financial institutions through such sources as federal funds, public funds, FHLB advances, the Federal Reserve’s primary credit program, foreign deposits, and brokered deposits, and deposits obtained through the Internet or certificate of deposit listing services.

The following chronology describes significant events in the history of Vineyard Bank, N.A. (Vineyard), including examinations conducted and enforcement actions taken by the Office of the Comptroller of the Currency (OCC). Appendix 5 contains additional information on the results of examinations, including any significant safety and soundness matters requiring attention, and recommended actions.

Date	Event
9/11/1981	The bank is established under the original name of Vineyard National Bank.
8/3/2001	Vineyard National Bank changes its name to Vineyard Bank. The bank's primary federal banking regulator changes from OCC to the Federal Deposit Insurance Corporation (FDIC).
10/29/2001	The California Department of Financial Institutions (DFI) and FDIC conduct a joint examination of Vineyard Bank. The examination finds the following: (1) the board places an emphasis on growth as opposed to controls, (2) internal audit independence and scope are inadequate, (3) accounting controls and administrative controls need improvement, and (4) earnings potentially may not fully support operations. DFI and FDIC assign Vineyard Bank a CAMELS composite rating of 3.
3/8/2002	Vineyard Bank, DFI, and FDIC enter into a memorandum of understanding (MOU) aimed at addressing less than satisfactory conditions detailed in the 2001 joint DFI and FDIC report of examination (ROE).
11/4/2002	DFI and FDIC conduct a joint examination of Vineyard Bank. The examination finds that bank management has adequately addressed all provisions of the March 2002 MOU. The examination concludes that the overall condition of the bank has improved and is satisfactory. DFI and FDIC assign Vineyard Bank a CAMELS composite rating of 2.
7/4/2003	Vineyard Bank acquires Southland Business Bank of Irwindale, California.
11/3/2003	DFI and FDIC conduct a joint examination of Vineyard Bank. The examination finds the risk profile of the bank to have increased to a level that warrants concern because of large construction loan concentration, rapid asset growth, substantial reliance on volatile funding, and inadequate risk management practices. DFI and FDIC assign Vineyard Bank a CAMELS composite rating of 3.
7/7/2004	Vineyard Bank, DFI, and FDIC enter into an MOU to correct the unsatisfactory conditions detailed in the 2003 ROE.
1/10/2005	DFI and FDIC conduct a joint examination of Vineyard Bank. The examiners conclude that the overall condition of the bank has improved but continue to have concerns about the bank's significant asset growth in construction loans and its credit administration practices. In addition, the examiners concluded that the performance of the bank's board and management is not fully satisfactory and that further efforts are necessary to comply fully with the 2004 MOU. DFI and FDIC assign Vineyard Bank a CAMELS composite rating of 2.
5/11/2005	The 2004 MOU between Vineyard Bank, DFI, and FDIC is terminated contingent upon the bank's adoption of a board resolution.
5/25/2005	Vineyard Bank adopts a board resolution that is to remain in effect until completion of the next regularly scheduled joint DFI/FDIC examination. Among other things, the board resolves to seek an additional outside director, prepare a risk profile analysis for board approval prior to entering into a new business, restrict internal asset growth to 25 percent per year, and adopt a written 3-year strategic plan.
12/30/2005	Vineyard Bank submits an application for a national charter with OCC.

Date	Event
4/18/2006	OCC conducts a preconversion examination of Vineyard Bank and assigns the bank a CAMELS composite rating of 2. The examiners conclude that the most significant concern regarding the bank is its large concentration in commercial real estate (CRE) loans, including speculative residential construction loans.
5/10/2006	Vineyard Bank changes its name to Vineyard Bank, N.A. (Vineyard). The bank's primary federal banking regulator changes from FDIC to OCC.
8/1/2006	Vineyard acquires Rancho Bank of San Dimas, California.
4/2/2007	OCC begins a full-scope examination of Vineyard (2007 ROE). The bank's CAMELS composite rating remains a 2 as a result of the examination. OCC examiners remain concerned about the bank's large concentration in CRE loans, particularly its residential construction and land development loans, and with its dependence on credit-sensitive funding sources.
11/26/2007	OCC conducts a targeted review of Vineyard's CRE loans. The examiners conclude that Vineyard is highly concentrated in CRE and that the risk associated with its loan portfolio is increasing. The examiners also identify weakness in the bank's credit management.
1/23/2008	Vineyard's former chief executive officer (CEO) resigns involuntarily. A board member becomes the interim CEO.
1/30/2008	Vineyard's board approves a $20 million cash dividend to its holding company in violation of 12 U.S.C. § 60 and 12 C.F.R. § 5.64(b). In the 2008 ROE, OCC required that the holding company return the $20 million cash dividend to Vineyard. The holding company returned the $20 million cash dividend to Vineyard.
2/25/2008	Vineyard's former CEO and one other shareholder initiate a proxy contest in an effort to amend the bank's bylaws to elect an alternate slate of directors (if successful, the former CEO could return to his former position).
3/31/2008	OCC conducts a full-scope examination of Vineyard and assigns the bank a CAMELS composite rating of 4. The examiners conclude that Vineyard's overall condition is unsatisfactory due to large CRE concentrations, weakening economic conditions, large allowance for loan and lease losses provisions, and costs associated with problem assets. The examiners also conclude that the bank's risk profile is high, which could have an adverse effect on capital adequacy.
4/14/2008	Vineyard's former CEO and one other shareholder announce that they have received enough proxies in favor of amending the bank's bylaws, which allows them to elect a new slate of directors.
5/5/2008	OCC notifies Vineyard of its troubled condition status based on deficiencies revealed in OCC's full-scope examination (2008 ROE).
7/15/2008	Vineyard's former CEO submits a request to OCC for nonobjection under section 914 of the Financial Institutions Reform, Recovery and Enforcement Act to once again become the CEO, director, and president of Vineyard. In a letter dated July 31, 2008, OCC denies this request due to its determination that the former CEO lacks the competency to serve in that capacity.
7/22/2008	Vineyard enters into a consent order with OCC. The bank is classified as adequately capitalized for prompt corrective action (PCA) purposes. One provision of the consent order requires that Vineyard maintain a tier 1 risk-based capital ratio of 9 percent.
7/28/2008	OCC transfers supervision of Vineyard to the Special Supervision Division in Washington, D.C.

Date	Event
8/5/2008	Vineyard holds its annual meeting of shareholders, where a vote is held on the alternate slate of directors proposed during the proxy contest. The shareholders elect five of the proposed directors; two of the current directors are also elected to serve on the new board.
8/27/2008	OCC downgrades Vineyard's CAMELS composite rating to 5. The examiners conclude that Vineyard's financial condition is critically deficient, as evidenced by the bank's deteriorated asset quality, significant losses, diminished earnings, eroded capital, and strained liquidity. The examiners notify the bank that its failure is highly probable without outside financial assistance.
11/3/2008	OCC conducts a targeted review of Vineyard's asset quality and compliance with the consent order. OCC assigns the bank a CAMELS composite rating of 5. The examiners conclude that asset quality deterioration, significant liquidity concerns, and capital inadequacies cause the bank to be in poor financial condition that threatens its ongoing viability.
4/1/2009	Vineyard's holding company discloses in a Securities and Exchange Commission filing that substantial doubt exists about its ability to continue as a going concern. The NASDAQ Stock Market delists the holding company's common stock effective May 29, 2009.
4/27/2009	OCC conducts a limited-scope examination of Vineyard and assigns a CAMELS composite rating to 5. The examiners conclude that the bank's asset quality has deteriorated and that it is critically deficient, presenting an imminent threat to the bank's viability.
5/1/2009	OCC notifies Vineyard that it is significantly undercapitalized for PCA purposes. OCC requires the bank to submit a capital restoration plan by May 18, 2009. The bank, however, never submits a capital restoration plan to OCC.
6/18/2009	OCC notifies Vineyard that it is critically undercapitalized for PCA purposes and that its CAMELS capital component is downgraded to 5.
7/17/2009	OCC closes Vineyard and appoints FDIC as receiver. FDIC estimates that the loss to the Deposit Insurance Fund caused by this failure is $572.8 million.

Source: OIG analysis of OCC, FDIC, and Vineyard Bank, N.A. data.

This appendix summarizes the Office of the Comptroller of the Currency's (OCC) preconversion and safety and soundness examinations of Vineyard Bank, N.A. (Vineyard) from March 2006 through March 2008 and provides information on the significant results of those examinations. The significant results of the last examination of Vineyard performed by the California Department of Financial Institutions (DFI) and the Federal Deposit Insurance Corporation (FDIC) are also summarized in this appendix to provide perspective on the long-term nature of some of the bank's issues. We list the following items from the reports of examination (ROE): (1) matters requiring attention and (2) other issues. Generally, matters requiring attention represent the most significant items requiring corrective action and are more serious.

Date examination started	CAMELS rating	Assets ($ millions)	Significant safety and soundness corrective actions and other issues cited in memorandum of understanding or reports of examination	Enforcement action
1/10/2005 (Performed by DFI and FDIC before conversion to a national bank charter)	2/223222	$1,294	<u>Provisions in memorandum of understanding (MOU) that required further attention</u> • Increase the board of directors by adding one independent director through appointment or election at a regular or special meeting of Vineyard's shareholders. • Implement a capital adequacy plan containing an analysis of the capital levels necessary to address the bank's elevated risk profile. Ensure that the capital plan requires a quarterly review to ensure that adequate capital levels are maintained. • Restrict total asset growth to 25 percent per year. • Revise, adopt, and implement written lending and collection polices to provide effective guidance and control over the bank's lending function. Ensure such policies address concerns regarding concentrations of credit and underwriting deficiencies. • Revise asset liability management policy to o address the two interest rate risk model scenarios, o establish more reasonable interest rate risk limits,	MOU (effective 7/7/2004)

Date examination started	CAMELS rating	Assets ($ millions)	Significant safety and soundness corrective actions and other issues cited in memorandum of understanding or reports of examination	Enforcement action
			o develop a more practical plan to correct breaches of interest rate risk limits, o establish specific requirements for supporting interest rate risk modeling assumptions, and o ensure that independent back-testing is conducted. Other issues/recommendations in the FDIC ROE • Ensure that outsourced audit reports are received and responded to in a timely manner. • Perform and document risk assessment on individual positions within the bank and have the board of directors review and approve the results. • Perform and document a financial review of the bank's vendors to assess vendors' continuing ability to provide services to the bank.	
3/6/2006 (OCC Conversion Examination Report)	2/222222	$1,705	Corrective actions • Ensure that the appraisal ordering and review processes are clearly independent and that appraisal reviews provide more qualitative analysis. • Ensure that stress testing of commercial real estate loans is a vigorous process. • Strengthen the process to quantify the level of foreign wire activity. Other issues/recommendations • Develop contingency plans for responding to adverse commercial real estate market conditions in conjunction with the strategic planning process. • Consider including loan portfolio stratifications by concentration, industries, commercial real estate geography, and risk rating.	None
4/2/2007 (Performed by OCC)	2/222222	$2,251	Matters requiring attention • Improve financial analysis of the borrowers, principals, and guarantors in large-tract development, single-family	None

Date examination started	CAMELS rating	Assets ($ millions)	Significant safety and soundness corrective actions and other issues cited in memorandum of understanding or reports of examination	Enforcement action
			construction, and land development loans. • Improve problem loan reporting. In assigning loan grades, expand evaluation of a borrower's ability to carry a project when it needs additional funds for interest reserves or project completion. Develop support for reserve percentages assigned to criticized and classified pools. Other issues/recommendations • Continue the directors' efforts to improve their qualifications for effective oversight of the company's size, scope, and direction.	
3/31/2008 (Performed by OCC)	4/444432	$2,340	Matters requiring attention • Appoint a capable chief executive officer and chief credit officer. • Ensure that capital ratios do not fall below the following levels until the board ensures effective reduction in the overall risk profile and establishment of sound asset quality and profitability: o Tier 1 capital equal to at least 9 percent of adjusted total assets (leverage ratio). o Total Tier 1 and Tier 2 capital equal to at least 11 percent of risk-weighted assets (total risk-based capital ratio). • Ensure that the board develops and implements a 3-year capital plan to include o specific plans for the maintenance of adequate capital, o projections for the sources and timing of additional capital to meet the bank's current and future needs, o primary and contingent sources of capital, and o a dividend policy that permits the declaration of a dividend only when the bank complies with its approved	Consent order, effective 7/22/2008

Date examination started	CAMELS rating	Assets ($ millions)	Significant safety and soundness corrective actions and other issues cited in memorandum of understanding or reports of examination	Enforcement action
			capital program and with 12 U.S.C. §§ 56 and 60 and has received prior written approval by the OCC. • Reassess the system for managing concentrations of credit and take action where necessary to make the system more effective. Ensure adherence to a written asset diversification program consistent with Concentrations of Credit (section 216) of the Comptroller's Handbook. Vineyard should take actions that include, but are not limited to, the following: o Review current policies, processes, and procedures to control and monitor concentrations of credits. Where concentration risk management is deficient for adequately controlling risk, revise the area to ensure effectiveness. Ensure appropriate attention to the impact of commitments. o Review the balance sheet to identify additional concentrations of credit. Consider the existence of any additional concentrations within those already identified, such as property types within commercial real estate mortgages or segmentation by geographic location or submarket. o Provide written analysis of any concentration of credit to identify and assess the inherent credit, liquidity, and interest rate risks. Include management's abilities and the risk of factors beyond bank control. o Establish safe and sound and formal risk limits for each concentration based on the above. o Ensure that an action plan is approved by the board to reduce the risk of any concentration deemed imprudent in the above	

Date examination started	CAMELS rating	Assets ($ millions)	Significant safety and soundness corrective actions and other issues cited in memorandum of understanding or reports of examination	Enforcement action
			analysis. o Ensure that future concentrations of credit are subject to the same analysis as above and that the analysis demonstrates that the concentration will not subject the bank to undue credit, liquidity, or interest rate risks. • Adhere to sound underwriting practices by developing a policy for nonrecourse lending, including stricter guidelines than used previously. These should include, but are not limited to o higher debt service ratios, o lower loan-to-cost/loan-to-value ratios, o larger cash equity requirements, and o financially capable sponsors with incentives to support the debt. • Ensure that loan officers and credit analysts obtain complete financial and income information and thoroughly analyze the sponsor/guarantor's cash flow sources and uses to evaluate their capacity to support projects. Ensure that management strengthens the annual review process for income-producing properties and track projects that require annual reviews. • Revise the loan-grading policy and evaluate methods to ensure that officers can effectively grade credits. • Ensure that credit administration strengthens its problem loan reports by including o specific reasons to support the loan grade, o detailed action plans that include timeframes and goals with borrower commitments, and o triggers for potential risk-rating upgrades or downgrades. • Ensure compliance with the December 13, 2006, interagency policy statement on allowances for loan and lease losses	

Date examination started	CAMELS rating	Assets ($ millions)	Significant safety and soundness corrective actions and other issues cited in memorandum of understanding or reports of examination	Enforcement action
			(ALLL): o Base analysis on an effective loan-grading system. o Support the allocations for criticized and classified loan pools with an evaluation of the bank's industry historic losses for each portfolio segment adjusted for qualitative factors that affect each segment. o Base analyses conducted in accordance with Financial Accounting Standards Board Statement 114, Accounting by Creditors for Impairment of a Loan, on the source of repayment using the discounted cash flow or collateral liquidation method. Use the discounted cash flow method for tract development projects where sales continue to occur and the bank is still looking at these sales to repay the loan. o Use the unallocated portion of loans as part of the qualitative adjustments. The amount should be calculated, specifically supported, and directionally consistent between reporting periods. o Include a reasonable range for the ALLL balance. This can be determined by using estimated ranges of inherent losses or qualitative adjustments. • Develop enterprise-wide and standardized approaches to key information technology (IT) processes. The board must ensure that management develops an enterprise-wide approach to system monitoring, disaster recovery, vendor management, and quality assurance. <u>Other issues/recommendations</u> • Strengthen the annual review process for income producing properties in the permanent loan portfolio.	

Date examination started	CAMELS rating	Assets ($ millions)	Significant safety and soundness corrective actions and other issues cited in memorandum of understanding or reports of examination	Enforcement action
			• Clearly justify in appraisal review reports the use of escrows and document discussions with appraisers when appraisal values are adjusted. • Consider in ALLL analysis the results from stress testing on multifamily and commercial real estate portfolios. • Increase IT management efforts to ensure that IT staff complete routine activities on time.	

Source: OIG analysis of OCC ROEs.

Since November 2008, we have completed ten mandated material loss reviews of failed banks regulated by the Office of the Comptroller of the Currency (OCC) in addition to our review of Vineyard Bank, N.A.[16] This appendix provides recommendations made to OCC resulting from these reviews. With one exception as footnoted in this appendix, OCC management concurred with the recommendations and has taken or planned corrective actions that are responsive to the recommendations. In certain instances, the recommendations address matters that require ongoing OCC management and examiner attention.

Report Title	**Recommendations to the Comptroller of the Currency**
Safety and Soundness: Material Loss Review of ANB Financial, NA, OIG-09-013 (Nov. 25, 2008) OCC closed ANB Financial and appointed the Federal Deposit Insurance Corporation (FDIC) as receiver on May 9, 2008. At that time, FDIC estimated that ANB Financial's failure would cost the Deposit Insurance Fund $214 million. FDIC's estimated cost to the Deposit Insurance Fund associated with ANB Financial's failure increased to $819 as of October 31, 2009.	Re-emphasize to examiners that they must closely investigate an institution's circumstances and alter the supervisory plan if certain circumstances exist as specified in OCC's Examiner's Guide to Problem Bank Identification, Rehabilitation, and Resolution. Re-emphasize to examiners that formal enforcement action is presumed warranted when certain circumstances specified in OCC's Enforcement Action Policy (PPM 5310-3) exist. Examiners should also be directed to document in the examination files the reason for not taking formal enforcement action if those circumstances do exist. Reassess guidance and examination procedures in the Comptroller's Handbook related to bank use of wholesale funding with a focus on heavy reliance on brokered deposits and other nonretail deposit funding sources for growth. Establish in policy a "lessons-learned" process to assess the causes of bank failures and the supervision exercised over the institution and to take appropriate action to address any significant weaknesses or concerns identified.
Safety and Soundness: Material Loss Review of First National Bank of Nevada and First Heritage Bank, NA, OIG-09-033 (Feb. 27, 2009) OCC closed First National Bank of Nevada and First Heritage Bank on July 25, 2008, and appointed FDIC as receiver. As of December 31, 2008, FDIC estimated a loss to the Deposit	Re-emphasize to examiners the need to ensure that banks take swift corrective actions in response to examination findings. Re-emphasize to examiners OCC's policy on the preparation of supervision workpapers (that is, workpapers are to be clear, concise, and readily understood by other examiners and reviewers).

[16] One material loss review was performed by a contractor under our supervision.

Report Title	Recommendations to the Comptroller of the Currency
Insurance Fund of $706 million for First National Bank of Nevada and $33 million for First Heritage Bank.	
Safety and Soundness: Material Loss Review of the National Bank of Commerce, OIG-09-042 (Aug. 6, 2009) OCC closed the National Bank of Commerce and appointed FDIC as receiver on January 16, 2009. As of June 30, 2009, FDIC estimated that the bank's failure would cost the Deposit Insurance Fund $92.5 million.	Conduct a review of investments by national banks for any potential high-risk concentrations and take appropriate supervisory action. Reassess examination guidance regarding investment securities, including government-sponsored enterprise securities.
Safety and Soundness: Material Loss Review of Ocala National Bank, OIG-09-043 (Aug. 26, 2009) OCC closed Ocala National Bank and appointed FDIC as receiver on January 30, 2009. As of August 7, 2009, FDIC estimated that the bank's failure would cost the Deposit Insurance Fund $99.6 million.	Caution examiners and their supervisors that it is incumbent that they support and document CAMELS ratings, including those that did not change from prior examinations, and support decisions not to take enforcement action. Remind examiners that it is prudent to expand examination procedures for troubled or high-risk banks to review the appropriateness of (a) dividends and (b) payments to related organizations, particularly when the dividends or payments may benefit bank management and board members. OCC should reassess and revise examination guidance related to when expanded reviews of dividends and related organizations should be performed.
Safety and Soundness: Material Loss Review of TeamBank, National Association, OIG-10-001 (Oct. 7, 2009) OCC closed TeamBank, N.A., and appointed FDIC as receiver on March 20, 2009. As of September 18, 2009, FDIC estimated that the bank's failure would cost the Deposit Insurance Fund $98.4 million.	Emphasize to examiners that matters requiring attention are to be issued in reports of examination in accordance with the criteria regarding deviations from sound management and noncompliance with laws or policies listed in the Comptroller's Handbook. Emphasize to examiners the need to (a) adequately assess the responsibilities of a controlling official (chief executive officer/president, for example) managing the bank to ensure that the official's duties are commensurate with the risk profile and growth strategy of the institution; (b) review incentive compensation and bonus plans for executives and loan officers; and (c) ensure that banks conduct transactional and portfolio stress testing when appropriate.

Report Title	Recommendations to the Comptroller of the Currency
Safety and Soundness: Material Loss Review of Omni National Bank, OIG-10-017 (Dec. 9, 2009) OCC closed Omni National Bank and appointed FDIC as receiver on March 27, 2009. As of October 31, 2009, FDIC estimated that the bank's failure would cost the Deposit Insurance Fund $288.2 million.	Review OCC processes to ensure that more timely enforcement action is taken once the need for such action is identified.[17] Impress upon examiner staff the importance of completing all activities in annual supervisory cycles, including quarterly monitoring. In this regard, supervisors should ensure that quarterly monitoring activities are scheduled and carried out. Implement a policy for examiner-in-charge rotation for midsize and community banks.
Safety and Soundness: Material Loss Review of Silverton Bank, National Association, OIG-10-033 (Jan. 22, 2010) OCC closed Silverton Bank and appointed FDIC as receiver on May 1, 2009. As of October 31, 2009, FDIC estimated that the bank's failure would cost the Deposit Insurance Fund $608.3 million. FDIC also estimated an additional loss of $649.6 million to its Transaction Account Guarantee Program for a total loss of $1.26 billion from Silverton's failure.	Promptly assign an EIC and ensure continuous supervisory coverage of converted institutions, to include the timely initiation of the first full-scope examination after conversion. Ensure that appropriate actions are taken to amend or reinforce OCC guidance in response to the lessons learned review of the Silverton failure. In particular, OCC should (1) determine that banks seeking conversion to a national charter satisfactorily address significant deficiencies identified by OCC or prior regulators before approval and (2) formalize the process for second level reviews of charter conversions.
Safety and Soundness: Material Loss Review of Citizens National Bank, OIG-10-038 (Mar. 22, 2010) OCC closed Citizens National Bank and appointed FDIC as receiver on May 22, 2009. As of January 29, 2010, FDIC estimated that the loss would be $26 million.	Due to the complexity of the risk-based capital treatment of structured investment securities, assess the adequacy of OCC Bulletin 2009-15, Investment Securities, after it has been in use for a reasonable time. Work with OCC's regulatory partners to determine whether to propose appropriate legislation and/or change regulatory guidance to establish limits or other controls for bank investments.

[17] OCC did not agree with this recommendation. In its response to our report, OCC asserted that current policies are sufficient to ensure that timely enforcement action is taken. We accepted its position with respect to its current processes and consider the recommendation closed.

Report Title	Recommendations to the Comptroller of the Currency
Safety and Soundness: Material Loss Review of Union Bank, National Association, OIG-CA-10-009 (May 11, 2010) (Review performed by Mayer Hoffman McCann P.C., an independent certified public accounting firm, under the supervision of the Treasury Office of Inspector General) OCC closed Union Bank and appointed FDIC as receiver on August 14, 2009. As of January 26, 2010, FDIC estimated that the bank's failure would cost the Deposit Insurance Fund $54.5 million.	OCC work with its regulatory partners to determine whether to propose legislation and/or change regulatory guidance to establish limits or other controls for concentrations that pose an unacceptable safety and soundness risk and determining an appropriate range of examiner response to high risk concentrations.

MEMORANDUM

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

To: Donald P. Benson, Audit Director

From: John C. Dugan, Comptroller of the Currency /s/

Date: June 23, 2010

Subject: Response to Material Loss Review of Vineyard Bank, N. A. Corona, California

We have received and reviewed your draft report titled "Material Loss Review of Vineyard Bank, N. A." Your overall objectives were to determine the cause of the failure of Vineyard Bank, N.A. (Vineyard) and assess the OCC's supervision of the bank, including implementation of the Prompt Corrective Action (PCA) provisions of section 38(k).

You concluded that Vineyard failed because of significant losses in its commercial real estate loan portfolio given its pursuit of an aggressive growth strategy beginning in 2001. Vineyard's board and management did not adequately control concentration risk or ensure that credit underwriting and administrative controls were adequate. You also determined that weak controls led to deterioration in underwriting standards and the origination of high-risk loans. These deficiencies were made worse by the decline in the real estate market and borrowers' inability to pay off loans as they matured. Your report concludes that the OCC should have deferred approval of Vineyard's conversion to a national charter until weaknesses identified at the pre-conversion examination had been addressed.

We acknowledge your reaffirmation of two prior recommendations relating to the charter conversion process. As discussed in our response to that earlier report, appropriate steps have been taken to address the recommendations.

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

Boston Audit Office

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Department of the Treasury

Deputy Secretary
Office of Strategic Planning and Performance Management
Office of Accounting and Internal Control

Office of the Comptroller of the Currency

Comptroller of the Currency
Liaison Officer

Office of Management and Budget

OIG Budget Examiner

United States Senate

Chairman and Ranking Member
Committee on Banking, Housing, and Urban Affairs

Chairman and Ranking Member
Committee on Finance

United States House of Representatives

Chairman and Ranking Member
Committee on Financial Services

Federal Deposit Insurance Corporation

Chairman
Inspector General

Government Accountability Office

Acting Comptroller General of the United States