Audit Report

OIG-11-014

SAFETY AND SOUNDNESS: Failed Bank Review of Marshall Bank, National Association

November 05, 2010

Office of Inspector General

Department of the Treasury

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

OFFICE OF
INSPECTOR GENERAL

November 05, 2010

OIG-11-014

MEMORANDUM FOR JOHN WALSH
ACTING COMPTROLLER OF THE CURRENCY
OFFICE OF THE COMPTROLLER OF THE CURRENCY

FROM: Kieu T. Rubb /s/
Director, Procurement and Manufacturing Audits

SUBJECT: Failed Bank Review of Marshall Bank, National Association

This memorandum presents the results of our review of the failure of Marshall Bank, National Association (Marshall). Marshall was established in 1943 as Northwestern State Bank of Hallock, Minnesota, and converted to a national bank charter with its current name in 2003. The bank had a main office and three branches in Minnesota and was a subsidiary of Marshall BankFirst Corporation, a bank holding company established in 2002. The Office of the Comptroller of the Currency (OCC) closed Marshall and appointed the Federal Deposit Insurance Corporation (FDIC) as receiver on January 29, 2010. At September 30, 2009, the bank had $59.9 million in total assets. FDIC estimated that the loss to the Deposit Insurance Fund (DIF) is $4.1 million.

Because the loss to the Deposit Insurance Fund is less than $200 million, as set forth by section 38(k) of the Federal Deposit Insurance Act (FDIA), we conducted a review of the failure of Marshall that was limited to (1) ascertaining the grounds identified by OCC for appointing the FDIC as receiver and (2) determining whether any unusual circumstances exist that might warrant a more in-depth review of the loss. In performing our review we (1) examined documentation related to the appointment of FDIC as receiver, (2) reviewed OCC reports of examination, and (3) interviewed OCC personnel.

We conducted this performance audit during August and September 2010 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Causes of Marshall's Failure

The primary causes of Marshall's failure were (1) aggressive growth in its commercial real estate (CRE) loan portfolio which included loans originated by the bank and loan participations purchased from an affiliate, BankFirst;[1] (2) ineffective board and management that lacked independence from affiliates; and (3) weak underwriting and credit administration by both Marshall and BankFirst. Marshall and BankFirst were both owned by Marshall BankFirst Corporation and the two banks shared management and board members. With the economic downturn, a significant amount of loan participations purchased from BankFirst were subsequently charged off as losses resulting in diminished earnings and capital and, ultimately, Marshall's failure.

Conclusion

Based on our review of the causes of Marshall's failure and the grounds identified by OCC for appointing FDIC as receiver, we determined that there were no unusual circumstances surrounding the bank's failure or the supervision exercised by OCC. Accordingly, we have determined that a more in-depth review of the bank's failure by our office is not warranted.

We provided a draft of this memorandum to OCC management for comment. In its response, OCC stated it agreed with our conclusion as to the causes of Marshall's failure and had no concerns with our determination that an in-depth review of the bank's failure was not warranted. The response is provided as Attachment 1. A list of the recipients of this memorandum is provided as Attachment 2.

We appreciate the courtesies and cooperation provided to our staff during the audit. If you have any questions, you may contact me at (202) 927-5904 or Deborah Harker, Audit Manager, at (202) 927-5762.

Attachments

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[1] BankFirst was a state member bank headquartered in Sioux Falls, South Dakota, regulated by the South Dakota Division of Banking and the Federal Reserve Bank of Minneapolis under delegated authority of the Board of Governors of the Federal Reserve System. BankFirst was closed and FDIC named receiver on July 17, 2009. On August 19, 2009, FDIC estimated the loss to the DIF was $90.0 million and total assets were $246.1 million. The Board of Governors of the Federal Reserve System Office of Inspector General completed a material loss review on the BankFirst failure and issued its report on February 19, 2010. The report stated that BankFirst failed because its Board of Directors and management did not establish a corporate governance and oversight framework to control the risks associated with its aggressive loan growth and high concentration in CRE loans.

MEMORANDUM

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

To: Kieu T. Rubb, Director, Procurement and Manufacturing Audits

From: John Walsh, Acting Comptroller /s/

Date: October 25, 2010

Subject: Response to Failed Bank Review of Marshall Bank, National Association

We have received and reviewed your draft report titled "Failed Bank Review of Marshall Bank, National Association (Marshall)." Because the loss to the Deposit Insurance Fund is less than $200 million, as set forth by section 38(k) of the Federal Deposit Insurance Act, you conducted a review of the failure of Marshall that was limited to: (1) ascertaining the grounds identified by the OCC for appointing the FDIC as receiver; and, (2) determining whether any unusual circumstances exist that might warrant a more in-depth review of the loss. In performing your review you: (1) examined documentation related to the appointment of FDIC as receiver; (2) reviewed OCC reports of examination; and, (3) interviewed OCC personnel.

You conducted this performance audit during August and September 2010 in accordance with generally accepted government auditing standards. Those standards require that you plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for your findings and conclusions based on your audit objectives. You believe that the evidence obtained provides a reasonable basis for your findings and conclusions based on your audit objectives.

You concluded that the primary causes of Marshall's failure were aggressive growth in its commercial real estate loan portfolio, which included loans originated by the bank and loan participations purchased from an affiliate, BankFirst; ineffective board and management that lacked independence from affiliates; and, weak underwriting and credit administrations by both Marshall and BankFirst. We agree.

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

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

Department of the Treasury

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