



# **TEXAS DEPARTMENT OF BANKING**

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## **SUPERVISORY MEMORANDUM – 1005**

**October 25, 2023**

**TO:** All State-Chartered Banks  
All Bank and Trust Examining Personnel

**FROM:** Charles G. Cooper, Banking Commissioner

**SUBJECT:** Policy on Enforcement Actions for State-Chartered Banks<sup>1</sup>

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### **OVERVIEW**

The purpose of this Memorandum is to set forth the circumstances under which enforcement actions are used by the Department of Banking (Department) with regard to the banks and bank holding companies<sup>2</sup> under its regulation, and to specify the general methodology which is followed. An enforcement action is designed to address and correct specific problems identified within the financial and operational affairs of a banking institution, and is an essential element of effective regulation.

### **PUBLIC DISCLOSURE OF ENFORCEMENT ACTIONS**

Other than final Prohibition or Removal Orders, Department enforcement actions, whether informal or formal, are confidential. The Banking Commissioner (Commissioner) has discretion to publicize final Cease and Desist Orders, final Administrative Penalty Orders, Orders of Supervision, and Orders of Conservatorship if the Commissioner concludes that the release would enhance effective enforcement of the order.

### **DEFINITIONS**

“Management” includes bank officers as well as bank directors.

“Regulatory responses” are actions taken by the Department in response to particular conditions at a bank. They include informal communications as well as enforcement actions.

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<sup>1</sup> This Supervisory Memorandum revises and supersedes the Memorandum issued on February 19, 2013. The revisions generally update this Memorandum to reflect changes in state banking statutes enacted by the 88<sup>th</sup> Legislature.

<sup>2</sup> Pursuant to Texas Finance Code Sections 201.009(a) and 202.005(a)(2), the Commissioner may bring an enforcement action against a bank holding company that controls a Texas bank to the same extent as if the bank holding company were a Texas state bank. Therefore, statements in this Memorandum referring to state banks or persons associated with state banks also apply to bank holding companies or persons associated with bank holding companies.

## **POLICY FOR IMPLEMENTING ENFORCEMENT ACTIONS**

Regulatory responses are initiated whenever the Department becomes aware of situations or issues that weaken the safety and soundness of an institution, or that arise from noncompliance with policies, procedures, regulations, or laws.

To assure uniformity of action and to ensure that supervisory efforts are directed to banks exhibiting elevated risk profiles or other major deficiencies, the general policy of the Department is to initiate enforcement actions on banks with composite CAMELS ratings of “3,” “4,” or “5.” (The CAMELS rating system is defined in Supervisory Memorandum – 1001.) Banks rated “1” or “2” generally do not warrant an enforcement action, although the Department may initiate one depending on the specific circumstances of the institution. In particular, banks have Information Technology examinations and Bank Secrecy Act examinations that may reveal the need for an enforcement action even though the bank has a composite rating of “1” or “2.”

Enforcement actions often set forth the practices, conditions, and violations giving rise to the particular problems or weaknesses identified. The actions also outline specific corrective measures, often including appropriate time frames and goals for achievement. Specific types of enforcement actions available to the Department are outlined below in the section, “Types of Enforcement Actions.”

The Department’s enforcement actions are not part of a hierarchy; they are not designed to build on one another. On a case-by-case basis, the Department thoroughly analyzes the situation at the bank and designs the action it believes to be the most effective in curing the bank’s adverse conditions.

### ***Bank Ratings***

#### ***1-Rated Banks***

A composite “1” rating implies that a bank is sound in all respects and that any weaknesses or deficiencies are so insignificant or immaterial that they pose no supervisory concern. Regulatory responses are generally limited to informal requests for future plans and/or a written response from the bank regarding the examiner's findings as indicated in the report of examination.

#### ***2-Rated Banks***

Banks having a composite rating of “2” are fundamentally sound. Identified weaknesses or deficiencies are generally of a moderate nature and correction is attainable in the normal course of business. Regulatory responses are the same as for 1-rated banks; however, a Board Resolution may be initiated depending on specific circumstances encountered. In instances of repeated or willful law violations and/or continuing unsound banking practices, the issuance of a stronger enforcement action may be warranted.

#### ***3-Rated Banks***

A composite “3” rating implies that a bank has weaknesses which, if not corrected, could worsen into a more severe situation. Regulatory responses will most likely be enforcement actions which require remedial action.

*4 and 5-Rated Banks*

Banks with composite ratings of “4” or “5,” by definition, have problems of sufficient severity to warrant a strong regulatory response. An enforcement action such as a Cease and Desist Order is issued when there is evidence of unsafe and unsound practices or conditions. Exceptions to this policy are considered only when the condition of the bank clearly reflects significant improvement resulting from an effective correction program or where individual circumstances militate against the appropriateness or feasibility of strong enforcement actions.

**TYPES OF ENFORCEMENT ACTIONS**

Enforcement actions are either formal or informal. With the exception of determination letters, informal enforcement actions are voluntary commitments made by bank management designed to correct identified deficiencies and ensure compliance. Formal enforcement actions are generally more severe and result in an order issued by the Commissioner. Banks have a statutory right of appeal from formal enforcement actions to which they have not agreed.

**A. Informal Enforcement Actions***Board Resolutions:*

A Board Resolution is a statement adopted by the board of directors of a bank that specifies corrective actions the board of directors will take. It is issued either on management's own volition or at the request of the Department. Board Resolutions are accepted from banks that exhibit only modest regulatory concerns.

*Memorandum of Understanding:*

A Memorandum of Understanding is an agreement between a bank and the Commissioner that sets forth specific corrective actions to be undertaken by the board of directors of a bank. This action is normally pursued with banks where management does not pose a significant regulatory concern, and where the Department believes management has the ability and the willingness to correct noted deficiencies. A Memorandum of Understanding is an agreement within the meaning of Texas Finance Code (TFC) Sections 31.002(a)(29)(C) and 35.002(a)(5). Therefore, violation of a Memorandum of Understanding is grounds for issuance of a Cease and Desist Order, and, if other conditions are met, a Supervision or Conservatorship Order. A Memorandum of Understanding may occasionally have a different title.

*Determination Letter:*

A Determination Letter is a warning issued pursuant to Section 35.001 of the TFC that the practices or condition of a bank need immediate attention to avoid the issuance of an enforcement order under the TFC. A Determination Letter includes a listing of the requirements to abate the Commissioner's determination. A Determination Letter is normally used in a bank where problems are of a serious nature, but the Commissioner believes that a more formal enforcement action may not be necessary to achieve correction.

## ***B. Formal Enforcement Actions***

### *Written Agreement:*

A Written Agreement between a bank and the Commissioner sets forth specific corrective actions to be undertaken by the board of directors of a bank and/or bank holding company. A Written Agreement is given a Commissioner's Order number. A Written Agreement is usually issued in conjunction with the Federal Reserve Bank of Dallas (Federal Reserve). The Commissioner will join with a federal agency in issuing a Written Agreement only after making the necessary findings to establish the action as a Cease and Desist Order under TFC Sections 35.002, 201.009, and 202.005. Therefore, the Commissioner may publicize a Written Agreement pursuant to Section 35.012. Written Agreements entered into with the Federal Reserve are public under federal law. The Commissioner's decision to issue a joint Written Agreement with the Federal Reserve includes a conclusion that effective enforcement of such a Written Agreement will be enhanced by its publication.

### *Cease and Desist Order:*

A Cease and Desist Order is issued pursuant to Section 35.002 of the TFC, demanding that a current or former officer, employee, or director of a state bank, or the bank itself discontinue violations and/or unsafe and unsound banking practices, and take certain affirmative action as may be necessary to correct the conditions resulting from such violations or practices. A Cease and Desist Order is deemed necessary and appropriate for serious violations and unsafe practices. Management of a bank subject to such an order would normally have demonstrated a disregard for safe and sound banking practices and/or the lack of willingness or ability to correct deficiencies on their own. If a bank agrees to enter into such an order, the order is called a Consent Order. The Commissioner may publish a final Cease and Desist Order or Consent Order pursuant to TFC Section 35.012. Cease and Desist Orders or Consent Orders entered into with the Federal Deposit Insurance Corporation (FDIC) are public under federal law. Therefore, the Commissioner will join with a federal agency in issuing a joint Cease and Desist Order or Consent Order only after making the findings required by TFC Section 35.012.

### *Order of Removal or Prohibition:*

A Removal or Prohibition Order is issued pursuant to Section 35.003 of the TFC if the Commissioner finds that a present or former officer, director, employee, controlling shareholder, or other person participating in the affairs of a state bank has committed or participated in violations of law or agreements, and/or unsafe and unsound banking practices, or made false entries, which caused certain effects, and which were done in other than an inadvertent or unintentional manner. Such orders have the effect of removing a person from office or employment or prohibiting a person from office, employment, or any further participation in the affairs of a state bank or any other entity chartered, registered, permitted, or licensed by the Commissioner. The Commissioner must publish all final Removal and Prohibition Orders.

Pursuant to Section 31.105(c-2) of the TFC, if an officer, director, employee, controlling shareholder, or other person participating in the affairs of a state bank refuses to comply with a subpoena issued under Section 31.105, the Commissioner may issue an order on an

emergency basis removing the person from the person's position and prohibiting the person from participating in the affairs of the state bank or any other entity chartered, registered, permitted, or licensed by the Commissioner until the person complies with the subpoena.

*Order of Supervision:*

Pursuant to Section 35.101 of the TFC, upon determining that a bank is in hazardous condition as defined by TFC Section 31.002(a)(29), the Commissioner may issue an Order of Supervision without prior notice to appoint an individual as a supervisor of the bank. Supervision is generally used in situations where the Commissioner has little confidence in the ability or willingness of the management of the bank to follow safe and sound banking practices. The authority of a supervisor, (enumerated under TFC Section 35.106), includes acting as the Commissioner's on-site observer and agent to assure, through approval authority and/or moral suasion, that the bank is operated properly and in accordance with law and the enforcement action.

*Order of Conservatorship:*

An Order of Conservatorship may be issued by the Commissioner pursuant to Section 35.102 of the TFC when it is determined that a bank is in hazardous condition and immediate and irreparable harm is threatened to the bank, its depositors, creditors or shareholders, or the public. Under TFC Section 35.107, the board of directors may not direct or participate in the affairs of the bank during conservatorship. An appointed conservator immediately takes charge of the bank, its property, books and records, and affairs on behalf of and at the direction and control of the Commissioner.

*Administrative Penalties:*

If a bank or person commits applicable violations of law or a Commissioner's order (see Section 35.009 of the TFC), the Commissioner may seek to assess monetary fines or penalties. The bank or person is notified that a hearing will be held to determine whether administrative penalties will be assessed. Unless the violation is of a Commissioner's order, the bank or person will be given an opportunity to correct the action and reduce or avoid the penalty. Section 35.010(b) of the TFC sets out factors the Commissioner must consider when setting the penalty and Section 35.010(c) sets out minimum and maximum penalty amounts.

## **PROCEDURE FOR IMPLEMENTING ENFORCEMENT ACTIONS**

Board Resolutions, Memorandums of Understanding and Determination Letters are normally handled through written correspondence with the board of directors of a bank. Nevertheless, they may require a special meeting of the board of directors. Other enforcement actions usually require a special meeting of the directorate of the bank and generally such meetings are conducted by senior Department officials, including a member of the legal staff, at the Austin headquarters office. If an enforcement action is a joint action with a federal agency, the board meeting may occur at the federal agency's regional office.

Follow-up by examining personnel on enforcement actions is conducted in accordance with the Department's examination priorities unless variance from policy is deemed necessary. A bank that

is placed under Supervision or Conservatorship will have the appointed supervisor or conservator assist in monitoring compliance with enforcement orders.