



## **Failed Bank Review**

**Citizens Bank | Sac City, Iowa**

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**March 2024**

**AEC Memorandum No. 24-02**

AEC Memorandum  
**Audits, Evaluations, and Cyber**





## NOTICE

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**Memorandum To:** Doreen R. Eberley  
Director, Division of Risk Management Supervision

**From:** Terry L. Gibson  
Assistant Inspector General for Audits, Evaluations, and Cyber

**Subject** | **Failed Bank Review** | Citizens Bank | Sac City, Iowa |  
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## Background

On November 3, 2023, the Iowa Division of Banking (IDOB) closed Citizens Bank and appointed the Federal Deposit Insurance Corporation (FDIC) as receiver. Originally established in 1929, Citizens Bank was a state-chartered, non-member bank in Sac City, Iowa. Citizens Bank was wholly owned by the Citizens Holding Company, Sac City, Iowa, which was 100 percent owned by the Thomas Lange family. Chairman and President Thomas Lange owned 48.7 percent of the holding company stock and his wife owned an additional 24.8 percent. Their three children owned the remaining shares.

According to the FDIC's Division of Finance, the estimated loss to the Deposit Insurance Fund (DIF) was \$14.8 million or 23 percent of the bank's \$65 million in total assets. Following a period of supervisory actions by regulators, the IDOB took possession and closed Citizens Bank during an ongoing examination because FDIC and IDOB examiners found significant loan losses in the loan portfolio. These loan losses eroded the institution's capital and earnings position and the bank had become insolvent.<sup>1</sup>

This Memorandum examines whether the subject bank failure warrants an In-Depth Review.<sup>2</sup>

In conducting this Failed Bank Review, we assessed key documents related to the bank's failure, including the Division of Risk Management Supervision's Supervisory History, the

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<sup>1</sup> According to Iowa Code, the superintendent may, without prior notice or hearings, order a state bank to cease to carry on its business whenever the superintendent determines that the state bank is insolvent or is otherwise in such condition that it is unsound, unsafe, or inexpedient for it to transact business. Upon ordering a state bank to cease to carry on its business, the superintendent shall immediately appoint the FDIC as receiver. Iowa Code § 524.224(1)(d), (2).

<sup>2</sup> When the DIF incurs a loss under \$50 million, the Federal Deposit Insurance Act requires the Inspector General of the appropriate federal banking agency to determine the grounds identified by the state or federal banking agency for appointing the FDIC as receiver and to determine whether any unusual circumstances exist that might warrant an In-Depth Review of the loss. Federal Deposit Insurance Act, 12 U.S.C. § 1831o(k)(5). An In-Depth Review is a formal evaluation of the FDIC's supervision of the failed institution, including the FDIC's implementation of the Prompt Corrective Action (PCA) provisions of Section 38 of the Federal Deposit Insurance Act. We address our self-developed criteria for triggering an In-Depth Review in the OIG Analysis section of this memorandum.

Division of Resolutions and Receiverships' Failing Bank Case, and examination and visitation reports dated 2014, 2015, 2017, 2018, 2020, 2021, 2022, and 2023.<sup>3</sup>

## Causes of Failure

Based on our review of key FDIC documents, Citizens Bank's failure occurred due to the Board and management's lax lending practices and failure to properly administer large commercial trucking relationships. In 2014, Citizens Bank began making commercial loans to trucking entities without sufficient risk management practices, adequate expertise, and sufficient Board oversight. By June 30, 2023, the bank had a significant exposure to commercial trucking loans (310 percent of Tier 1 Capital and Allowance for Credit Losses), with these loans accounting for 43 percent of the bank's portfolio.

The financial condition of many of these borrowers worsened as the commercial trucking industry faced supply-chain issues and increased costs of fuel, insurance, and repairs during the 2020 to 2022 timeframe. Citizens Bank compounded these issues by advancing additional funds to problem borrowers through overdrafts, often in excess of the State's lending limit, and without first obtaining current financial information or conducting proper collateral analysis. The significant deterioration in the bank's loan portfolio and operating losses led to a serious depletion of the bank's capital and stressed its liquidity, ultimately resulting in its failure.

## FDIC Supervision

Citizens Bank provided traditional consumer and commercial loan and deposit products to its local community. Agriculture is the main industry in the trade area and historically, agricultural loans to borrowers around Sac City, Iowa were the primary driver of profitability and risk for Citizens Bank. However, from 2020 to 2023, management increased the volume of trucking operation loans in and outside of the bank's primary trade area. This, coupled with the bank's poor credit underwriting and administration practices, resulted in significantly increased risks and regulatory concerns.

The March 9, 2020 FDIC examination of Citizens Bank included Matters Requiring Board Attention (MRBA),<sup>4</sup> which recommended that the Board improve the bank's credit administration policies and practices to address concerns over the bank's ability to effectively manage credit risks. The subsequent April 2021 State and July 2022 FDIC examination reports included repeated instances of inadequate loan underwriting and credit administration deficiencies, in addition to violations of Iowa's legal lending limits.<sup>5</sup> As a result, the bank's asset quality continued to deteriorate and contribute to capital concerns. In January 2023, the FDIC and IDOB imposed a Memorandum of Understanding (MOU)<sup>6</sup> in which the Board agreed to address the examinations' concerns, including previously reported MRBAs.

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<sup>3</sup> This review does not constitute an audit conducted in accordance with Generally Accepted Government Auditing Standards.

<sup>4</sup> MRBA are issues or risks of significant importance that require the bank Board's attention.

<sup>5</sup> According to Iowa Code, a state bank may grant loans and extensions of credit to one borrower in an amount not to exceed 15 percent of the state bank's aggregate capital, as defined in section 524.103. Iowa Code § 524.904(2).

<sup>6</sup> An MOU is an informal action and agreement used by regulatory agencies to obtain a commitment from a bank's Board of Directors to implement corrective measures.

A joint visitation<sup>7</sup> by the FDIC and IDOB in May 2023 found the overall condition of the bank to be critically deficient and downgraded Citizens Bank’s composite rating from a “3” (Less Than Satisfactory) to “4” (Deficient).<sup>8</sup> Examiners attributed the rapid decline in the bank’s condition to Board and management inaction in addressing previous examination findings, resulting in repeat regulatory criticisms, and apparent violations of laws and regulations. To address the issues identified during the visitation, the FDIC and IDOB issued a Consent Order<sup>9</sup> on August 1, 2023. The provisions in the Consent Order required the bank to, among other things, engage a loan consultant, restrict overdrafts, develop risk reduction plans, limit the extension of credit to adversely classified borrowers, and maintain minimum liquidity and capital requirements. Further, the bank was required to provide progress reports to the FDIC and State regulators within 30 days of each calendar quarter.

During the August 2023 joint examination by the FDIC and IDOB, examiners found that significant losses in the loan portfolio had eroded the institution’s capital and earnings position. Further, the bank failed to adequately address and respond to the provisions of the MOU and Consent Order. On October 2, 2023, the FDIC and IDOB issued an interim CAMELS rating downgrade letter to the Board, assigning each component and composite area a “5” (Critically Deficient) rating.

The FDIC also issued a letter to the Board stating that Citizens Bank, Sac City, Iowa fell within the “Critically Undercapitalized”<sup>10</sup> position for PCA purposes as of October 2, 2023. On November 3, 2023, the IDOB closed Citizens Bank and appointed the FDIC as receiver.

## **OIG Analysis**

When conducting Failed Bank Reviews, the OIG considers a series of factors to determine whether unusual circumstances warrant further review. These factors include: (1) the magnitude and significance of the loss to the DIF in relation to the total assets of the failed institution; (2) the extent to which the FDIC’s supervision identified and effectively addressed the issues that led to the bank’s failure or the loss to the DIF; (3) indicators of fraudulent activity that significantly contributed to the loss to the DIF; and (4) other relevant conditions or circumstances that significantly contributed to the bank’s failure or the loss to the DIF.

If we learn about potential fraudulent activity during our review at the failed bank, it is our practice to refer the matter to appropriate authorities for consideration and potential action. In addition, where we identify significant programmatic weaknesses in the FDIC’s supervision, we will determine if there is a need for follow-up work and take the appropriate course of action.

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<sup>7</sup> Visitations are conducted to review the compliance posture of an institution that is newly chartered, involved in a recent or proposed merger, or recently converted to state nonmember status; to review an institution’s progress on corrective actions since its last examination; to ascertain an institution’s compliance with an enforcement action; or to investigate problems brought to the FDIC’s attention.

<sup>8</sup> Financial institution regulators evaluate a bank’s performance in six components represented by the CAMELS acronym: **C**apital adequacy, **A**sset quality, **M**anagement capabilities, **E**arnings sufficiency, **L**iquidity position, and **S**ensitivity to market risk. Examiners assign each CAMELS component and an overall, composite score, a rating of “1” (strong) through “5” (critically deficient), with “1” having the least supervisory concern and “5” having the greatest concern.

<sup>9</sup> A Consent Order is a type of formal enforcement action that is issued by regulatory agencies. The Consent Order is agreed to by a bank and contains specific provisions for improvement, usually within a specific period of time. Agencies review the bank’s progress in addressing Consent Order provisions and recommend termination of the Order when appropriate corrective actions have been taken to resolve Order provisions.

<sup>10</sup> The FDIC deems a supervised institution “Critically Undercapitalized” if it has a ratio of tangible equity to total assets that is equal to or less than 2.0 percent. 12 U.S.C. 1831o; 12 C.F.R. § 324.403(b)(5).

With respect to the first factor, the loss to the DIF in relation to Citizens Bank's total assets was 23 percent, which is consistent with average losses to the DIF of other failures within the last 5 years. Therefore, we did not find this loss to be of sufficient magnitude or significance to warrant an In-Depth Review. With respect to the second factor, we found that the FDIC's supervision identified and effectively addressed the issues that led to the bank's failure and the loss to the DIF. Specifically, the FDIC issued MRBAs to address weaknesses that led to the bank's failure, increased examination and monitoring activities, and escalated these concerns through informal and formal actions. Ultimately, the bank's inaction to address these supervisory recommendations resulted in its failure. With respect to the third factor, examiners identified multiple instances of conflicts of interest in loans administered by the bank Chairman and President and we communicated these issues to the appropriate authorities. However, we did not find that these issues significantly contributed to the loss to the DIF. With respect to the fourth factor, we did not identify other relevant conditions or circumstances that significantly contributed to the bank's failure or the loss to the DIF.

## **Conclusion**

Citizens Bank's failure occurred primarily due to insufficient Board and management oversight of its credit administration practices. Specifically, the bank issued loans to commercial trucking clients without adequate credit underwriting, risk management practices, or adequate expertise. When the commercial trucking industry began to experience supply-chain and financial issues, management compounded its risk by extending credit through overdrafts, without properly assessing these additional risks. Citizen Bank's Board and management also failed to complete recommended corrective actions to improve the bank's safety and soundness. The significant loan losses eroded Citizens Bank's capital levels and liquidity position, and ultimately led to the bank's failure.

Our review did not find unusual circumstances that warrant an In-Depth Review of the loss.



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