



Audit Report



OIG-11-010

SAFETY AND SOUNDNESS: Failed Bank Review of Beach First National Bank

November 3, 2010

Office of
Inspector General

Department of the Treasury



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

OFFICE OF
INSPECTOR GENERAL

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MEMORANDUM FOR JOHN WALSH
ACTING COMPTROLLER OF THE CURRENCY

FROM: Jeffrey Dye /s/
Director, Banking Audits

SUBJECT: Failed Bank Review of Beach First National Bank

This memorandum presents the results of our review of the failure of Beach First National Bank (Beach First). Beach First opened in September 1996 and had a main office in Myrtle Beach, South Carolina, and seven branches located throughout South Carolina in North Myrtle Beach, Surfside Beach, Pawleys Island, and Hilton Head. The Office of the Comptroller of the Currency (OCC) closed Beach First and appointed the Federal Deposit Insurance Corporation (FDIC) as receiver on April 9, 2010. As of December 31, 2009, Beach First had approximately \$585.1 million in total assets and \$516.0 million in total deposits. FDIC has estimated that the loss to the Deposit Insurance Fund is \$130.3 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 Beach First 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) reviewed documentation related to the appointment of FDIC as receiver, (2) reviewed OCC reports of examination, and (3) interviewed OCC examination personnel.

We conducted this performance audit in 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 Beach First's Failure

The primary cause of Beach First's failure was management's aggressive growth strategy primarily concentrated in non-owner occupied commercial real-estate (CRE) within South Carolina, specifically vacation homes in the state's coastal region. Beach First's management underwrote CRE loans with variable interest rates without establishing any lower interest rate thresholds. These loans were also funded using high-cost funding sources, including brokered deposits. When interest rates began to fall during the decline in the real estate market in 2007, the bank's interest income was not sufficient to cover the high-cost of funding, resulting in negative net interest income.

Poor credit risk and loan portfolio management were also causes of the bank's failure. For example, examiners found that the bank performed incomplete analyses of borrowers' financial condition and failed to obtain appropriate real estate appraisals. When the CRE market declined, the bank's asset quality deteriorated, threatening the bank's viability by adversely impacting capital and earnings. Increased loan losses and provision expenses caused the bank's capital levels to fall to critically undercapitalized, which ultimately led to the bank's failure.

Conclusion

Based on our review of the causes of Beach First'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 Beach First's failure and that it 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) 927-0384 or Rashmi Bartlett, Audit Manager, at (202) 927-5839.

Attachments



MEMORANDUM

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

To: Jeffrey Dye, Director, Banking Audits

From: John Walsh, Acting Comptroller /s/

Date: October 25, 2010

Subject: Response to Failed Bank Review of Beach First National Bank

We have received and reviewed your draft report titled "Failed Bank Review of Beach First National Bank (Beach First)." 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 Beach First 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 in 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 cause of Beach First's failure was management's aggressive growth strategy primarily concentrated in non-owner occupied commercial real estate within South Carolina, specifically vacation homes in the state's coastal region. 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 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

Deputy Secretary
Office of Strategic Planning and Evaluations
Office of Accounting and Internal Control

Office of the Comptroller of the Currency

Acting Comptroller of the Currency
Liaison Officer

Office of Management and Budget

OIG Budget Examiner