



Audit Report



OIG-11-073

SAFETY AND SOUNDNESS: Failed Bank Review of Appalachian Community Bank, F.S.B.

June 07, 2011

Office of Inspector General

Department of the Treasury



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

OFFICE OF
INSPECTOR GENERAL

June 07, 2011

OIG-11-073

MEMORANDUM FOR JOHN E. BOWMAN
ACTING DIRECTOR
OFFICE OF THRIFT SUPERVISION

FROM: Jeffrey Dye /s/
Director, Banking Audits

SUBJECT: Failed Bank Review of Appalachian Community Bank, F.S.B.

This memorandum presents the results of our review of the failure of Appalachian Community Bank, F.S.B. (Appalachian) located in McCaysville, Georgia. Appalachian was established in April 2007 and operated a main office in McCaysville and branches in North Carolina and Tennessee. The Office of Thrift Supervision (OTS) closed Appalachian and appointed the Federal Deposit Insurance Corporation (FDIC) as receiver on December 17, 2010, while the thrift was still in its de novo phase. As of September 30, 2010, Appalachian had approximately \$68.2 million in total assets and \$76.4 million in total deposits. FDIC estimated that the loss to the Deposit Insurance Fund is \$26.0 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 Appalachian that was limited to (1) ascertaining the grounds identified by OTS 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 OTS reports of examination, and (3) interviewed OTS examination personnel.

We conducted this performance audit during December 2010 and January 2011 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 Appalachian's Failure

OTS appointed FDIC as receiver based on the following grounds: (1) the thrift's assets were less than its obligations to its creditors and others, (2) the thrift was critically undercapitalized, and (3) the thrift's board of directors consented to the appointment.

The primary cause of Appalachian's failure was the thrift's high concentration in nonresidential real estate and land loans in Georgia. The thrift's management pursued a high-risk strategy to rapidly grow the institution, which resulted in total assets almost doubling from 2007 to 2008. This rapid growth represented a material change from the thrift's original business plan and included a large amount of loan participations from Appalachian Community Bank, a state chartered bank under the same holding company as Appalachian. This growth in high-risk loans without adequate loan portfolio diversification and concentration limits contributed to the increase in problem assets, which subsequently led to the erosion of capital and earnings.

Appalachian was reliant on Appalachian Community Bank for managerial and back office support, including general accounting services, information technology support, and loan operations. Appalachian failed nine months after the Georgia Department of Banking and Finance closed the state-chartered bank on March 19, 2010.

Conclusion

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

We provided a draft of this memorandum to OTS management for comment. In its response, OTS stated it agreed with our conclusion as to the causes of the failure of Appalachian Community Bank and that it concurs with our determination that an in-depth review of the bank's failure is not warranted. The response is provided as Attachment 1. A list of the recipients of this memorandum is provided as Attachment 2.

OIG-11-073

Page 3

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

**Office of Thrift Supervision**
Department of the TreasuryThomas A. Barnes
Deputy Director, Examinations, Supervision, and Consumer Protection

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May 17, 2011

MEMORANDUM FOR: Jeffrey Dye
Director, Banking Audits
Office of Inspector General
U.S. Department of the Treasury

FROM: Thomas A. Barnes /s/
Deputy Director

SUBJECT: Draft Failed Bank Review of
Appalachian Community Bank, FSB
McCaysville, GA

Thank you for the opportunity to comment on your draft memorandum entitled "Failed Bank Review of Appalachian Community Bank, FSB, McCaysville, Georgia." Because the estimated loss of \$26 million to the Deposit Insurance Fund is below the \$200 million threshold set forth in section 38(k) of the Federal Deposit Insurance Act, your office's review of the failure of Appalachian Community Bank, FSB (the Bank) was limited to ascertaining the grounds identified by OTS for appointment of the FDIC as receiver and determining whether any unusual circumstances exist warranting a more in-depth review.

The memorandum summarizes the primary causes of the Bank's failure, which are consistent with the information contained in the OTS Reports of Examination and documents provided in support of the grounds for receivership. Specifically, the memorandum cites high concentrations in nonresidential real estate and land loans in Georgia. We agree with your assessment that rapid growth in high-risk loans without loan portfolio diversification and concentration limits contributed to the increase in problem assets, which subsequently led to the erosion of capital and earnings.

Your memorandum identified no unusual circumstances surrounding the Bank's failure or the supervision exercised by OTS warranting a more in-depth review by the Office of Inspector General. Although we have not yet completed our internal failed bank review, based on our preliminary work to date we concur with your memorandum's assessment.

Jeffrey Dye
Director, Banking Audits
Office of Inspector General
May 17, 2011

-2-

We are currently in the process of completing our internal failed bank review. Nothing has come to our attention that warrants a more in-depth review. Our findings are consistent with the findings above.

Thank you again for the opportunity to review and respond to the draft failed bank review of Appalachian Community Bank, FSB. OTS appreciates the professionalism and courtesies provided by the staff of the Office of Inspector General in completing this review.

Department of the Treasury

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

Office of Thrift Supervision

Acting Director
Liaison Officer

Office of Management and Budget

OIG Budget Examiner