Office of Inspector General
Board of Governors of the Federal Reserve System
Consumer Financial Protection Bureau

Executive Summary, 2018-SR-B-007, March 19, 2018

Review of the Failure of Allied Bank

Findings

Allied Bank failed because of corporate governance weaknesses and asset quality deterioration resulting from deficient credit risk-management practices. Ineffective oversight by Allied Bank's board of directors allowed two management officials, the Special Assets Officer and the President, to exert a dominant influence over the bank's affairs, including its lending decisions, and allegedly engage in insider abuse. Allied Bank's management also failed to establish adequate credit risk-management practices commensurate with the risks in the bank's loan portfolio. Weak credit underwriting and administration practices resulted in violations of certain regulations and bank lending policies, significant loan concentrations, and an excessive volume of classified assets. The bank's asset quality deterioration significantly impaired profitability and eventually depleted capital levels, resulting in the failure.

With respect to supervision, the Federal Reserve Bank of St. Louis (FRB St. Louis) generally took decisive supervisory action to address Allied Bank's weaknesses and deficiencies during the time frame we reviewed, 2009 through 2016, by appropriately downgrading the bank's CAMELS composite rating consistent with its risk profile, increasing the frequency of examinations, and assigning more experienced staff to examinations. FRB St. Louis's supervisory activity included formal enforcement actions and a recommendation to implement enforcement actions against certain Allied Bank officials. We determined that FRB St. Louis could have taken stronger steps by recommending that the Board of Governors of the Federal Reserve System (Board) report suspicious activity to law enforcement when FRB St. Louis first identified signs of insider abuse. Our review resulted in findings related to Suspicious Activity Report filings by the Federal Reserve System and enhanced communication between the Board's Legal Division and the Reserve Banks.

Recommendations

Our report contains recommendations designed to improve supervisory processes and to enhance communication between the Board's Legal Division and Reserve Banks following requests for enforcement action. In its response to our draft report, the Board concurs with our recommendations and outlines actions to address each recommendation. We will follow up to ensure that the recommendations are fully addressed.

Purpose

In accordance with the requirements of section 38(k) of the Federal Deposit Insurance Act, as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act, we conducted an in-depth review of the failure of Allied Bank because the failure presented unusual circumstances that warranted an in-depth review.

Background

Allied Bank, formerly known as The Bank of Mulberry, Mulberry, Arkansas, began operations in 1902 as a state nonmember bank. In 1997, Allied Bank became a state member bank supervised by FRB St. Louis, jointly with the Arkansas State Bank Department. On September 23, 2016, the Arkansas State Bank Department closed the bank and appointed the Federal Deposit Insurance Corporation as receiver.