



SR003_7: Failed Bank Report

Integrity Bank

1315 West Indiantown Road
Jupiter, FL 33458

(7/12/2004 –7/31/2009)

Report Objective

This report has **two** objectives, using the bank's **data***:

1. To examine the bank finances in the quarters prior to its failure.
2. To analyze the bank finances using our Key Performance Indicator (KPI) scoring approach to determine if the bank's failure is something we could have predicted.

*Data source: FDIC and company filings.



Bank Background

FDIC Certificate #	9873
Parent Holding Company	FSB Bancorp, Inc.
Bank Charter Class	Commercial Bank
Asset Concentration	Commercial Lending Specialization
Product Specialty	Personal and Business Banking Services
Number of Branches	1 (as of June 30, 2009)
Number of Employees	15 (as of June 30, 2009)

Executives

SVP	Cindy Sheppard
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What took place?

Integrity Bank, Jupiter, FL was closed by the Florida Office of Financial Regulation, and the Federal Deposit Insurance Corporation (FDIC) was named Receiver. The estimated cost to the FDIC Deposit Insurance Fund is \$46,000,000. All deposits and roughly half of the assets acquired by Stonegate Bank in Fort Lauderdale.

Key Performance Indicators

KPI Summary for 2009 Q2	
Normalized Income Rating	Very Poor
Delinquent Asset Rating	Poor
Asset: Liability Rating	Very Poor
Real Estate Asset Rating*	Poor
Bankability Composite Score	-46.70**(Very Poor)

Possible ratings: *Excellent, Good, Moderate, Poor, Very Poor.*

*This rating is relevant to the current “financial crisis” fueled by mortgage security backed loans.

**This is out of 100.

Bank Financial Snapshot

Financial Data Overlay (thousands)			
	2008 Q2	2009 Q2	Percentage Change
Assets	\$ 139,190	\$ 105,300	↓ 24.35%
Liabilities	\$ 125,950	\$ 106,450	↓ 15.48%
Net Income	-\$ 1,030	-\$ 10,970	↓ 965.05%

- The average net income change for all FDIC banks was -176.66% in the same period.
- The average net income change for all the commercial lending specialization banks was -139.89% in the same period.
- Compared with the whole industry and other commercial lending specialization banks, Integrity Bank's decline in Net Income was relatively large (-965.05%) during 2009.

Normalized Income Analysis

	2008Q1	2008Q2	2008Q3	2008Q4	2009Q1	2009Q2
Normalized Income	-0.08%	-0.67%	-0.09%	-3.07%	-3.49%	-6.33%
SD's from Average*	-0.38	-1.07	-0.03	-2.56	-4.95	-6.38
Ranking	Moderate	Poor	Moderate	Very Poor	Very Poor	Very Poor


- Integrity Bank had a normalized income of -6.33% in the second quarter of 2009, the quarter before it failed.
- Banks of the same asset concentration hierarchy (commercial lending specialization) had an average normalized income of -0.17%. The standard deviation of the normalized incomes was 0.96%, which means that Integrity Bank was more than 6 SD's below the average.
- Since the first quarter of 2008, Integrity Bank's normalized income in relation to banks of the same asset concentration hierarchy has declined significantly.

*Average of banks of the same asset concentration hierarchy



Indicates sign of bank in financial distress

Delinquent Asset Analysis

	2008Q1 	2008Q2	2008Q3	2008Q4	2009Q1	2009Q2
Weighted Delinquent Asset	7.87%	0.23%	6.03%	2.64%	2.87%	4.89%
SD's from Average*	3.30	-0.62	2.28	0.43	0.41	1.50
Ranking	Very Poor	Good	Very Poor	Moderate	Moderate	Poor


- Integrity Bank had a weighted delinquent assets out of total assets ratio of 4.89% in the second quarter of 2009, the quarter before it failed.
- Banks of the same asset concentration hierarchy (commercial lending specialization) had an average weighted delinquent asset of 1.76%. The standard deviation of the delinquent assets was 2.07%, which means that Integrity Bank was about 1.50 SD's above the average.
- Integrity Bank's weighted delinquent assets ratio has been volatile in the 6 quarters prior to its failure.

*Average of banks of the same asset concentration hierarchy



Indicates sign of bank in financial distress

Real Estate Loan Asset Analysis

	2008Q1 	2008Q2	2008Q3	2008Q4	2009Q1	2009Q2
Real Estate Loan Asset Ratio	71.25%	70.13%	67.72%	68.80%	67.62%	66.71%
SD from Average*	1.03	0.92	0.74	0.82	0.79	0.75
Ranking	Poor	Poor	Poor	Poor	Poor	Poor


- Integrity Bank of had a R/A ratio of 66.71% in 09 Q2, the quarter before it failed.
- In 09 Q2, banks of the same asset concentration hierarchy (commercial lending specialization) had an average R/A ratio of 56.21%. The standard deviation of the R/A ratio was 14.07%, which means that Integrity Bank was actually 0.75 SD's above the average, earning the rank of "Poor".

* Average of banks of the same asset concentration hierarchy



Indicates sign of bank in financial distress

Asset: Liability Analysis

	2008Q1	2008Q2	2008Q3	2008Q4	2009Q1	2009Q2 
Asset: Liability Ratio	112.49%	110.51%	110.45%	108.46%	104.83%	98.92%
Median A/L Ratio*	110.92%	110.69%	110.65%	110.51%	110.53%	110.52%
Ranking	Moderate	Moderate	Moderate	Poor	Very Poor	Very Poor

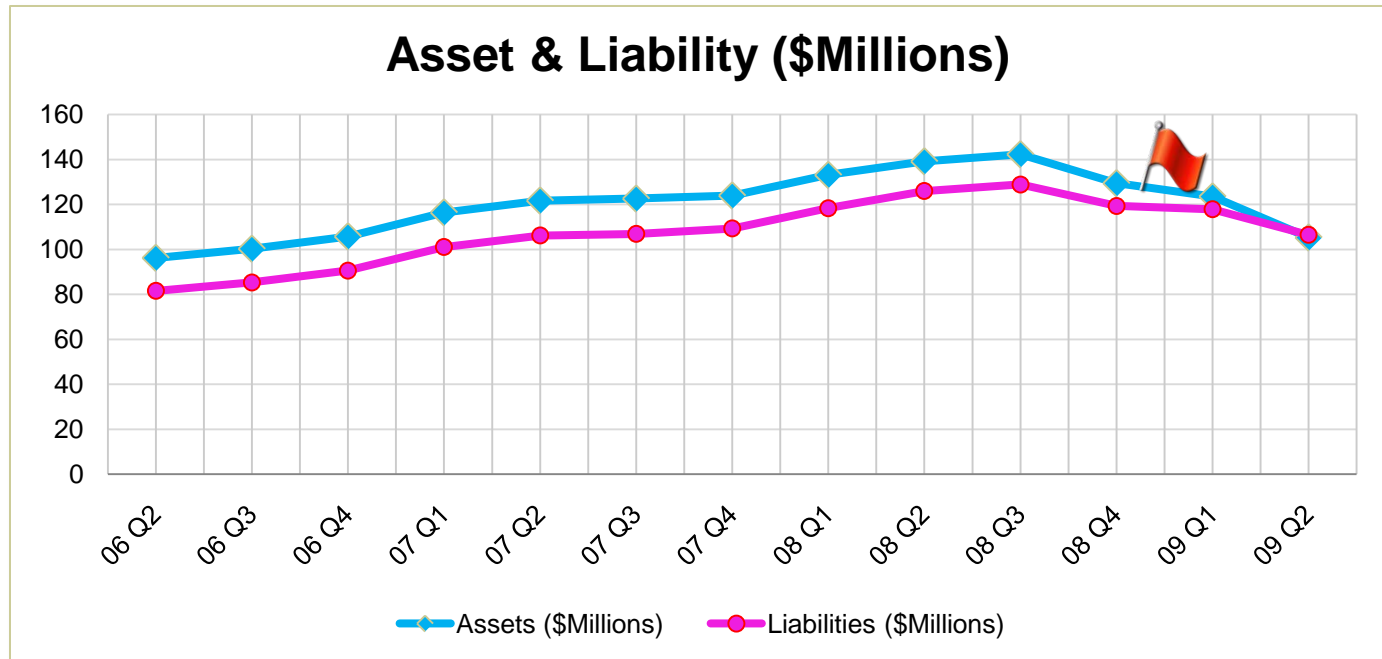
- Integrity Bank's A/L ratio had been declining in every quarter prior to its failure, and dropped to 98.92% in the quarter before it failed, where its liabilities exceeded its assets.
- The median A/L ratio for all banks in the same asset concentration hierarchy (commercial lending specialization) was 110.52% in the same period, meaning that Integrity Bank was almost 12% under the median. The median A/L ratio for all banks in 2009 Q2 was 110.98%.
- Of the 50 banks failed in 2009 Q3, 94% of them had an A/L ratio under 107%.

* Median of banks of the same asset concentration hierarchy



Indicates sign of bank in financial distress

Asset & Liability History

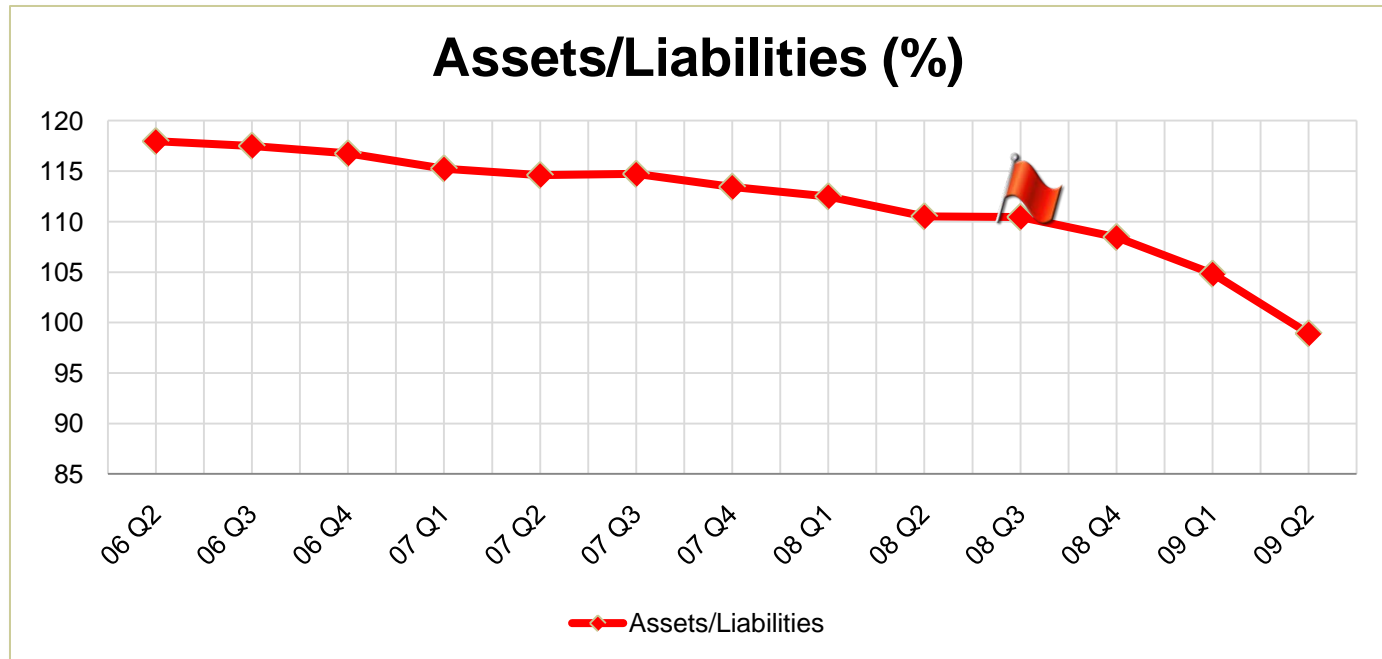


- The difference between asset and liability was getting closer in 08 Q4.



Indicates sign of bank in financial distress

Asset/Liability History

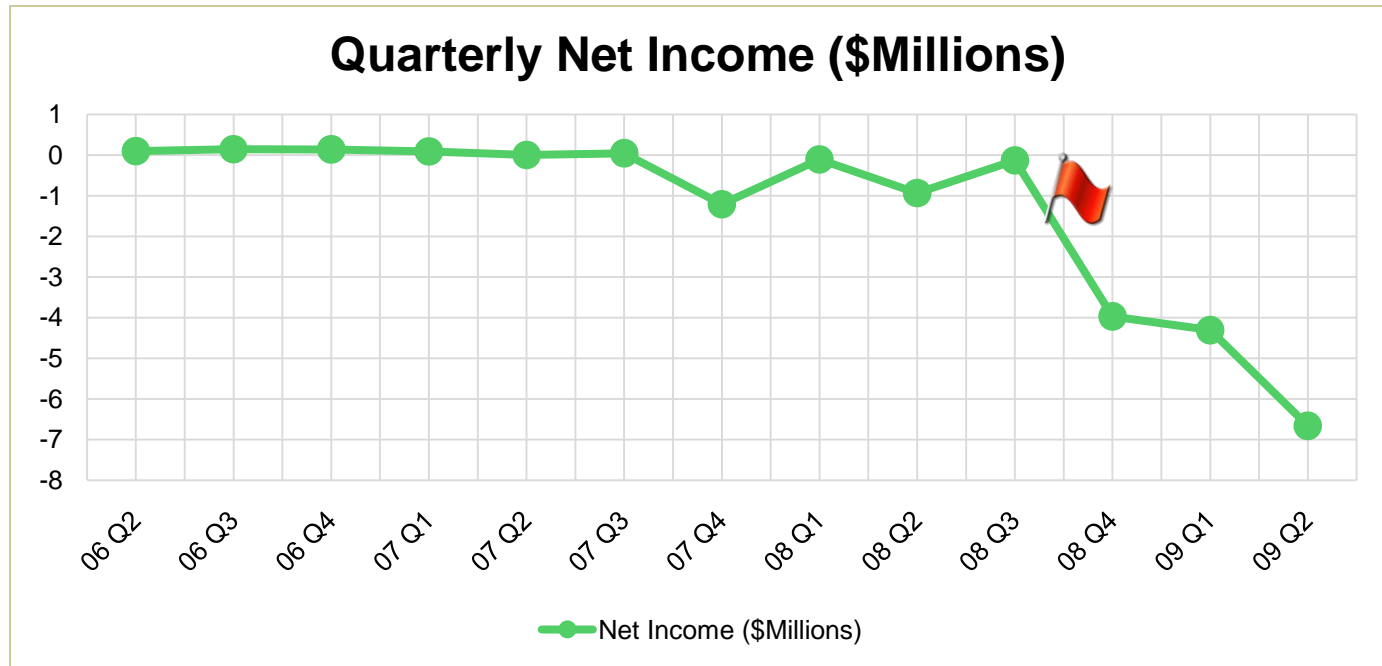


- The A/L ratio steadily declines after 08 Q2.



Indicates sign of bank in financial distress

Net Income History

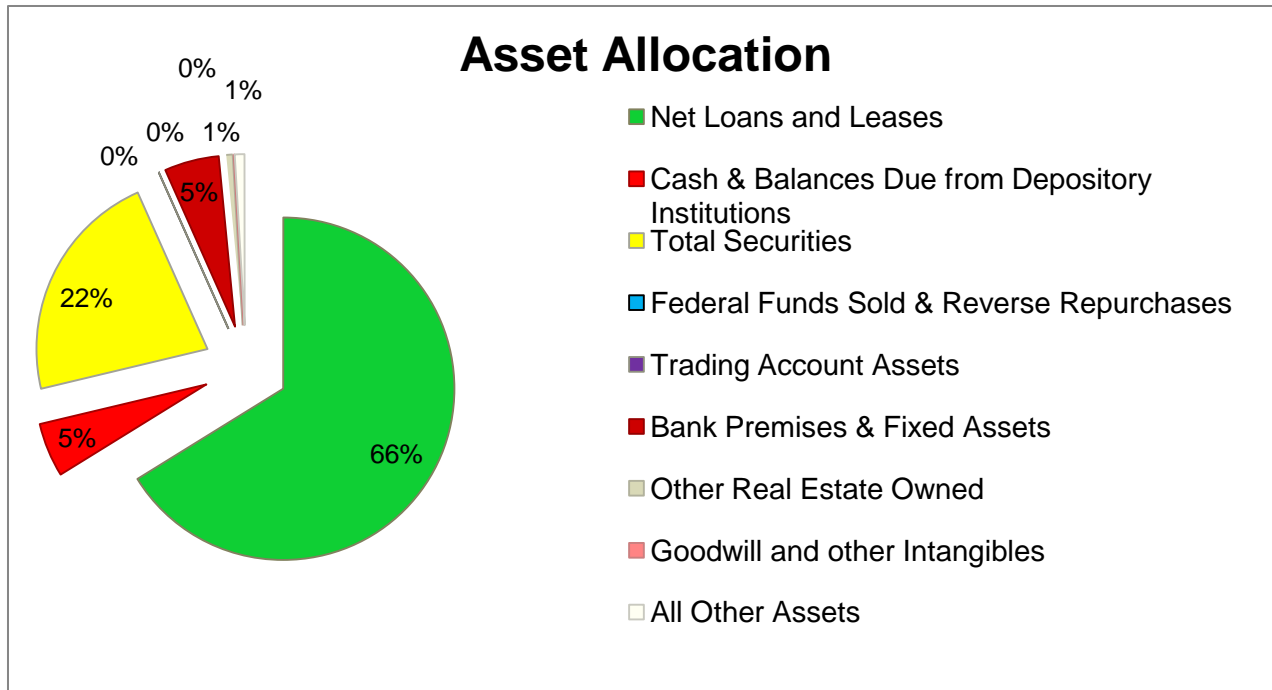


- Net income drops steeply in 08 Q3.
- The bank recorded big losses in the last three quarters prior to failure.



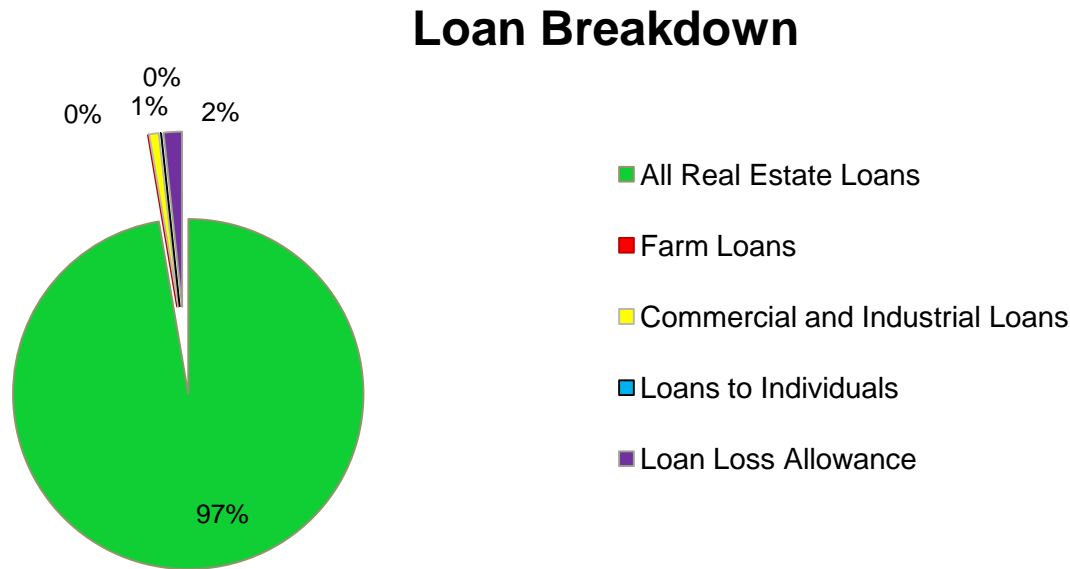
Indicates sign of bank in financial distress

Asset Allocation



- The average percentage of Net Loans for banks of the same Asset Concentration Hierarchy in the second quarter of 2009 was 67.77%.
- The average Net Loan percentage of all banks in the second quarter of 2009 was 55.79%.

Loan Breakdown



- The average percentage of Real Estate Loans for banks of the same Asset Concentration Hierarchy in the second quarter of 2009 was 68.36%.
- The average percentage for all banks in the second quarter of 2009 was 63.40%.

Events Timeline

- Oct 7, 08** - Emergency Economic Stabilization Act of 2008 Temporarily Increases Basic FDIC Insurance Coverage from \$100,000 to \$250,000 per Depositor.
- Oct 14, 08** - FDIC creates new program to guarantee bank debts and fully insure non-interest bearing deposit transaction accounts.
- Oct 14, 08** - The Treasury Department will invest up to \$250 billion in the nation's banks via the Capital Purchase Program.
- Nov 20, 08** - FDIC announces the availability of IndyMac Loan Modification Model.
- Nov 25, 08** - Created the Term Asset-Backed Securities Loan Facility to support the issuance of asset-backed securities collateralized by loans.
- Dec 3, 08** - SEC approved measures to strengthen oversight of credit rating agencies.
- Dec 16, 08** - Troubled banks have to provide certain position level and counterparty level data and QFC counterparty and portfolio identifiers to FDIC in a timely manner.
- Dec 23, 08** - Treasury provides TARP funds to focal Banks by purchasing \$2.8 billion investment from 49 banks.
- Dec 30, 08** - The Fed announced that it will purchase mortgage-backed securities.
- Jan 15, 09** - The Senate voted to allow access to the remaining bailout funds of \$350 billion.
- Jan 27, 09** - As part of the Capital Purchase Program, Treasury announced investments of \$386 million in 23 healthy banks.
- Feb 10, 09** - A Capital Assistance Program to help ensure banks hold sufficient capital, produce a more consistent and forward-looking assessment of risks on banks' balance and their potential capital needs.

Events Timeline

- Feb 10, 09** - Treasury and Fed expanded the Term Asset-Backed Securities Lending facility up to \$1 trillion.
- Feb 18, 09** - President Obama signs the American Recovery and Reinvestment Act of 2009, which limits bonuses of the highest earning executives.
- Mar 4, 09** - Treasury announced loan modification guidelines under the Administration's Homeowner Affordability and Stability Plan.
- Mar 23, 09** - Using TARP capital and capital from private investors, the Public-Private Investment Program will generate \$500 billion in purchasing power to buy legacy assets.
- May 1, 09** - The Fed announces that, starting in June, commercial mortgage backed securities and securities backed by insurance premium finance loans will be eligible collateral under the TALF. The Treasury purchases a total of \$45.5 million in preferred stock from 7 U.S. banks under the Capital Purchase Program.
- May 7, 09** - Looking for capital or a merger to help pay for undercapitalized first quarter losses. The bank started with a private offering and received some commitments, but fell short of the minimum amount needed to receive funds.
- May 8, 09** - The Treasury purchases of total of \$42 million in preferred stock from 7 U.S. banks under the Capital Purchase Program.
- May 13, 09** - The Treasury proposes amendments to the Commodity Exchange Act and securities laws to enhance govt. regulation of over the counter derivatives markets.

* All internal news are written in blue color.

Events Timeline

- May 14, 09** - SEC proposed amendments to strengthen safeguards of investor funds controlled by investment advisers.
- May 29, 09** - FDIC tightens the deposit interest rates paid by banks that are less than well capitalized. Generally, such banks will be permitted to offer to "national rate" plus 75 basis points.
- Jun 9, 09** - 10 of the largest U.S financial institutions are expected to make CPP repayments to Treasury.
- Jul 2, 09** - FDIC proposed guidelines require private equity firms to hold bank purchases for 3 years and maintain capital levels.
- Jul 8, 09** - The Legacy Securities program is designed to facilitate price discovery to re-deploy capital and extend new credit to households and businesses. Treasury will invest up to \$30 billion of equity and debt.
- Jul 15, 09** - SEC voted unanimously to propose rule amendments to improve the quality and timeliness of municipal securities disclosure.
- Jul 29, 09** - SEC announced several actions that would protect against abusive short sales and make more short sale information available to the public.
- Jul 31, 09** - Integrity Bank was closed by Florida Office of Financial Regulation. Stonegate Bank assumed all the deposits.

* All internal news are written in blue color.

Events Timeline

- Aug 26, 09** - Banking organizations affected by the new accounting standards generally will be subject to higher minimum regulatory capital requirements. New standards for investors interested in acquiring or investing in the deposit liabilities of failed banks or thrifts.
- Aug 27, 09** - Aggregate net loss of \$3.7 billion in the second quarter of 2009, a decline of \$8.5 billion from the \$4.8 billion in profits the industry reported in the second quarter of 2008.
- Sep 9, 09** - FDIC Board adopted a Notice of Proposed Rulemaking (NPR) that reaffirms the expiration of the debt guarantee component of the Temporary Liquidity Guarantee Program.
- Sep 17, 09** - SEC voted unanimously to take several rulemaking actions to bolster oversight of credit ratings agencies by enhancing disclosure and improving the quality of credit ratings.
- Sep 24, 09** - Credit quality declined sharply for loan commitments of \$20 million or more held by multiple federally supervised institutions.
- Sep 28, 09** - SEC (Section 31) fee rate applicable to securities transactions on the exchanges and in the over-the-counter markets will be set at \$12.70 per million dollars.
- Sep 29, 09** - Institutions to prepay their estimated quarterly risk-based assessments for the fourth quarter of 2009 and for all of 2010, 2011, and 2012.

Report Summary – *Surprise?*

Based on the methods with which we analyzed Integrity Bank, its failure was ***not a surprise.***

Here are the indications that The Integrity Bank should fail:

- 1) **The Integrity Bank's normalized income experienced a total loss (of its total assets) of almost 13% over the last 3 quarters.**
- 2) **The bank had a mounting volume of delinquent assets in the quarters before its failure.**
- 3) **The bank's asset to liability ratio dropped below 107% two quarters prior to failure. It had a 98.92% ratio the quarter before it failed.**
- 4) **Integrity Bank had a bankability composite score of -46.70 the quarter before it failed, indicating the bank's very poor overall financial health and likelihood to fail.**

References

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