

UNITED STATES OF AMERICA
BEFORE THE
BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D.C.

TEXAS DEPARTMENT OF BANKING
AUSTIN, TEXAS

In the Matter of

HERRING BANCORP, INC.
Amarillo, TX

Docket No. 22-024-B-HC

Department Docket No. 2022-015

Order to Cease and Desist Issued
Upon Consent Pursuant to the
Federal Deposit Insurance Act, as
Amended, and Subtitles A and G of
Title 3 of the Texas Finance Code

WHEREAS, Herring Bancorp, Inc., Amarillo, Texas (“HBI”), a registered bank holding company, owns and controls Herring Bank, Amarillo, Texas (the “Bank”), a state-chartered bank, and various nonbank subsidiaries;

WHEREAS, the Board of Governors of the Federal Reserve System (the “Board of Governors”) is the appropriate federal supervisor of HBI;

WHEREAS, the Texas Department of Banking (“Department”) is the appropriate state banking supervisor for the Bank;

WHEREAS, on October 6, 2021, the Federal Deposit Insurance Corporation (“FDIC”) and Department issued a Consent Order designed to improve, among other things, the Bank’s board and management oversight, its policy on affiliate transactions, internal controls, information technology, and its asset and liability management (the “Bank Order”);

WHEREAS, the Federal Reserve Bank of Dallas (the “Reserve Bank”) and Department previously identified deficiencies in HBI’s board oversight and financial reporting that HBI has yet to fully correct;

WHEREAS, the most recent inspection of HBI conducted by the Reserve Bank as of June 30, 2022 identified deficiencies in HBI’s board and management oversight, liquidity and funds management practices, and affiliate transaction policies;

WHEREAS, the Board of Governors, the Reserve Bank, Department, and HBI have the common goals that HBI maintains the financial soundness of HBI and its nonbank subsidiaries so that HBI may serve as a source of strength to the Bank and that HBI operates in compliance with all applicable federal and state laws, rules, and regulations;

WHEREAS, HBI, the Board of Governors, and Department have mutually agreed to enter into this Cease and Desist Order (the “Order”); and

WHEREAS, the board of directors of HBI, at a duly constituted meeting, adopted a resolution authorizing and directing the undersigned to enter into this Order on behalf of HBI, and consenting to compliance with each and every provision of this Order by HBI, and waiving all rights that HBI may have pursuant to section 8 of the Federal Deposit Insurance Act, as amended (the “FDI Act”) (12 U.S.C. § 1818) and subtitles A and G of title 3 of the Texas Finance Code, including but not limited to: (i) the issuance of a notice of charges on any and all matters set forth in this Order; (ii) a hearing for the purpose of taking evidence on any matters set forth in this Order; (iii) judicial review of this Order; and (iv) challenging or contesting, in any manner, the basis, issuance, validity, terms, effectiveness or enforceability of this Order or any provision hereof.

NOW, THEREFORE, it is hereby ordered that, before the filing of any notices, or taking of any testimony, or adjudication of or finding on any issues of fact or law herein, and solely for the purpose of settling this matter without a formal proceeding being filed and without the necessity for protracted or extended hearings or testimony, pursuant to sections 8(b)(1) and (3) of the FDI Act (12 U.S.C. §§ 1818(b)(1) and 1818(b)(3)) and section 35.002 of the Texas Finance Code, HBI and its institution-affiliated parties, as defined in section 3(u) of the FDI Act (12 U.S.C. §§ 1813(u) and 1818(b)(3)), shall cease and desist and take affirmative action as follows:

Source of Strength

1. The board of directors of HBI shall take appropriate steps to fully utilize HBI's financial and managerial resources, pursuant to section 225.4(a) of Regulation Y of the Board of Governors (12 C.F.R. § 225.4(a)), to serve as a source of strength to the Bank, including, but not limited to, taking steps to ensure that the Bank complies with the Bank Order, and any other supervisory action taken by the Reserve Bank and Department.

Board Oversight

2. Within 60 days of this Order, the board of directors of HBI shall submit a written plan acceptable to the Reserve Bank and Department to strengthen board oversight of the management and operations of HBI and its nonbank subsidiaries. The plan shall include the following three items:

(a) the actions that HBI's board of directors will take to improve HBI's condition and maintain effective control over, and supervision of, HBI's major operations and activities, including capital, earnings, liquidity, corporate expenses, internal controls, and audit;

(b) steps to monitor management's adherence to approved policies and procedures, and applicable laws and regulations, and to monitor exceptions to approved policies and procedures; and

(c) the establishment of appropriate risk tolerance guidelines and risk limits.

Risk Management

3. Within 60 days of this Order, HBI shall submit to the Reserve Bank and Department an acceptable written plan to enhance HBI's risk management practices. The plan shall, at a minimum, address, consider, and include:

(a) measures to strengthen board and senior management oversight of risks of HBI and its nonbank subsidiaries;

(b) written policies and procedures designed to identify, assess, manage, and monitor risk exposures, including, but not limited to, risks in new activities and products, investments, and liquidity;

(c) steps to improve the information and reports that will be regularly reviewed by the board of directors, committees, and senior executive officers of HBI in their oversight and operation of HBI and its nonbank subsidiaries, including information on internal controls, risk management, capital, liquidity, earnings, corporate expenses, and audit; and

(d) a strategic plan that addresses direction, objectives, and long-range goals, includes the holding company and its nonbank subsidiaries, and explains how the organization's products and services align with the plan and strategic goals while addressing related budgeting.

Corporate Governance and Management Review

4. Within 30 days of this Order, the board of directors of HBI shall retain an independent third party acceptable to the Reserve Bank and Department to assess the

effectiveness of HBI's corporate governance, board and management structure, and staffing needs (the "Independent Review"), and to prepare a written report of findings and recommendations (the "Independent Report").

(a) The Independent Review shall include an assessment of and recommendation for:

(i) the current structure, qualifications, and composition of HBI's board of directors, to determine whether each member has the knowledge, time, and independence to effectively and appropriately oversee HBI and ensure it operates in a safe and sound manner, and the current structure, qualifications, and composition of its committees, including its audit committee, to evaluate their effectiveness and independence as well as ensure risk management processes promote effective challenge to business and strategic decisions; and

(ii) reporting line structures, to ensure management has the authority and ability to effectively identify, monitor, and control risks of HBI.

(b) Within 10 days of the Reserve Bank and Department's approval of HBI's independent third-party selection, HBI shall submit an engagement letter acceptable to the Reserve Bank and Department for approval. The engagement letter shall require the independent third party to submit the Independent Report within 90 days of regulatory approval of the engagement letter and include commitments that the Independent Report and any drafts thereof will be provided to the Reserve Bank and Department at the same time that it is provided to HBI's board of directors, and that any information supporting the conclusions in the Independent Report will be made available to the Reserve Bank and Department upon its request.

(c) Within 30 days of receipt of the Independent Report, HBI's board of directors shall submit a written board oversight and management plan to the Reserve Bank and

Department that fully addresses the findings and recommendations in the Independent Report and describes the specific actions that the board of directors will take in order to strengthen HBI's board of directors' and management committee's corporate governance structure, and to hire, as necessary, additional or replacement directors, officers or staff to properly oversee, manage, and operate HBI.

Internal Controls

5. Within 60 days of this Order, HBI shall submit written policies and procedures acceptable to the Reserve Bank and Department to strengthen HBI's system of internal controls. The policies and procedures shall address, consider, and include, at a minimum, the following areas:

(a) internal controls to prevent HBI insiders from using corporate funds for personal use, including policies and procedures to ensure that corporate expenses are appropriately documented, reasonable, and approved prior to reimbursement;

(b) internal controls to ensure that all debits from HBI's checking account have the necessary documentation to determine the business purpose and reason for payment; and

(c) the strengthening of HBI's audit function by:

(i) expanding the function's audit universe and audit risk assessment to incorporate HBI and its nonbank subsidiaries;

(ii) ensuring audit engagement letters for the annual consolidated audit and all enterprise-wide audits are approved by HBI's board and audit committee; and

(iii) completing an annual audit of intercompany transactions, including a review of HBI expenses to insiders, the Bank, and affiliates, to determine if they are properly

documented, in conformance with HBI policies and procedures, and in conformance with laws and regulations.

Asset Management

6. (a) Within 30 days after June 30, 2023, HBI shall submit to the Reserve Bank and Department a complete accounting of its assets which shall, at a minimum, include:

- (i) the current market value of each non-Bank stock asset;
- (ii) the current book value of Bank stock;
- (iii) the name of the account in which the asset is held; and
- (iv) the location of the asset.

(b) Within 45 days after the end of each calendar quarter following this Order, HBI shall submit to the Reserve Bank and Department the value of HBI's assets.

(c) HBI shall not enter into an agreement to sell any asset or lease HBI property without the prior written approval of the Reserve Bank and Department. Any request for prior approval pursuant to this paragraph shall be accompanied by documentation adequate to provide the Reserve Bank and Department with the details of the asset to be sold.

(d) The Chairman of the Audit Committee of HBI shall review all expenses paid to or on behalf of the chairman and senior executive officers of HBI, as defined in Subpart H of Regulation Y, at 12 C.F.R. § 225.71, prior to payment of any reimbursements to ensure they are properly documented and in conformance with policies and procedures. The Chairman of the Audit Committee shall provide the results of such review and actions to the board of HBI, the Reserve Bank, and Department. In addition, the board of HBI shall ensure the responsible party refunds any inappropriate expenses that were identified in the forensic audit of insider expenses conducted by HBI's third-party audit firm in 2021 and 2022 related to the payment of expenses

to the Chairman and Vice Chairman. In addition, policies and procedures must be developed and maintained to ensure that all expenses submitted for reimbursement in the future, over a stated reasonable amount, are appropriate and that full HBI board approval is obtained prior to reimbursement.

Dividends and Distributions

7. (a) HBI shall not declare or pay any dividends without the prior written approval of the Reserve Bank, the Director of the Division of Supervision and Regulation of the Board of Governors (the “Director”), and Department.

(b) HBI shall not, directly or indirectly, take dividends or any other form of payment representing a reduction in capital from the Bank without the prior written approval of the Reserve Bank and Department.

(c) HBI and its nonbank subsidiaries shall not make any distributions of interest, principal, or other sums on subordinated debentures, shareholder loans, or trust preferred securities without the prior written approval of the Reserve Bank, the Director, and Department.

(d) All requests for prior approval shall be received by the Reserve Bank and Department at least 30 days prior to the proposed dividend declaration date, proposed distribution on subordinated debentures, and required notice of deferral on trust preferred securities. All requests shall contain, at a minimum, current and projected information on HBI’s capital, earnings, and cash flow; the Bank’s capital, asset quality, earnings, and allowance for loan and lease losses; and identification of the sources of the funds for the proposed payment or distribution.

Debt and Stock Redemption

8. (a) HBI and its nonbank subsidiaries shall not, directly or indirectly, incur, increase, or guarantee any debt, including the issuance of new trust preferred securities, without prior written approval of the Reserve Bank and Department. All requests for prior written approval shall contain, but not be limited to, a statement regarding the purpose of the debt, the terms of the debt, and the planned source(s) for debt repayment, and an analysis of the cash flow resources available to meet such debt repayment.

(b) HBI shall not, directly or indirectly, purchase or redeem any shares of its stock, without the prior written approval of the Reserve Bank and Department.

Liquidity and Funds Management

9. Within 60 days of this Order, HBI shall submit a written consolidated liquidity policy and funding plan acceptable to the Reserve Bank and Department that includes the following five items:

- (a) liquidity and dependency reporting against board-approved limits;
- (b) sources and uses analyses;
- (c) a forward-looking assessment of HBI's and its nonbank subsidiaries' liquidity position;
- (d) measures to ensure that HBI has the ability to finance its activities, and that HBI's debt can be serviced and repaid, without adversely affecting the condition of the Bank; and
- (e) measures to ensure timely reporting of HBI's liquidity position to the board of directors.

Compliance with Laws and Regulations

10. (a) In appointing any new director or senior executive officer, or changing the responsibilities of any senior executive officer so that the officer would assume a different senior executive officer position, HBI shall:

(i) comply with the notice provisions of section 32 of the FDI Act (12 U.S.C. § 1831i) and Subpart H of Regulation Y of the Board of Governors (12 C.F.R. §§ 225.71 *et seq.*); and

(ii) provide Department with at least 30 days prior written notice of the proposed change and will not make the noticed change if Department objects within 30 days of receipt of the completed notice.

(b) HBI shall comply with the restrictions on indemnification and severance payments of section 18(k) of the FDI Act (12 U.S.C. § 1828(k)) and Part 359 of the FDIC's Regulations (12 C.F.R. Part 359).

Affiliate Transactions

11. (a) HBI shall take all necessary actions to ensure that the Bank complies with sections 23A and 23B of the Federal Reserve Act (12 U.S.C. §§ 371c and 371c-1) and Regulation W of the Board of Governors (12 C.F.R. Part 223) in all transactions between the Bank and its affiliates, including but not limited to, HBI and its nonbank subsidiaries.

(b) HBI and its nonbank subsidiaries shall not cause the Bank to violate any provision of sections 23A and 23B of the Federal Reserve Act or Regulation W of the Board of Governors.

(c) Within 30 days of this Order, HBI shall submit to the Reserve Bank and Department an acceptable written policy regarding transactions between HBI, including its

nonbank subsidiaries, and the Bank, addressing all affiliate and related intercompany service or management agreements, that includes, but is not limited to:

(i) measures to ensure that intercompany transactions that either directly or indirectly compensate HBI or its non-bank subsidiaries are conducted on an arms-length basis; and

(ii) procedures to ensure that fees paid directly or indirectly to HBI are supported by a fair market value analysis of fees for comparable transactions.

(d) Within 60 days of this Order, HBI shall submit written policies and procedures acceptable to the Reserve Bank and Department that shall address, consider, and include, the improvement of intercompany service agreements by:

(i) updating intercompany service agreements as previously identified by the Reserve Bank and Department and ensuring market rates are confirmed;

(ii) developing new intercompany service agreements as previously identified by the Reserve Bank and ensuring market rates are confirmed; and

(iii) ensuring the updated and new intercompany service agreements are approved by the Bank, the Reserve Bank, and Department.

Approval, Implementation, and Progress Reports

12. (a) HBI shall submit the written plans, policies and procedures, and programs that are acceptable to the Reserve Bank and Department within the applicable time periods set forth in paragraphs 2, 3, 4(c), 5, 9, 11(c), and 11(d) of this Order. Each plan, policy and procedure, and program shall contain a timeline for full implementation with specific deadlines for the completion of each component. An independent party acceptable to the Reserve Bank and Department shall be retained by HBI within the time period set forth in paragraph 4 of this

Order. An engagement letter acceptable to the Reserve Bank and Department shall be submitted within the time period set forth in paragraph 4(b) of this Order.

(b) Within 10 days of approval by the Reserve Bank and Department, HBI shall adopt the approved plans and programs. Upon adoption, HBI shall promptly implement the approved plans and programs, and thereafter fully comply with them.

(c) During the term of this Order, the approved plans and programs shall not be amended or rescinded without the prior written approval of the Reserve Bank and Department.

13. Within 45 days after the end of each calendar quarter following the date of this Order, HBI shall submit to the Reserve Bank and Department written progress reports detailing the form and manner of all actions taken to secure compliance with this Order, a timetable and schedule to implement specific remedial actions to be taken, the results thereof, and a parent company only balance sheet, income statement, and, as applicable, reports of changes in stockholders' equity. The Reserve Bank and Department may, in writing, discontinue the requirement for progress reports or modify the reporting schedule.

Communications

14. All communications regarding this Order shall be sent to:
- (a) Richard M. Ashton
Deputy General Counsel
 - Jason A. Gonzalez
Assistant General Counsel
 - Board of Directors of the Federal Reserve System
20th and C Streets, NW
Washington, D.C. 20551

- (b) Amy McGregor
Vice President
Federal Reserve Bank of Dallas
2200 North Pearl Street
Dallas, Texas 75201
- (c) Charles G. Cooper
Banking Commissioner
Texas Department of Banking
2601 Lamar Blvd., Austin, Texas 78705
- (d) Coney Burgess
Chairman
Herring Bancorp, Inc.
2201 Civic Circle, Suite 1001
Amarillo, Texas 79109

Miscellaneous

15. Notwithstanding any provision of this Order to the contrary, the Reserve Bank and Department may, in its sole discretion, grant written extensions of time to HBI to comply with any provision of this Order.

16. The provisions of this Order shall be binding on HBI, and each of its institution-affiliated parties, as defined in section 3(u) and 8(b)(3) of the FDI Act (12 U.S.C. §§ 1813(u) and 1818(b)(3)), in their capacities as such, and their successors and assigns.

17. Each provision of this Order shall remain effective and enforceable until stayed, modified, terminated, or suspended in writing by the Reserve Bank and Department.

18. The provisions of this Order shall not bar, estop, or otherwise prevent the Board of Governors, the Reserve Bank, Department, or any other federal or state agency from taking any other action affecting HBI, any of its subsidiaries, or any of its current or former institution-affiliated parties and their successors and assigns.

By order of the Board of Governors of the Federal Reserve System effective this 29th
day of June, 2023.

HERRING BANCORP, INC.

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM

By: /s/ Coney Burgess
Coney Burgess
Chairman

By: /s/ Ann E. Misback
Ann E. Misback
Secretary of the Board

TEXAS DEPARTMENT OF BANKING

By: /s/ Charles G. Cooper
Charles G. Cooper
Banking Commissioner