

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 87038 / September 20, 2019

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 4083 / September 20, 2019

ADMINISTRATIVE PROCEEDING
File No. 3-19479

In the Matter of

DONALD F. MCGRAW, JR.,

Respondent.

**ORDER INSTITUTING CEASE-AND-
DESIST PROCEEDINGS PURSUANT TO
SECTION 21C OF THE SECURITIES
EXCHANGE ACT OF 1934, MAKING
FINDINGS, AND IMPOSING A CEASE-
AND-DESIST ORDER**

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 (“Exchange Act”) against Donald F. McGraw, Jr. (“McGraw” or “Respondent”).

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (“Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over him and the subject matter of these proceedings, which are admitted, and except as provided herein in Section V, Respondent consents to the entry of this Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order (“Order”), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds¹ that

SUMMARY

1. This matter concerns failures between April 2012 and September 2014 of The Bancorp, Inc. ("Bancorp") to properly classify certain loans and to take appropriate charges for individually impaired loans, resulting in Bancorp materially understating its Allowance for Loan and Lease Losses ("ALLL") and its Provision for Loan and Lease Losses ("PLLL") in its requisite periodic reports filed with the Commission. Bancorp repeatedly overlooked indicators of borrowers' and guarantors' financial distress as it failed to assign appropriate risk ratings to certain loans and to identify certain large lending relationships as containing impaired or otherwise substandard loans.

2. As a result of these failures, on September 28, 2015, Bancorp restated its financial results and financial statements for certain prior fiscal years. Pursuant to the restatement, the aggregate adjustment to the PLLL for the fiscal years 2010 through 2013 was approximately \$138.6 million. Pursuant to the adjustments to the historical ALLL set forth in the restatement, Bancorp's ALLL for 2012 increased by 78.23% from the balance previously reported, and the ALLL for 2013 increased by 73.97%. In its annual Report on Form 10-K for its fiscal year 2014, which contained the restated financial statements, Bancorp disclosed a material weakness in its internal control over financial reporting for its fiscal years 2012, 2013, and 2014 related to its "failure to maintain controls over credit file maintenance, including the risk-rating of borrowers and the evaluation of collateral."

3. In his position as Bancorp's Chief Credit Officer during those fiscal years, McGraw was ultimately responsible for Bancorp's credit file maintenance, including ensuring that credit files contained necessary, appropriate, and current information. However, as a result of his conduct described herein, McGraw failed to provide reasonable assurances that Bancorp's credit files contained necessary and current documentation.

4. In addition, beginning in October 2011, McGraw was one of four members of the Bancorp committee tasked with evaluating loan modifications to determine if they were Troubled Debt Restructurings ("TDRs"). Moreover, it was McGraw's responsibility to identify loans for review by the committee and to draft the materials presented to the committee. However, as a result of his conduct described herein, McGraw failed to provide the committee with information sufficient for it to make appropriate determinations. Consequently, McGraw knew or should have known that the determinations made by the committee at times were likely to be inaccurate.

¹ The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

5. As a result of the conduct described above, McGraw caused Bancorp's violations of Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act and violated Rule 13b2-1 thereunder.

FACTS

A. Respondent

6. Donald F. McGraw, Jr. has been Bancorp's Chief Credit Officer since 2000. Previously, McGraw was a Federal Deposit Insurance Corporation bank examiner. McGraw, age 62, is a resident of Media, Pennsylvania.

B. Other Relevant Entity

7. Bancorp is a Delaware corporation with its principal executive offices in Wilmington, Delaware. Its common stock is registered with the Commission pursuant to Section 12(b) of the Exchange Act and trades on the NASDAQ Stock Market under the ticker symbol TBBK. Bancorp is the bank holding company for The Bancorp Bank ("Bancorp Bank"), a regional bank headquartered in Wilmington, Delaware. Bancorp Bank is Bancorp's primary wholly-owned subsidiary.

C. Accounting Guidance

8. Banking institutions carry loans on their balance sheets as assets and record on their income statements any interest revenue on the loans. According to Generally Accepted Accounting Principles ("GAAP"), an individual loan is impaired when "based on current information and events, it is probable that a creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement." Accounting Standards Codification ("ASC") 310-10-35. Furthermore, loan losses must be recognized for impairment of large groups of smaller balance loans and loans with similar risk characteristics when it is probable that the asset is impaired as of the date of the financial statements and the amount of loss can be reasonably estimated. *Id.*

9. GAAP also requires that when a loan is modified—whether by restructure, extension, renewal, or other modification—the transaction must be evaluated to determine if the loan modification constitutes a Troubled Debt Restructuring ("TDR"). Pursuant to ASC 310-40-15, a loan is a TDR if there is a restructuring for a borrower in financial difficulty and the creditor grants a concession to the borrower that it would not otherwise consider. A loan restructured as a TDR is an impaired loan. ASC 310-40-35.

10. The ALLL is the current estimate of the aggregate probable loss inherent in a loan portfolio and is reflected on the balance sheet as a reduction to the loan balance. The ALLL encompasses the effects of two types of loan losses: (1) loans identified and evaluated for impairment individually; and (2) loans grouped by common risk characteristics and analyzed for impairment on an aggregate basis. ASC 310-10-35. The PLLL reflects the income statement impact of impaired loans for the period being reported.

D. Bancorp's Restatement

11. On September 28, 2015, Bancorp filed its annual Report on Form 10-K for its fiscal year 2014, which included restated financial data for its fiscal years 2010 through 2013 and restated financial statements for its fiscal years 2012 and 2013, as well as for the first three quarters of 2013 and 2014. The restatement included an aggregate adjustment to the PLLL of approximately \$138.6 million in Bancorp's commercial loan portfolio from 2010 to 2013. That total adjustment included an adjustment adding \$90.5 million to the loan loss provision for 2012 and an adjustment adding \$28.9 million to the provision for 2013. The adjustment for 2012 exceeded the \$24.4 million in income before taxes previously reported by Bancorp, resulting in an overall loss for that fiscal year.

12. In the annual Report on Form 10-K for its fiscal year 2014, Bancorp also disclosed a material weakness in its internal control over financial reporting for its fiscal years 2012, 2013, and 2014 related to its "failure to maintain controls over credit file maintenance, including the risk-rating of borrowers and the evaluation of collateral and industry-specific information that [Bancorp] believed to be relevant in determining the occurrence of a loss event and measuring impairment under ASC 310."

E. Bancorp's Business Model

13. During the relevant time period, Bancorp engaged in a business model called "relationship banking." Bancorp sought to develop long-standing banking relationships with certain individuals and businesses within Bancorp Bank's geographic region and provide them with the attention of senior Bancorp Bank management. Bancorp's focus on long-standing relationships with borrowers and guarantors holding multiple Bancorp Bank loans was intended to encourage cross-selling, provide insight into borrowers' risk, and increase customer loyalty. Bancorp executives also believed that this model allowed Bancorp Bank to cross-collateralize loans and take a holistic approach to loan management.

14. However, Bancorp made risk rating and impairment decisions that relied too heavily on borrowers' and guarantors' reputations, their historic business and banking relationship with Bancorp Bank, and their expected future prospects for more business, while overlooking indicators of financial distress. This was particularly the case with respect to certain large or high-profile lending relationships and with respect to borrowers and guarantors with long relationships with Bancorp Bank. As a result, Bancorp failed to identify loan impairments and credit deterioration within individual loans and repeatedly failed to re-evaluate loans and downgrade risk ratings when confronted with negative information. This caused Bancorp to materially understate its PLLL from 2010 through 2013 and its ALLL from 2010 through the third quarter of 2014.

F. McGraw's Role

15. For its fiscal years 2012, 2013, and 2014, Bancorp had devised internal accounting controls for credit file maintenance, but failed to maintain the controls. The controls were intended

to provide reasonable assurance that Bancorp's credit files contained relevant information, including timely appraisals and relevant financial information regarding borrowers. In his role as Chief Credit Officer, McGraw was responsible for this process. He had responsibility for ensuring that credit files contained necessary, appropriate, and current information. In fact, between at least April 2012 and September 2014, Bancorp's credit files were incomplete. The lack of complete credit files contributed to Bancorp's failure during this period to fairly and accurately assign risk ratings and estimate loan impairment.

16. Current appraisals were important for properly evaluating the real estate collateral underlying many Bancorp Bank loans and therefore for fairly and accurately assigning risk ratings and estimating impairment. Bancorp policies required new appraisals under certain circumstances. In his role as Chief Credit Officer, McGraw did not consistently enforce the appraisal policy. As a result, Bancorp frequently relied upon outdated appraisals in connection with assignment of risk ratings and impairment decisions. In multiple instances, Bancorp relied upon pre-financial crisis real estate appraisals well after the crisis had ended.

17. McGraw failed on at least two occasions to provide reasonable assurances that Bancorp's credit files included contemporaneous information concerning criminal cases involving borrowers or guarantors. In one of those instances, although McGraw was aware by January 2013 that the guarantor in a large lending relationship had pleaded guilty to bank fraud, there was no mention of the criminal case in the loan paperwork for a March 2013 maturity extension or in the loan paperwork for a line of credit increase in September 2013. In connection with the restatement of its financial statements, Bancorp recognized some impairment losses for all loans in this relationship during the fourth quarter of 2012.

18. Bancorp also failed to record instances of delinquency within credit files. Even when additional credit was granted in order to allow delinquent borrowers to bring their loan payments current, McGraw did not require the lending staff to document the delinquencies in the credit requests for these increases.

19. Additionally, under McGraw's oversight, Bancorp at times did not provide reasonable assurances that current financial statements that met the requirements of loan agreements were obtained and included in its credit files. On one occasion, when it extended the maturity of an entity's \$1.5 million line of credit, Bancorp failed to obtain timely financial information required under the terms of the line of credit. Instead, it relied upon outdated tax returns and financial statements and projections that had not been reviewed and audited as required.

20. As a result of the conduct described above, Bancorp failed to maintain internal accounting controls over credit file maintenance sufficient to provide reasonable assurances that transactions were recorded as necessary to permit preparation of financial statements in accordance with GAAP. By his acts and omissions described above, including his failure to ensure that the credit files contained timely appraisals and negative information concerning borrowers and guarantors, and his failure to include references to delinquencies in credit requests, McGraw

contributed to Bancorp's failure, and McGraw knew or should have known that his acts or omissions would so contribute.

21. In addition, from its inception, McGraw was a member of the Bancorp committee that evaluated loan modifications to determine if they were TDRs. From October 2011 through October 2013, he was the committee member tasked with compiling materials and creating summaries for the committee. His summaries often failed to include important information about the loans being considered, including information concerning the financial difficulties of borrowers or guarantors of modified loans. As a result, the committee was not provided with information sufficient to accurately identify TDRs.

22. For example, McGraw prepared the materials for the committee's evaluation of March 2012 modifications that extended the maturity and interest-only periods of certain loans in a \$44 million loan relationship with a long-time Bancorp Bank customer. The materials described the modifications as short-term, interest-only requests from a borrower that was not experiencing financial difficulties and failed to mention the delinquency of the loans or the customer's recent federal felony conviction. The committee determined that the modifications were not TDRs. In the restatement of its financial statements, Bancorp determined that it should have taken impairment charges related to those loans as of the March 2012 modifications.

23. During this time, as described above, Bancorp failed to make and keep books, records, and accounts, which in reasonable detail, accurately and fairly reflected its transactions and the disposition of its assets. By his acts and omissions described above, including his failure to maintain accurate and current credit files and his providing summaries to the TDR identification committee that omitted important information regarding loans, borrowers, and guarantors, McGraw contributed to Bancorp's failure, and McGraw knew or should have known that his acts or omissions would so contribute.

24. By his conduct described above, McGraw, directly or indirectly, falsified or caused to be falsified, books, records, and accounts that Bancorp was required to make and keep, in reasonable detail, to accurately and fairly reflect its transactions and the disposition of its assets.

G. Violations

25. As a result of the conduct described above, Respondent caused Bancorp's violation of Section 13(b)(2)(B) of the Exchange Act, which requires an issuer of securities registered pursuant to Section 12 of the Exchange Act to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that: transactions are executed in accordance with management's general and specific authorization; transactions are recorded as necessary to permit preparation of financial statements in conformity with GAAP or any other criteria applicable to such statements, and to maintain accountability for assets; access to assets is permitted only in accordance with management's general or specific authorization; and the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences.

26. As a result of the conduct described above, Respondent caused Bancorp's violation of Section 13(b)(2)(A) of the Exchange Act, which requires an issuer of securities registered pursuant to Section 12 of the Exchange Act to make and keep books, records, and accounts which, in reasonable detail, accurately and fairly reflect the issuer's transactions and dispositions of assets.

27. As a result of the conduct described above, Respondent violated Rule 13b2-1 under the Exchange Act by directly or indirectly falsifying or causing to be falsified books, records, and accounts required to be maintained by Bancorp.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent Donald F. McGraw, Jr.'s Offer.

Accordingly, it is hereby ORDERED that:

A. Pursuant to Section 21C of the Exchange Act, Respondent cease and desist from committing or causing any violations and any future violations of Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act and Rule 13b2-1 thereunder.

B. Respondent shall pay a civil money penalty in the amount of \$50,000 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury, subject to Exchange Act Section 21F(g)(3). Payment shall be made in the following installments: \$20,000 to be paid within 10 days of the entry of this order, \$10,000 to be paid within 120 days of the entry of this order, \$10,000 to be paid within 240 days of the entry of this order, and \$10,000 to be paid within 350 days of the entry of this order. Payments shall be applied first to post-order interest, which accrues pursuant to 31 U.S.C. § 3717. Prior to making the final payment set forth herein, Respondent shall contact the staff of the Commission for the amount due. If Respondent fails to make any payment by the date agreed and/or in the amount agreed according to the schedule set forth above, all outstanding payments under this Order, including post-order interest, minus any payments made, shall become due and payable immediately at the discretion of the staff of the Commission without further application to the Commission.

Payment must be made in one of the following ways:

- (1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;
- (2) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at <http://www.sec.gov/about/offices/ofm.htm>; or
- (3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying Donald F. McGraw, Jr. as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Carolyn M. Welshhans, Associate Director, Division of Enforcement, Securities and Exchange Commission, 100 F St., NE, Washington, DC 20549.

C. Amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondent agrees that in any Related Investor Action, he shall not argue that he is entitled to, nor shall he benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondent agrees that he shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the Securities and Exchange Commission. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against Respondent by or on behalf of one or more investors based on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

V.

It is further Ordered that, solely for purposes of exceptions to discharge set forth in Section 523 of the Bankruptcy Code, 11 U.S.C. § 523, the findings in this Order are true and admitted by Respondent, and further, any debt for disgorgement, prejudgment interest, civil penalty or other amounts due by Respondent under this Order or any other judgment, order, consent order, decree or settlement agreement entered in connection with this proceeding, is a debt for the violation by Respondent of the federal securities laws or any regulation or order issued under such laws, as set forth in Section 523(a)(19) of the Bankruptcy Code, 11 U.S.C. § 523(a)(19).

By the Commission.

Vanessa A. Countryman
Secretary