

#2000-65

AGREEMENT BY AND BETWEEN
THE FIRST NATIONAL BANK OF FREEMAN
FREEMAN, SOUTH DAKOTA
AND
THE OFFICE OF THE COMPTROLLER OF THE CURRENCY

The First National Bank of Freeman, Freeman, South Dakota, (Bank) and the Comptroller of the Currency of the United States of America (Comptroller) wish to protect the interests of the depositors, other customers, and shareholders of the Bank, and, toward that end, wish the Bank to operate safely and soundly and in accordance with all applicable laws, rules and regulations.

The Comptroller, through his National Bank Examiners, has examined the Bank, and his findings are contained in the Report of Examination, dated March 27, 2000 (ROE).

In consideration of the above premises, it is agreed, between the Bank, by and through its duly elected and acting Board of Directors (Board), and the Comptroller, through his authorized representative, that the Bank shall operate at all times in compliance with the articles of this Agreement.

This Agreement shall be construed to be a "written agreement entered into with the agency" within the meaning of 12 U.S.C. § 1818(b)(1).

This Agreement shall be construed to be a "written agreement between such depository institution and such agency" within the meaning of 12 U.S.C. § 1818(e)(1) and 12 U.S.C. § 1818(i)(2).

This Agreement shall be construed to be a "formal written agreement" within the meaning of 12 C.F.R. § 5.51(c)(6)(ii). *See* 12 U.S.C. § 1831i.

This Agreement shall be construed to be a "written agreement" within the meaning of 12 U.S.C. § 1818(u).

All reports or plans which the Bank or Board has agreed to submit to the Assistant Deputy Comptroller pursuant to this Agreement shall be forwarded to:

Assistant Deputy Comptroller Christine A. Hartman
Sioux Falls Field Office
4900 South Minnesota Avenue
Suite 300
Sioux Falls, South Dakota 57108-2865

ARTICLE I

MANAGEMENT AND BOARD SUPERVISION STUDY

(1) Within sixty (60) days the Board shall employ an independent outside management consultant. Prior to employment of the consultant, the name and the qualifications of the consultant considered for employment shall be submitted to the Assistant Deputy Comptroller, who shall have the power of veto over the employment of the proposed consultant. However, failure to exercise such veto power shall not constitute approval or endorsement of the consultant.

(2) Within ninety (90) days, the Consultant shall complete a study of current staffing, management and Board supervision presently being provided to the Bank's lending function, and also of the Bank's management structure, and its staffing requirements in light of the Bank's present condition. The findings and recommendations of the Consultant shall be set forth in a written report to the Board. At a minimum, the report shall contain:

- (a) the identification of present and future management and staffing requirements of each area of the Bank, with particular emphasis given to the lending area;
- (b) an evaluation of the president, each vice president, each assistant vice president and cashier's qualifications and abilities and a determination of whether each of these individuals possesses the experience and other qualifications required to perform present and anticipated duties of his/her officer position;
- (c) recommendations as to whether management or staffing changes should be made, including the need for additions to or deletions from the current management team;
- (d) objectives by which management's effectiveness will be measured;
- (e) an evaluation of current lines of authority, reporting responsibilities and delegation of duties for all officers, including identification of any overlapping duties or responsibilities;
- (f) an assessment of whether Board members are receiving adequate information on the operation of the Bank to enable them to fulfill their fiduciary responsibilities and other responsibilities under law;
- (g) recommendations to expand the scope, frequency and sufficiency of information provided to the Board by management;
- (h) recommendations to correct or eliminate any other deficiencies in the supervision or organizational structure of the Bank.

(3) Within sixty (60) days of receipt of the written report, the Board shall develop, implement, and thereafter ensure Bank adherence to a written plan, with specific time frames, that will correct any deficiencies which are noted in the study.

(4) Copies of the Board's written plan and the Consultant's study shall be forwarded to the Assistant Deputy Comptroller. The Assistant Deputy Comptroller shall retain the right to determine the adequacy of the report and its compliance with the terms of this Agreement. In the event the written plan, or any portion thereof, is not implemented, the Board shall immediately advise the Assistant Deputy Comptroller, in writing, of specific reasons for deviating from the plan.

ARTICLE II

VIOLATIONS OF LAW

(1) The Board shall immediately take all necessary steps to ensure that Bank management corrects each violation of law, rule or regulation cited in the ROE and in any subsequent Report of Examination. The Bank shall report the status of such corrective action to the Assistant Deputy Comptroller on a quarterly basis and shall include the date and manner in which each correction has been effected during that reporting period.

(2) Within sixty (60) days, the Board shall adopt, implement, and thereafter ensure Bank adherence to specific procedures to prevent future violations as cited in the ROE and shall adopt, implement, and ensure Bank adherence to general procedures addressing compliance management which incorporate internal control systems and education of employees regarding laws, rules and regulations applicable to their areas of responsibility.

(3) Within thirty (30) days of receipt of any subsequent Report of Examination which cites violations of law, rule, or regulation, the Board shall adopt, implement, and thereafter ensure Bank adherence to specific procedures to prevent future violations as cited in the ROE and shall adopt, implement, and ensure Bank adherence to general procedures addressing compliance management which incorporate internal control systems and education of employees regarding laws, rules and regulations applicable to their areas of responsibility.

ARTICLE III

AUDIT PROGRAM

(1) Within sixty (60) days, the Bank shall retain the services of a qualified and independent Certified Public Accountant to audit and render an opinion on the Bank's June 30, 1999 Statement of Condition (Balance Sheet) and its Income Statement, and annually thereafter during the term of this Agreement.

(2) As part of this audit program, the Board shall evaluate the audit reports of any party providing services to the Bank, and shall assess the impact on the Bank of any audit deficiencies cited in such reports.

ARTICLE IV

LOAN PORTFOLIO MANAGEMENT

(1) The Board shall within sixty (60) days, employ or designate a sufficiently experienced and qualified person(s) or firm to perform an independent identification of problem loans and leases. Within ninety (90) days, the findings and recommendations of the independent identification process shall be set forth in a written report.

(2) The Board shall, within sixty (60) days, develop, implement, and thereafter ensure Bank adherence to a written program to improve and a system to monitor the Bank's loan portfolio management. The program shall include, but not be limited to:

- (a) early problem loan identification to assure the timely identification and rating of loans based on lending officer submissions;
- (b) the monitoring of previously charged-off assets and their recovery potential;
- (c) procedures to ensure compliance with the Bank's lending policies and laws, rules, and regulations pertaining to the Bank's lending function;
- (d) procedures to ensure satisfactory and perfected collateral documentation;
- (e) procedures to ensure that extensions of credit are granted, by renewal or otherwise, to any borrower only after obtaining and analyzing current and satisfactory credit information;

- (f) procedures to ensure conformance with loan approval requirements;
- (g) a system to track and analyze exceptions to the written program;
- (h) procedures to track and analyze concentrations of credit, significant economic factors, and general conditions and their impact on the credit quality of the Bank's loan and lease portfolios.

(3) Upon completion, a copy of the program shall be forwarded to the Assistant Deputy Comptroller.

(4) Beginning on July 31, 2000, and on a monthly basis thereafter, management will provide the Board with written reports on the Bank's loan portfolio, including, at a minimum, the following information:

- (a) the identification, type, rating, and amount of problem loans;
- (b) the identification, severity and amount of delinquent loans;
- (c) credit and collateral documentation exceptions;
- (d) the identification and status of credit related violations of law, rule or regulation;
- (e) the identity of the loan officer who originated and/or currently administers each loan reported in accordance with subparagraphs (a) through (d) of this Article and Paragraph;
- (f) the identification of loans not in conformance with the Bank's lending policies, and exceptions to the Bank's lending policies.

(5) Within sixty (60) days, the Board shall adopt, implement, and thereafter ensure Bank adherence to written work out plans for each loan or line of credit exceeding Seventy Five Thousand dollars (\$75,000), which are designed to eliminate the basis of criticism of assets criticized in the ROE, in any subsequent Report of Examination, or by any internal or external loan review, or in any list provided to management by the National Bank Examiners during any examination as "doubtful," "substandard," or "special mention." These work out plans shall include at a minimum:

- (a) an identification of the expected sources of repayment;
- (b) the estimated value of supporting collateral and the position of the Bank's lien on such collateral where applicable;
- (c) an analysis of current and satisfactory credit information, including cash flow analysis where loans are to be repaid from operations;
and,
- (d) the proposed action to eliminate the basis of criticism and the time frame for its accomplishment.

(6) Upon adoption, copies of the work out plans for all criticized assets, equal to or exceeding Seventy Five Thousand dollars (\$75,000), shall be forwarded to the Assistant Deputy Comptroller.

ARTICLE V

CREDIT AND COLLATERAL EXCEPTIONS

(1) Within sixty (60) days, the Board shall obtain current and satisfactory credit information on all loans lacking such information, including those listed in the ROE, in any subsequent Report of Examination, in any internal or external loan review, or in any listings of loans lacking such information provided to management by the National Bank Examiners at the conclusion of an examination.

(2) Within sixty (60) days, the Board shall ensure proper collateral documentation is maintained on all loans and correct each collateral exception listed in the ROE, in any subsequent Report of Examination, in any internal or external loan review, or in any listings of loans lacking such information provided to management by the National Bank Examiners at the conclusion of an examination.

(3) Effective immediately, the Bank may grant, extend, renew, alter, advance under a line of credit or restructure any loan or other extension of credit exceeding Twenty Five Thousand dollars (\$25,000) only after:

- (a) documenting the specific reason or purpose for the extension of credit;
- (b) identifying the expected source of repayment in writing;
- (c) structuring the repayment terms to coincide with the expected source of repayment;

- (d) obtaining and analyzing current and satisfactory credit information, including cash flow analysis where loans are to be repaid from operations.
 - (i) Failure to obtain the information in (d) shall require a majority of the full Board (or a delegated committee thereof) to fully document, in writing, the specific reasons why obtaining and analyzing the information in (d) would be detrimental to the best interests of the Bank.
 - (ii) A copy of the Board certification shall be maintained in the credit file of the affected borrower(s). The certification will be reviewed by this Office in subsequent examinations of the Bank; and,
- (e) documenting, with adequate supporting material, the value of collateral and properly perfecting the Bank's lien on it where applicable.

ARTICLE VI

ALLOWANCE FOR LOAN AND LEASE LOSSES

(1) Prior to the filing of Consolidated Reports of Condition and Income, the Board shall review the adequacy of the Bank's Allowance for Loan and Lease Losses (Allowance) and shall establish a program for the maintenance of an adequate Allowance. This review and program shall be designed in light of the comments on maintaining a proper Allowance found in the Allowance for Loan and Lease Losses

booklet, A-ALLL, of the Comptroller's Handbook, and shall focus particular attention on the following factors:

- (a) results of any Bank's internal loan review;
- (b) results of any Bank's external loan review;
- (c) an estimate of inherent loss exposure on each credit in excess of Seventy Five Thousand dollars (\$75,000);
- (d) loan loss experience;
- (e) trends of delinquent and nonaccrual loans;
- (f) concentrations of credit in the Bank; and,
- (g) present and prospective economic conditions.

(2) The program shall provide for a review of the Allowance by the Board at least once each calendar quarter. Any deficiency in the Allowance shall be remedied in the quarter it is discovered, prior to the filing of the Consolidated Reports of Condition and Income, by additional provisions from earnings. Written documentation shall be maintained indicating the factors considered and conclusions reached by the Board in determining the adequacy of the Allowance.

ARTICLE VII

CAPITAL PLAN

(1) Within ninety (90) days, the Board shall develop, implement, and thereafter ensure Bank adherence to a three year capital program. The program shall include contingency plans that identify alternative sources of capital should existing capital become insufficient to support the Bank's operations.

(2) Upon completion, the Bank's capital program shall be submitted to the Assistant Deputy Comptroller for approval. Upon approval by the Assistant Deputy Comptroller, the Bank shall implement and adhere to the capital program. The Board shall review and update the Bank's capital program on an annual basis, or more frequently if necessary. Copies of the reviews and updates shall be submitted to the Assistant Deputy Comptroller.

ARTICLE VIII

IMPLEMENTATION AND ADHERENCE

(1) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to Articles I, II, IV and VI of the Agreement.

ARTICLE IX

PROGRESS REPORTING

(1) The Board shall submit quarterly progress reports to the Assistant Deputy Comptroller. These reports shall set forth in detail:

- (a) actions taken to comply with each Article of the Agreement;
- (b) results of those actions; and,
- (c) a description of the actions needed to achieve full compliance with each Article of this Agreement.

(2) The progress reports should also include any actions initiated by the Board and the Bank pursuant to the criticisms and comments in the ROE or in any future Report of Examination. The first progress report shall be submitted for the period ending September 30, 2000 and will be due within thirty (30) days of that date. Thereafter, progress reports will be due within thirty (30) days after each quarter end.

ARTICLE X

CLOSING

(1) Although the Board has agreed to submit certain programs and reports to the Assistant Deputy Comptroller for review or approval, the Board expressly acknowledges it has the ultimate responsibility for proper and sound management of the Bank.

(2) It is expressly and clearly understood that if, at any time, the Comptroller deems it appropriate in fulfilling the responsibilities placed upon him by the several laws of the United States of America to undertake any action affecting the Bank, nothing in this Agreement shall in any way inhibit, estop, bar, or otherwise prevent the Comptroller from so doing.

(3) Any time limitations imposed by this Agreement shall begin to run from the effective date of this Agreement. Such time requirements may be extended in writing by the Assistant Deputy Comptroller for good cause, upon written application by the Board.

(4) The provisions of this Agreement shall be effective upon execution by the parties hereto and its provisions shall continue in full force and effect unless or until such provisions are amended in writing by mutual consent of the parties to the Agreement or excepted, waived, or terminated in writing by the Comptroller.

(5) It is expressly understood by the Board that this Agreement shall continue in full force and effect against the Bank and all of its corporate successors (other than one which succeeds by the purchase and assumption of the Bank's assets and liabilities), unless otherwise amended, excepted, waived or terminated. If such a business combination does occur, the terms hereof, however, shall only apply to those assets, liabilities and operations of the successor financial institution as have been acquired from the Bank.

IN TESTIMONY WHEREOF, the undersigned, authorized by the Comptroller, has hereunto set his hand on behalf of the Comptroller.

Signed

July 14, 2000

Jerilyn Gilland
Deputy Comptroller
Midwestern District

Date

IN TESTIMONY WHEREOF, the undersigned, as the duly elected and acting Board of Directors of the Bank, have hereunto set their hands on behalf of the Bank.

Signed

7-14-2000

Milton T. Mehlhaf
Chairman of the Board of Directors

Date

7-14-2000

Signed

John Waltner
Director and President

Date

7-14-2000

Signed

Jacqueline J. Mehlhaf.
Director

Date

7-14-2000

Signed

Pauline B. Waltner
Director

Date

7-14-2000

Signed

Jan K. Weier
Director

Date