

**#2003-27 also Terminates  
#2002-60**

**UNITED STATES OF AMERICA  
DEPARTMENT OF THE TREASURY  
OFFICE OF THE COMPTROLLER OF THE CURRENCY**

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**In the Matter of:** )  
The Lake Bank, National Association )  
Two Harbors, Minnesota; )  
Lance Schwanke, Senior Lending Officer; and )  
Thomas Kell, President )

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**CONSENT ORDER**

The Comptroller of the Currency of the United States of America (Comptroller), through his National Bank Examiner, has examined The Lake Bank, National Association, Two Harbors, Minnesota (Bank), and his findings are contained in the Report of Examination, dated October 28, 2002 (ROE).

The Bank, by and through its duly elected and acting Board of Directors (Board), has executed a "Stipulation and Consent to the Issuance of a Consent Order," dated March 20, 2003, that is accepted by the Comptroller. By this Stipulation and Consent, which is incorporated by reference, the Bank has consented to the issuance of this Consent Order (Order) by the Comptroller.

Pursuant to the authority vested in him by the Federal Deposit Insurance Act, as amended, 12 U.S.C. § 1818, the Comptroller hereby orders that:

**ARTICLE I**

**COMPETENT MANAGEMENT**

(1) Effective immediately upon the issuance of this Order, the Board shall relieve Lance Schwanke of the title "Senior Lending Officer" and shall relieve Lance Schwanke of all

duties and responsibilities associated with the Senior Lending Officer position, including but not limited to: acting as the Chairperson or a member of the Lending Committee; authorizing or approving loans for other lending officers; authorizing or approving loan workout plans for other lending officers; supervising lending officers; conducting performance appraisals of lending officers; determining the training needs of other lending officers; and analyzing or maintaining the allowance for loan and lease losses.

(2) Effective immediately upon the issuance of this Order, the Board shall require written approval by the Lending Committee and Board prior to Lance Schwanke making any loans or extensions of credit to one borrower in the aggregate amount of one hundred fifty thousand dollars (\$150,000) or more. Loans or extensions of credit to one borrower shall be determined in accordance with the provisions set forth in 12 U.S.C. § 84 and 12 C.F.R. § 32.

(3) Effective immediately upon the issuance of this Order, the Board shall require written approval by the Lending Committee and Board prior to Lance Schwanke authorizing any workout plan, restructure, or collection decision for any loans or extensions of credit to one borrower in the aggregate amount of one hundred fifty thousand dollars (\$150,000) or more. Loans or extensions of credit to one borrower shall be determined in accordance with the provisions set forth in 12 U.S.C. § 84 and 12 C.F.R. § 32.

(4) Within thirty (30) days, the Board shall review Lance Schwanke's compensation and ensure that it is at a level commensurate with his duties and responsibilities and the compensation provided to other lending officers at the Bank.

(5) Effective immediately upon the issuance of this Order, the Board shall limit Thomas Kell's duties and responsibilities associated with the Bank's lending department, including but not limited to: assuming the title or duties of Chairperson of the Lending

Committee; authorizing or approving loans to one borrower in the aggregate amount of one hundred fifty thousand dollars (\$150,000) or more without prior written Board approval; authorizing or approving loan workout plans to one borrower in the aggregate amount of one hundred fifty thousand dollars (\$150,000) or more without prior written Board approval; supervising lending officers; or analyzing and maintaining the allowance for loan and lease losses. Loans or extensions of credit to one borrower shall be determined in accordance with the provisions set forth in 12 U.S.C. § 84 and 12 C.F.R. § 32.

(6) Within thirty (30) days, the Board shall ensure that the Bank has competent management in place in the Senior Loan Officer and President positions to carry out the Board's policies, ensure compliance with this Order, applicable laws, rules and regulations, and manage the day-to-day operations of the Bank in a safe and sound manner.

(7) Prior to the appointment of any individual to an executive officer position, the Board shall submit to the Assistant Deputy Comptroller the following information:

- (a) the information sought in the "Changes in Directors and Senior Executive Officers" booklet of the Comptroller's Corporate Manual, together with a legible fingerprint card for the proposed individual;
- (b) a written statement of the Board's reasons for selecting the proposed officer; and
- (c) a written description of the proposed officer's duties and responsibilities.

(8) The Assistant Deputy Comptroller shall have the power of veto over the employment of the proposed executive officer. However, the failure to exercise such veto power shall not constitute an approval or endorsement of the proposed officer.

(9) The requirement to submit information and the prior veto provisions of this Article are based on the authority of 12 U.S.C. § 1818(b)(6)(E) and do not require the Comptroller to complete his review and act on any such information or authority within ninety (90) days.

## ARTICLE II

### LOAN REVIEW CONSULTANT

(1) Within fifteen (15) days, the Board shall employ a qualified, independent consultant to perform an ongoing asset quality review of the Bank. The consultant shall be utilized until such time as an ongoing internal asset quality review system is developed by the Board, implemented, and demonstrated to be effective. Before terminating the consultant's asset quality review services, the Board shall both certify the effectiveness of the internal asset quality review system, and receive prior determination of no supervisory objection from the Assistant Deputy Comptroller.

(2) Prior to hiring a consultant or entering into any contract with a consultant, the Bank shall submit the proposed terms of employment and the qualifications of the consultant to the Assistant Deputy Comptroller who shall have the power of veto. However, the failure to exercise such veto power shall not constitute an approval or endorsement of the proposed consultant.

(3) The requirement to submit information and the prior veto provisions of this Article are based on the authority of 12 U.S.C. § 1818(b) and do not require the Comptroller to complete his review and act on any such information or authority within ninety (90) days.

### ARTICLE III

#### INTERNAL LOAN REVIEW

(1) The Board shall employ or designate a sufficiently experienced and qualified person(s) or firm to ensure the timely and independent identification of problem loans and leases.

(2) Within thirty (30) days, the Board shall establish an effective, independent and on-going loan review system to review, at least quarterly, the Bank's loan and lease portfolios to assure the timely identification and categorization of problem credits. The system shall provide for a written report to be filed with the Board after each review and shall use a loan and lease grading system consistent with the guidelines set forth in Rating Credit Risk, A-RCR, of the Comptroller's Handbook. Such reports shall, at a minimum, include conclusions regarding:

- (a) the overall quality of the loan and lease portfolios;
- (b) the identification, type, rating, and amount of problem loans and leases;
- (c) the identification and amount of delinquent loans and leases;
- (d) credit and collateral documentation exceptions;
- (e) the identification and status of credit related violations of law, rule or regulation;
- (f) the identity of the loan officer who originated each loan reported in accordance with subparagraphs (b) through (e) of paragraph (2) of the Article;
- (g) concentrations of credit;
- (h) loans and leases to executive officers, directors, principal shareholders (and their related interests) of the Bank; and

- (i) loans and leases not in conformance with the Bank's lending and leasing policies, and exceptions to the Bank's lending and leasing policies.

(3) Within sixty (60) days of employing or designating the person(s) or firm referenced in paragraph (1), the Board shall develop, implement, and thereafter ensure Bank adherence to a written program providing for independent review of problem loans and leases in the Bank's loan and lease portfolios for the purpose of monitoring portfolio trends, on at least a quarterly basis. The program shall require a quarterly report to the Board. At a minimum, the program shall provide for an independent reviewer's assessment of the Bank's:

- (a) monitoring systems for early problem loan identification to assure the timely identification and rating of loans and leases based on lending officer submissions;
- (b) statistical records that serve as a basis for identifying sources of problem loans and leases by industry, size, collateral, indirect dealer, and individual lending officer;
- (c) system for monitoring previously charged-off assets and their recovery potential;
- (d) system for monitoring compliance with the Bank's lending policies and laws, rules, and regulations pertaining to the Bank's lending function; and
- (e) system for monitoring the adequacy of credit and collateral documentation.

(4) A written description of the program called for in this Article shall be forwarded to the Assistant Deputy Comptroller upon implementation.

(5) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the program developed pursuant to this Article.

(6) The Board shall evaluate the internal loan and lease review report(s) and shall ensure that immediate, adequate, and continuing remedial action, if appropriate, is taken upon all findings noted in the report(s).

(7) A copy of the reports submitted to the Board, as well as documentation of the action taken by the Bank to collect or strengthen assets identified as problem credits, shall be preserved in the Bank.

#### ARTICLE IV

##### LOAN PORTFOLIO MANAGEMENT

(1) The Board shall, within thirty (30) days, develop, implement, and thereafter ensure Bank adherence to a written program to improve the Bank's loan portfolio management.

The program shall include, but not be limited to:

- (a) procedures to ensure satisfactory and perfected collateral documentation;
- (b) 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;
- (c) procedures to ensure conformance with loan approval requirements;
- (d) a system to track and analyze exceptions;
- (e) procedures to ensure conformance with Call Report instructions;

- (f) procedures to ensure the accuracy of internal management information systems;
- (g) a performance appraisal process, including performance appraisals, job descriptions, and incentive programs for loan officers, which adequately consider their performance relative to policy compliance, documentation standards, accuracy in credit grading, and other loan administration matters;
- (h) procedures to track and analyze concentrations of credit, significant economic factors, volume of lending outside or the Bank's trade area, and general conditions and their impact on the credit quality of the Bank's loan and lease portfolios; and
- (i) procedures to ensure the adequacy of the Allowance for Loan and Lease Losses.

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

(3) Within thirty (30) days, the Board shall develop, implement, and thereafter ensure Bank adherence to systems which provide for effective monitoring of:

- (a) early problem loan identification to assure the timely identification and rating of loans and leases based on lending officer submissions;
- (b) statistical records that will serve as a basis for identifying sources of problem loans and leases by industry, size, collateral, indirect dealer, and individual lending officer;
- (c) previously charged-off assets and their recovery potential;

- (d) compliance with the Bank's lending policies and laws, rules, and regulations pertaining to the Bank's lending function;
- (e) adequacy of credit and collateral documentation; and
- (f) concentrations of credit.

(4) Beginning March 31, 2003, and on a monthly basis thereafter, management will provide the Board with written reports including, at a minimum, the following information:

- (a) the identification, type, rating, and amount of problem loans and leases;
- (b) the identification and amount of delinquent loans and leases;
- (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 each loan reported in accordance with subparagraphs (a) through (d) of paragraph (4) of the Article;
- (f) an analysis of concentrations of credit, significant economic factors, and general conditions and their impact on the credit quality of the Bank's loan and lease portfolios;
- (g) the identification and amount of loans and leases to executive officers, directors, principal shareholders (and their related interests) of the Bank;
- (h) the identification of loans and leases not in conformance with the Bank's lending and leasing policies, and exceptions to the Bank's lending and leasing policies; and,
- (i) the identification of all loans meeting the criteria for nonaccrual status.

(5) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the program and systems developed pursuant to this Article.

## ARTICLE V

### ALLOWANCE FOR LOAN AND LEASE LOSSES

(1) The Board shall make minimum provisions to the Bank's Allowance for Loan and Lease Losses (Allowance) of one hundred sixteen thousand dollars (\$116,000) as of September 30, 2002.

(2) The Board shall review the adequacy of the Bank's 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 the Bank's internal and external loan reviews;
- (b) an estimate of inherent loss exposure on each significant credit, including any credit categorized as "watch," "special mention," "substandard," "doubtful," "loss," "nonaccrual," past due greater than or equal to sixty (60) days, or any other credit with an outstanding balance equal to or greater than one hundred thousand dollars (\$100,000);
- (c) loan loss experience;
- (d) trends of delinquent and nonaccrual loans;
- (e) concentrations of credit in the Bank;

- (f) present and prospective economic conditions;
- (g) capabilities of changes in lending staff;
- (h) changes in loan volume and/or mix;
- (i) the volume of out-of-area lending; and
- (j) estimates of loss exposure for individual credits based on net realizable liquidation values of collateral.

(3) The program developed according to paragraph (2) of this Article 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.

(4) A copy of the Board's program required pursuant to paragraph (2) shall be submitted to the Assistant Deputy Comptroller for review and prior determination of no supervisory objection.

(5) Within five (5) days of submission to the Board, a copy of each quarterly Allowance review and documentation submitted to the Board pursuant to paragraph (3) shall be submitted to the Assistant Deputy Comptroller for a determination of no supervisory objection. In the event the Assistant Deputy Comptroller deems the methodology or Allowance balance inadequate, the Board shall take an immediate provision from earnings in the amount required by the Assistant Deputy Comptroller and amend the Report of Condition and Income.

(6) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the program developed pursuant to this Article.

## ARTICLE VI

### NONACCRUAL LOANS

(1) As detailed in the ROE, any subsequent Report of Examination, any internal or external loan review, or any correspondence or list provided to the Board or Bank management by the National Bank Examiners, the Bank shall immediately reverse or charge off all interest that has been accrued contrary to the requirements contained in the Instructions for Preparation of Consolidated Reports of Condition and Income (Call Report Instructions) governing nonaccrual loans. Further, the Bank shall immediately reverse or charge off that portion of the remaining accrued interest on such loans that, when combined with principal, is not protected by sound collateral values.

(2) Within thirty (30) days, the Board shall adopt and implement written policies and procedures governing the supervision and control of nonaccrual loans. Such policies and procedures shall:

- (a) be consistent with the accounting requirements contained in the Call Report Instructions;
- (b) address the circumstances under which accrued interest due on a loan may be added to the outstanding principal amount when the loan is renewed or restructured; and

(c) require the monthly presentation to the Board of all loans meeting any of the nonaccrual criteria.

(3) Within thirty (30) days, the Board shall develop and implement a written policy governing the identification of and accounting treatment for nonaccrual loans. The policy shall address paragraph (2) above and shall be consistent with the accounting requirements contained in the Call Report Instructions.

(4) Within thirty (30) days, the Board shall develop and implement a written policy that shall provide for auditing accrued interest on loans. The policy shall, at a minimum, provide for quarterly audits of loan accruals and incorporate procedures for periodically testing the Bank's identification of nonaccrual loans as governed by the policies adopted pursuant to paragraphs (2) and (3) above.

(5) Upon adoption, a copy of the written policies and procedures shall be forwarded to the Assistant Deputy Comptroller and the Board shall thereafter ensure Bank adherence to all policies and procedures developed pursuant to this Article.

(6) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the policies developed pursuant to this Article.

## ARTICLE VII

### CALL REPORTS - REFILE

(1) Within thirty (30) days, the Board shall cause the Bank to refile amended Reports of Condition and Income for the periods ending September 30, 2002, and December 31, 2002. As detailed in the ROE, any subsequent Report of Examination, any internal or external loan

review, or any correspondence or list provided to the Board or Bank management by the National Bank Examiners, the amended reports shall incorporate the required Allowance provisions, reversal of interest income on loans subject to nonaccrual status, and charge-off of inappropriate prepaid expenses and capitalized legal expenses.

(2) Within thirty (30) days, the Board shall adopt and cause the Bank to implement policies and procedures, in accordance with the Instructions for Preparation of Consolidated Reports of Condition and Income, to ensure that all official and regulatory reports filed by the Bank accurately reflect the Bank's condition as of the date that such reports are submitted. Thereafter the Board shall ensure Bank adherence to the policies and procedures adopted pursuant to this Article.

(3) Upon completion of the policies, the Board shall submit a copy of the policies to the Assistant Deputy Comptroller.

(4) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the policies developed pursuant to this Article.

## ARTICLE VIII

### CAPITAL PLAN AND HIGHER MINIMUMS

(1) The Bank shall achieve by March 31, 2003, and thereafter maintain, the following capital levels (as defined in 12 C.F.R. Part 3):

- (a) Total risk based capital at least equal to ten percent (10%) of risk-weighted assets;
- (b) Tier 1 capital at least equal to eight percent (8%) of risk-weighted assets;

(c) Tier 1 capital at least equal to seven percent (7%) of adjusted total assets.<sup>1</sup>

(2) The requirement in this Order to meet and maintain a specific capital level means that the Bank may not be deemed to be “well capitalized” for purposes of 12 U.S.C. § 1831o and 12 C.F.R. Part 6 pursuant to 12 C.F.R. § 6.4(b)(1)(iv).

(3) Within thirty (30) days, the Board shall develop, implement, and thereafter ensure Bank adherence to a three-year capital program. The program shall include:

- (a) specific plans for the maintenance of adequate capital that may in no event be less than the requirements of paragraph (1);
- (b) projections for growth and capital requirements based upon a detailed analysis of the Bank's assets, liabilities, earnings, fixed assets, and off-balance sheet activities;
- (c) projections of the sources and timing of additional capital to meet the Bank's current and future needs;
- (d) the primary source(s) from which the Bank will strengthen its capital structure to meet the Bank's needs;
- (e) contingency plans that identify alternative methods should the primary source(s) under paragraph (d) above not be available;
- (f) specific timeframes for the Bank's return to “well capitalized” as defined in 12 C.F.R. Part 6 for Prompt Corrective Action; and,
- (g) a dividend policy that permits the declaration of a dividend only:
  - (i) when the Bank is in compliance with its approved capital program;
  - (ii) when the Bank is in compliance with 12 U.S.C. §§ 56 and 60; and

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<sup>1</sup> Adjusted total assets is defined in 12 C.F.R. § 3.2(a) as the average total asset figure used for Call Report purposes minus end-of-quarter intangible assets.

(iii) with the prior determination of no supervisory objection by the Assistant Deputy Comptroller.

(4) Upon completion, the Bank's capital program shall be submitted to the Assistant Deputy Comptroller for prior determination of no supervisory objection. Upon receiving a determination of no supervisory objection from 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.

(5) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the program developed pursuant to this Article.

## ARTICLE IX

### CRITICIZED ASSETS

(1) The Bank shall take immediate and continuing action to protect its interest in those assets criticized in the ROE, in any subsequent Report of Examination, by internal or external loan review, or in any correspondence or list provided to the Board or Bank management by the National Bank Examiners.

(2) The Board shall immediately adopt, implement, and thereafter ensure Bank adherence to a written program 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 correspondence or list provided to the Board or Bank management by the National Bank

Examiners as "doubtful," "substandard," or "special mention." This program shall include, at a minimum:

- (a) an identification of the expected sources of repayment;
- (b) the appraised value and net realizable liquidation 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.

(3) Upon adoption, a copy of the program for all criticized assets equal to or exceeding one hundred thousand dollars (\$100,000) shall be forwarded to the Assistant Deputy Comptroller.

(4) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the program developed pursuant to this Article.

- (5) The Board shall conduct a review on at least a monthly basis, to determine:
- (a) the status of each criticized asset or criticized portion thereof that equals or exceeds one hundred thousand dollars (\$100,000);
  - (b) management's adherence to the program adopted pursuant to this Article;
  - (c) the status and effectiveness of the written program; and
  - (d) the need to revise the program or take alternative action.

(6) A copy of each review shall be forwarded to the Assistant Deputy Comptroller on a monthly basis (in a format similar to Appendix A, attached hereto).

(7) The Bank may extend credit, directly or indirectly, including renewals, extensions or capitalization of accrued interest, to a borrower whose loans or other extensions of credit are criticized in the ROE, in any subsequent Report of Examination, in any internal or external loan review, or in any list provided to management by the National Bank Examiners during any examination and whose aggregate loans or other extensions exceed fifty thousand dollars (\$50,000) only if each of the following conditions is met:

- (a) the Board finds that the extension of additional credit is necessary to promote the best interests of the Bank and that prior to renewing, extending or capitalizing any additional credit, a majority of the full Board approves the credit extension and records, in writing, why such extension is necessary to promote the best interests of the Bank; and
- (b) a comparison to the written program adopted pursuant to this Article shows that the Board's formal plan to collect or strengthen the criticized asset will not be compromised.

(8) A copy of the approval of the Board, including documentation demonstrating consideration of the factors contained in paragraph (7) above, shall be maintained in the file of the affected borrower.

## ARTICLE X

### CREDIT AND COLLATERAL EXCEPTIONS

(1) Within thirty (30) 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 thirty (30) 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, or restructure any loan or other extension of credit 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 (3)(d) shall require a majority of the full Board (or a delegated committee thereof) to certify in writing the specific reasons why obtaining and analyzing the information in (3)(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 XI

### CREDIT RISK

(1) Within thirty (30) days, the Board shall develop, implement, and thereafter ensure Bank adherence to a written program to reduce the high level of credit risk in the Bank. The program shall include, but not be limited to:

- (a) procedures to strengthen credit underwriting, particularly in the commercial and commercial real estate portfolios;
- (b) procedures to strengthen management of commercial lending operations and to maintain an adequate, qualified staff in all commercial and commercial real estate loan functional areas;
- (c) procedures for strengthening collections; and
- (d) an action plan to limit aggregate commercial and commercial real estate loan growth to no more than three percent (3%) per annum.

(2) The Board shall submit a copy of the program to the Assistant Deputy Comptroller.

(3) At least quarterly, the Board shall prepare a written assessment of the bank's credit risk, which shall evaluate the Bank's progress under the aforementioned program. The Board shall submit a copy of this assessment to the Assistant Deputy Comptroller.

(4) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the program developed pursuant to this Article.

## ARTICLE XII

### 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, any subsequent Report of Examination, or any correspondence provided to the Board or Bank management by the National Bank Examiners. The monthly progress reports required by Article XIII of this Order shall include the date and manner in which each correction has been effected during that reporting period.

(2) Within thirty (30) 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 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.

(4) Upon adoption, a copy of these procedures shall be promptly forwarded to the Assistant Deputy Comptroller.

(5) The Board shall ensure that the Bank has policies, processes, personnel, and control systems to ensure implementation of and adherence to the procedures developed pursuant to this Article.

### ARTICLE XIII

#### COMPLIANCE COMMITTEE AND PROGRESS REPORTS

(1) Within thirty (30) days, the Board shall appoint a Compliance Committee of at least three (3) directors, of which no more than one (1) member shall be an employee of the Bank or a family member of any such person. Upon appointment, the names of the members of the Compliance Committee shall be submitted in writing to the Assistant Deputy Comptroller. The Compliance Committee shall be responsible for monitoring and coordinating the Bank's adherence to the provisions of this Order.

(2) The Compliance Committee shall meet at least monthly.

(3) Within thirty (30) days of the appointment of the Committee and every thirty (30) days thereafter, the Compliance Committee shall submit a written report to the Board setting forth in detail:

- (a) actions taken to comply with each Article of this Order; and
- (b) the results of those actions.

(4) Upon its review of the Compliance Committee report, the Board shall set forth in writing a progress report describing the actions needed to achieve full compliance with each Article of the Order and 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.

(5) The Board shall forward a copy of the Compliance Committee's report, together with the Board's progress report, to the Assistant Deputy Comptroller, Minneapolis North Field Office, 920 Second Avenue South, Suite 800, Minneapolis, Minnesota 55402. The first progress report shall be submitted by the Board to the Assistant Deputy Comptroller for the period ending March 31, 2003, and shall be due within ten (10) days of that date. Thereafter, progress reports will be due within ten (10) days after the month end.

#### ARTICLE XIV

##### STRATEGIC PLAN FOR THE RESOLUTION OF THE BANK

(1) If at any time, but no earlier than thirty (30) days from the issuance of this Order, the OCC determines, in its sole judgment, that the Bank has failed to comply with the requirements of Article I, Article IV, or Article VIII, then within thirty (30) days of receiving written notice from the OCC of such fact, the Bank shall develop and shall submit to the OCC for its review and prior determination of no supervisory objection a Contingency Plan, which shall detail the Board's proposal to either: (i) sell or merge the Bank; or (ii) liquidate the Bank in conformance with 12 U.S.C. § 181 and in a manner that will result in no loss or cost to the Federal Deposit Insurance Corporation. The Bank agrees that it will not schedule a vote of its shareholders so as to seek their approval to liquidate the Bank prior to securing the OCC's written determination of no supervisory objection to the Contingency Plan.

(2) After the OCC has advised the Bank that it does not take supervisory objection to the Contingency Plan, the Board shall immediately implement, and shall thereafter ensure adherence to, the terms of the Contingency Plan. Failure to submit a timely, acceptable Contingency Plan may be deemed a violation of this Order, in the exercise of the OCC's sole discretion.

(3) In lieu of implementing Article I, Article IV, and/or Article VIII, the Bank may, within thirty (30) days of the effective date of this Order, submit the written Contingency Plan described in paragraph (1) of this Article to the OCC for its review and prior written determination of no supervisory objection.

(4) After the OCC has advised the Bank that it does not take supervisory objection to the Contingency Plan submitted pursuant to paragraph (3) of this Article, the Board shall immediately implement, and shall thereafter ensure adherence to, the terms of the Contingency Plan. Failure to submit a timely, acceptable Contingency Plan may be deemed a violation of this Order, in the exercise of the OCC's sole discretion.

## ARTICLE XV

### REPLACEMENT OF THE JUNE 21, 2002 FORMAL AGREEMENT

(1) On June 21, 2002, the Bank entered into a Formal Agreement (Formal Agreement) with the Comptroller. Effective immediately upon the issuance of this Order, the Articles of the Formal Agreement shall be replaced in their entirety by this Order.

## ARTICLE XVI

### CLOSING

(1) Although the Board is by this Order required to submit certain proposed actions and programs for the review or approval of the Assistant Deputy Comptroller, the Board 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 Order shall in any way inhibit, estop, bar or otherwise prevent the Comptroller from so doing.

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

(4) The provisions of this Order are effective upon issuance of this Order by the Comptroller, through his authorized representative whose hand appears below, and shall remain effective and enforceable, except to the extent that, and until such time as, any provisions of this Order shall have been amended, suspended, waived, or terminated in writing by the Comptroller.

(5) In each instance in this Order in which the Board is required to ensure adherence to, and undertake to perform certain obligations of the Bank, it is intended to mean that the Board shall:

- (a) authorize and adopt such actions on behalf of the Bank as may be necessary for the Bank to perform its obligations and undertakings under the terms of this Order;

- (b) require the timely reporting by Bank management of such actions directed by the Board to be taken under the terms of this Order;
- (c) follow-up on any non-compliance with such actions in a timely and appropriate manner; and
- (d) require corrective action be taken in a timely manner of any non-compliance with such actions.

(6) This Order is intended to be, and shall be construed to be, a final order issued pursuant to 12 U.S.C. § 1818(b), and expressly does not form, and may not be construed to form, a contract binding on the OCC or the United States.

(7) The terms of this Order, including this paragraph, are not subject to amendment or modification by any extraneous expression or prior agreements or arrangements between the parties, whether oral or written.

IT IS SO ORDERED, this 20<sup>th</sup> day of March, 2003.

/s/ Thomas J. Tott

Thomas J. Tott  
Assistant Deputy Comptroller  
Minneapolis North Field Office

3/20/2003

Date

**UNITED STATES OF AMERICA  
DEPARTMENT OF THE TREASURY  
OFFICE OF THE COMPTROLLER OF THE CURRENCY**

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**In the Matter of:** )  
The Lake Bank, National Association )  
Two Harbors, Minnesota; )  
Lance Schwanke, Senior Lending Officer; and )  
Thomas Kell, President )

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**STIPULATION AND CONSENT TO THE ISSUANCE  
OF A CONSENT ORDER**

The Comptroller of the Currency of the United States of America (Comptroller) has initiated cease and desist proceedings against The Lake Bank, National Association, Two Harbors, Minnesota (Bank) pursuant to 12 U.S.C. § 1818(b).

The Bank, in the interest of compliance and cooperation, consents to the issuance of a Consent Order, dated March 20, 2003 (Order);

In consideration of the above premises, the Comptroller, through his authorized representative, and the Bank, through its duly elected and acting Board of Directors, hereby stipulate and agree to the following:

ARTICLE I

Jurisdiction

(1) The Bank is a national banking association chartered and examined by the Comptroller pursuant to the National Bank Act of 1864, as amended, 12 U.S.C. § 1 *et seq.*

(2) The Comptroller is “the appropriate Federal banking agency” regarding the Bank pursuant to 12 U.S.C. §§ 1813(q) and 1818(b).

(3) The Bank is an “insured depository institution” within the meaning of 12 U.S.C. § 1818(b)(1).

## ARTICLE II

### Agreement

(1) The Bank, without admitting or denying any wrongdoing, hereby consents and agrees to the issuance of the Order by the Comptroller.

(2) The Bank further agrees that said Order shall be deemed an “order issued with the consent of the depository institution” as defined in 12 U.S.C. § 1818(h)(2), and consents and agrees that said Order shall become effective upon its issuance and shall be fully enforceable by the Comptroller under the provisions of 12 U.S.C. § 1818(i). Notwithstanding the absence of mutuality of obligation, or of consideration, or of a contract, the OCC may enforce any of the commitments or obligations herein undertaken by the Bank under its supervisory powers, including 12 U.S.C. § 1818(i), and not as a matter of contract law. The Bank expressly acknowledges that neither the Bank nor the OCC has any intention to enter into a contract.

(3) The Bank also expressly acknowledges that no OCC officer or employee has statutory or other authority to bind the United States, the U.S. Treasury Department, the OCC, or any other federal bank regulatory agency or entity, or any officer or employee of any of those entities to a contract affecting the OCC’s exercise of its supervisory responsibilities.

## ARTICLE III

### Waivers

- (1) The Bank, by signing this Stipulation and Consent, hereby waives:
- (a) the issuance of a Notice of Charges pursuant to 12 U.S.C. § 1818(b);
  - (b) any and all procedural rights available in connection with the issuance of the Order;

- (c) all rights to seek any type of administrative or judicial review of the Order; and
- (d) any and all rights to challenge or contest the validity of the Order.

ARTICLE IV

Other Action

(1) The Bank agrees that the provisions of this Stipulation and Consent shall not inhibit, estop, bar, or otherwise prevent the Comptroller from taking any other action affecting the Bank if, at any time, he deems it appropriate to do so to fulfill the responsibilities placed upon him by the several laws of the United States of America.

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

/s/ Thomas J. Tott

Thomas J. Tott  
Assistant Deputy Comptroller  
Minneapolis North Field Office

3/20/2003

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 _____ John Fredrickson	3-18-03 _____ Date
_____ Todd Haugen	_____ Date
Signed _____ Mark Johnson	3/18/03 _____ Date
Signed _____ Tom Kell	3-20-03 _____ Date
_____ Jacqueline Murray	_____ Date

**APPENDIX A**  
The Lake Bank, National Association  
Two Harbors, Minnesota

CRITICIZED ASSET REPORT AS OF: \_\_\_\_\_

BORROWER(S): \_\_\_\_\_

ASSET BALANCE(S) AND OCC RATING (SM, SUBSTANDARD, DOUBTFUL OR LOSS):

\$ \_\_\_\_\_ CRITICISM \_\_\_\_\_

AMOUNT CHARGED OFF TO DATE \_\_\_\_\_

FUTURE POTENTIAL CHARGE-OFF \_\_\_\_\_

PRESENT STATUS (Fully explain any increase in outstanding balance; include past due status, nonperforming, significant progress or deterioration, etc.):

FINANCIAL AND/OR COLLATERAL SUPPORT (include brief summary of most current financial information, appraised value of collateral and/or estimated value and date thereof, bank's lien position and amount of available equity, if any, guarantor(s) info, etc.):

PROPOSED PLAN OF ACTION TO ELIMINATE ASSET CRITICISM(S) AND TIME FRAME FOR ITS ACCOMPLISHMENT:

IDENTIFIED SOURCE OF REPAYMENT AND DEFINED REPAYMENT PROGRAM (repayment program should coincide with source of repayment):

Use this form for reporting each criticized asset that exceeds one hundred thousand dollars (\$100,000) and retain the original in the credit file for review by the examiners. Submit your reports monthly for credits exceeding one hundred fifty thousand dollars (\$150,000) until notified otherwise, in writing, by the Assistant Deputy Comptroller.