

#2004-16 also *Terminates*
#2003-27

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

In the Matter of:)
The Lake Bank, National Association)
Two Harbors, Minnesota)

AMENDED 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).

The Bank, by and through its duly elected and acting Board of Directors (Board), executed a Stipulation and Consent to the Issuance of a Consent Order, dated March 20, 2003, that was accepted by the Comptroller (March 2003 Order).

The Bank, by and through its duly elected and acting Board, has executed a “Stipulation and Consent to the Issuance of an Amended Consent Order,” dated March 10, 2004, 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 Amended Consent Order (Order) by the Comptroller. This Order replaces in its entirety the March 2003 Order, and the March 2003 Order is hereby terminated.

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

STRATEGIC PLAN

(1) Within ninety (90) days, the Board shall adopt, implement, and thereafter ensure adherence to a written strategic plan for the Bank covering at least a three-year period. The strategic plan shall establish objectives for the Bank's overall risk profile, earnings performance, growth, balance sheet mix, off-balance sheet activities, liability structure, capital adequacy, reduction in the volume of non-performing assets, product line development and market segments that the Bank intends to promote or develop, together with strategies to achieve those objectives and, at a minimum, include:

- (a) a mission statement that forms the framework for the establishment of strategic goals and objectives;
- (b) a formal assessment of the Bank's present and future operating environment to include a written risk management program consistent with the Bank Supervision Process booklet, EP-Sup, of the Comptroller's Handbook to include, at a minimum, the following:
 - (i) identification and analysis of existing risks;
 - (ii) action plans and time frames to reduce risks in areas identified as high risk to include those discussed in the Report of Examination;
 - (iii) reasonable and appropriate limits for credit, interest rate, liquidity, transaction, compliance, strategic, and reputation risks, which limits shall be consistent with the Strategic Plan and defined in terms of readily measurable standards;

- (iv) policies, procedures, control, monitoring and reporting systems to ensure that the Bank complies with the risk limits approved by the Board; and
 - (v) policies and procedures to ensure that relevant Bank employees have the necessary skills to supervise effectively the current and the new business risks within the Bank, and procedures to describe the actions to be taken to address deficiencies in staff levels and skills.
- (c) the development of strategic goals and objectives to be accomplished over the short and long term;
 - (d) an identification of the Bank's present and future market and product lines (assets and liabilities) that will be utilized to accomplish the strategic goals and objectives established in (1)(c) of this Article;
 - (e) an evaluation of the Bank's internal operations, staffing requirements, board and management information systems and policies and procedures for their adequacy and contribution to the accomplishment of the goals and objectives developed under (1)(c) of this Article;
 - (f) a management employment and succession program to promote the hiring, retention and continuity of capable management; and
 - (g) systems to monitor the Bank's progress in meeting the plan's goals and objectives.

(2) Upon adoption, a copy of the plan, or any subsequent revisions or amendments, shall be forwarded to the Director for Special Supervision (Director) for review.

(3) The Board shall ensure that the Bank develops and thereafter maintains processes, personnel, and control systems to ensure implementation of and adherence to the plan developed pursuant to this Article.

Article II

PROFIT PLAN

(1) Within sixty (60) days, the Board shall develop, implement, and thereafter ensure adherence to a written profit plan to improve and sustain the earnings of the Bank. This plan shall cover at least a three-year period, consistent with the Strategic Plan, and shall include, at minimum, the following elements:

- (a) identification of the major areas and means by which the Board will seek to improve the Bank's operating performance;
- (b) realistic and comprehensive budgets, including projected balance sheets and year-end income statements;
- (c) a budget review process to monitor both the Bank's income and expenses, and to compare actual figures with budgetary projections; and
- (d) a description of the operating assumptions that form the basis for major projected income and expense components.

(2) The Board shall submit the budgets and related documents required in paragraph (1) above for 2004 to the Director upon completion. Thereafter, prior to the new year, the Board shall submit to the Director annual budgets as described in paragraph (1) above.

(3) The Board shall forward comparisons of its actual balance sheet and profit and loss statement to the profit plan projections to the Director on a quarterly basis.

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

Article III

CAPITAL PLAN AND HIGHER MINIMUMS

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

- (a) Tier 1 capital at least equal to seven percent (7%) of adjusted total assets.¹
- (b) Tier 1 capital at least equal to eight percent (8%) of risk-weighted assets;

(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 sixty (60) 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;

¹ 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.

- (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; and
- (f) 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
 - (iii) with the prior determination of no supervisory objection by the Director.

(4) Upon completion, the Bank's capital program, or any subsequent revisions or amendments, shall be submitted to the Director for prior determination of no supervisory objection. Upon receiving a determination of no supervisory objection from the Director, 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 Director.

(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 IV

LOAN PORTFOLIO MANAGEMENT

(1) The Board shall, within ninety (90) 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, procedures and monitoring systems:

- (a) to ensure satisfactory and perfected collateral documentation;

- (b) 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) to ensure that loan participations are consistent with safe and sound banking practices, and the guidelines set forth in Banking Circular 181 (Revised), dated August 2, 1984;
- (d) to ensure conformance with the Bank's lending policies and loan approval requirements;
- (e) to track and analyze exceptions to the Bank's lending policies;
- (f) to track and analyze previously charged-off assets and their recovery potential; and
- (g) to track and analyze concentrations of credit, volume of lending outside of the Bank's trade area, and significant economic factors and their impact on the credit quality of the Bank's loan and lease portfolios.

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

(3) Within ninety (90) days, the Board shall develop, implement, and thereafter ensure adherence to 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, early identification of problem loans, accuracy in credit grading, and other loan administration matters.

(4) On a monthly basis, 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) a quarterly analysis of concentrations of credit, significant economic factors, and general economic 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, including approved 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

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 ninety (90) 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:

- (a) conclusions regarding 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) the identification of credit and collateral documentation exceptions;
- (e) the identification of loans meeting the criteria for nonaccrual status;
- (f) the identification and status of credit related violations of law, rule or regulation;
- (g) the identification of loans and leases not in conformance with the Bank's lending and leasing policies, including approved exceptions to the Bank's lending and leasing policies;
- (h) the identity of the loan officer who originated or is responsible for each loan reported in accordance with subparagraphs (b) through (g) of paragraph (2) of the Article;
- (i) the identification of concentrations of credit; and
- (j) the identification of loans and leases to executive officers, directors, principal shareholders (and their related interests) of the Bank.

(3) The Board shall evaluate the loan 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).

(4) 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.

(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 VI

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, within thirty (30) days of identification of a criticized asset, adopt (in a format similar to Appendix A, attached hereto), 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 identified 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 those criticized assets equal to or exceeding one hundred thousand dollars (\$100,000) shall be forwarded to the Director.

(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 equal to or exceeding 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 for those criticized assets equal to or exceeding one hundred thousand dollars (\$100,000) shall be forwarded to the Director on a monthly basis.

(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, or committee thereof, 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 Board, or committee thereof, 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 VII

CREDIT AND COLLATERAL EXCEPTIONS

(1) Within thirty (30) days of identification or notice, the Board shall take all steps necessary to obtain current and satisfactory credit information on loans lacking such information, including those loans 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 of identification or notice, the Board shall take all steps necessary to ensure proper collateral documentation is maintained on all loans and correct each collateral exception, 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.

(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 VIII

ALLOWANCE FOR LOAN AND LEASE LOSSES

(1) 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 loan review;
- (b) inherent loss exposure in each significant credit, including estimates of loss exposure for individual credits based on net realizable liquidation values of collateral;
- (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 lending staff;
- (h) changes in loan volume and/or mix; and
- (i) the volume of out-of-area lending..

(2) 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.

(3) 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

NEW SENIOR LENDING OFFICER

(1) If the Office of the Comptroller of the Currency determines that the Bank requires the services of a full time Senior Lending Officer in order to ensure adequate supervision and

management of the Bank's lending function, then within ninety (90) days of receiving written notice from the Director of such determination, the Bank shall identify a new capable Senior Lending Officer who, following review and a determination of no supervisory objection by the Director, shall be vested with sufficient executive authority to fulfill the duties and responsibilities of the position.

(2) The requirement to submit information and the prior determination of no supervisory objection provisions of this Article are based on the authority of 12 U.S.C. § 1818(b).

Article X

COMPLIANCE COMMITTEE AND PROGRESS REPORTS

(1) Within thirty (30) days, the Board shall appoint a Compliance Committee of at least three (3) directors. Upon appointment, the names of the members of the Compliance Committee shall be submitted in writing to the Director. 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 Compliance Committee and monthly 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) Unless notified in writing by the Director, the monthly reporting requirement contained in paragraph (3) shall revert to quarterly, one hundred and twenty (120) days after the effective date of this Order.

(5) 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.

(6) The Board shall forward a copy of the Compliance Committee's report, together with the Board's progress report, to the Director.

Article XI

CLOSING

(1) Although the Board is by this Order required to submit certain proposed actions and programs for the review or approval of the Director, 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 Director 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 15th day of March, 2004.

/s/ Ronald G. Schneck

Ronald G. Schneck
Director for Special Supervision
Comptroller of the Currency

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

In the Matter of:)
The Lake Bank, National Association)
Two Harbors, Minnesota)

**STIPULATION AND CONSENT TO THE ISSUANCE
OF AN AMENDED CONSENT ORDER**

The Lake Bank, National Association, Two Harbors, Minnesota (Bank), by and through its duly elected and acting Board of Directors (Board), in the interest of compliance and cooperation, consents to the issuance of an Amended Consent Order, dated March 10, 2004 (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 Consent Order dated March 20, 2003, between the Bank and the Comptroller is hereby superceded by this Order, and, therefore, the March 20, 2003 Consent Order is hereby terminated.

(2) 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/ Ronald G. Schneck

3/15/04

Ronald G. Schneck
Director for Special Supervision
Comptroller of the Currency

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 _____ Stephen Daggett	3/10/04 _____ Date
Signed _____ Charles Gesme	3-10-04 _____ Date
Signed _____ Paul Gesme	3/10/04 _____ Date
Signed _____ Peter F. Jeronimus	3/10/04 _____ Date
Signed _____ Dennis Lind	3-10-04 _____ Date
Signed _____ Bryan Rude	3-10-04 _____ Date
Signed _____ Richard Shepley	3/10/04 _____ Date