

UNITED STATES OF AMERICA
Before The
OFFICE OF THRIFT SUPERVISION

In the Matter of)
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D&N BANK, A FEDERAL SAVINGS BANK)
HANCOCK, MICHIGAN (OTS #0787))
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Re: Resolution No. 100 91-2

STIPULATION AND CONSENT TO ISSUANCE
OF ORDER TO CEASE AND DESIST

The Office of Thrift Supervision ("OTS"), by and through its Regional Director for the Central Region and D&N Bank, A Federal Savings Bank, Hancock, Michigan (the "Institution"), stipulate and agree as follows:

1. Consideration. The OTS, based upon information reported to it, is of the opinion that grounds exist to initiate an administrative cease and desist proceeding against the Institution pursuant to Section 8(b) of the Federal Deposit Insurance Act ("FDIA"), as amended by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183 ("FIRREA") (to be codified at 12 U.S.C. 1818(b)). The Institution desires to cooperate with the OTS and to avoid the time and expense of such administrative litigation and, without admitting or denying that such grounds exist, hereby stipulates and agrees to the following terms in consideration of the forbearance by the OTS from initiating such administrative cease-and-desist litigation against the Institution with respect to the matters covered in the accompanying Order to Cease and Desist ("Order").

2. Jurisdiction.

(a) The Institution is a "savings association" within the meaning of Section 3 of the FDIA and Section 2 of the Home Owners' Loan Act, as amended by FIRREA. Accordingly, it is an "insured depository institution" as that term is defined in Section 3(c) of the FDIA, as amended by FIRREA (to be codified at 12 U.S.C. 1813(c)).

(b) Pursuant to Section 3 of the FDIA, as amended by FIRREA, the Director of OTS is the "appropriate Federal Banking agency" to maintain an enforcement proceeding against such a savings association. Therefore, the Institution is subject to the authority of the OTS to initiate and maintain a cease and desist proceeding against it pursuant to Section 8(b) of the FDIA, as amended by FIRREA (to be codified at 12 U.S.C. 1818(b)).

3. Consent. The Institution consents to the issuance by the OTS of the Order. It further agrees to comply with the terms of the Order upon issuance and stipulates that the Order complies with all requirements of law.

4. Finality. The Order is issued under Section 8(b) of the FDIA, as amended by FIRREA (to be codified at 12 U.S.C. 1818(b)). Upon its issuance by the Regional Director for the Central Region, OTS, it shall be a final order, effective and fully enforceable by the OTS under the provisions of Section 8(i) of the FDIA, as amended by FIRREA (to be codified at 12 U.S.C. 1818(i)).

5. Waivers. The Institution waives its right to a notice of charges and the administrative hearing provided by Section 8(b) of the FDIA, as amended by FIRREA (to be codified at 12 U.S.C. 1818(b)), and further waives any right to seek judicial review of the Order, including any such right provided by Section 8(h) of the FDIA, as amended by FIRREA (to be codified at 12 U.S.C. 1818(h)), or otherwise to challenge the validity of the Order.

2. Reduce the volume of its classified assets; and
3. Establish and maintain adequate reserves for loan losses.

IT IS FURTHER ORDERED that:

STRATEGIC PLANNING

1. D&N shall take action in cooperation with D&N Financial Corporation to evaluate the desirability of marketing the savings association to a potential acquirer or merger partner who could meet all known legal and policy requirements for acquisition of D&N. Such action shall include documented contacts with potential acquirers/merger partners, written reports by management to the Board and documented deliberations by the Board. Evaluation of the desirability of marketing the savings association shall specifically address the feasibility of D&N attaining capital compliance and regulatory compliance as well as adherence to safe and sound practices by means which do not include an acquisition. D&N shall report in writing to the Deputy Regional Director of OTS on its evaluation of the desirability of marketing the association within 60 days of the date of the hiring of an investment banking firm by D&N to assist in this evaluation and each 30 days thereafter or more frequently at the request of the Deputy Regional Director.

PERSONNEL

2. During the effectiveness of this Order, D&N shall make every reasonable effort to employ additional qualified executive officers acceptable to the Deputy Regional Director of the OTS. D&N, acting through its Board,

shall terminate or reassign any executive officer of D&N as directed in writing by the Deputy Regional Director of OTS. D&N shall implement such termination or reassignment immediately upon receiving the OTS notification. Qualified executive officers at D&N shall include a new experienced Senior Loan Officer with loan workout experience and a new Chief Financial Officer. If either of the two current officers in these positions are to be retained in employment in another capacity at D&N, the Board will provide justification for this decision, impose limits on their authority, and establish oversight over their activities in a manner acceptable to the Deputy Regional Director. Executive officers shall include persons holding the title of Chief Executive Officer, Chairman of the Board, Chief Operating Officer, Managing Officer, President, Executive Vice President, Senior Vice President and any other officer who participates or has the authority to participate in major policy making decisions at D&N. D&N may apply to the Deputy Regional Director of OTS to obtain a determination as to whether a particular officer participates or has the authority to participate in major policy making decisions at D&N for the purposes of this Order.

3. D&N shall not appoint any person to an executive officer position without the prior written approval of the Deputy Regional Director of the OTS. Any executive officer of D&N shall be required by the Board to read this Order and certify such in writing at the direction of the Deputy Regional Director of OTS.

4. In order to improve loan workout capability, the Board shall assess adequacy of personnel resources to manage asset quality workout efforts. A written report of its assessment and a plan to improve staffing shall be submitted to the Deputy Regional Director of the OTS within the earlier of thirty (30) days of the date of hiring a new Senior Loan Officer or sixty (60)

days from the date of this Order.

5. D&N shall not pay any bonus to, or increase the salary or benefits of, any executive officer without the prior written approval of the Deputy Regional Director of the OTS unless otherwise required by law as supported by a legal opinion from counsel for D&N which is acceptable to the Deputy Regional Director of OTS.

6. D&N shall not increase its directors' fees or benefits without the prior written approval of the Deputy Regional Director of the OTS.

7. D&N shall immediately terminate the practice of paying employees and officers for accrued sick leave in circumstances in which the employee is not eligible for such leave based on actual illness unless otherwise required by law as supported by a legal opinion from counsel for D&N which is acceptable to the Deputy Regional Director of OTS.

8. D&N shall not enter into or renew any employment contract with any officer or employee without the prior written approval of the Deputy Regional Director of the OTS. If any existing employment contract contains an automatic renewal ("evergreen") provision, D&N shall immediately take all necessary steps to terminate the automatic renewal feature.

9. Within thirty (30) days of the date hereof, D&N shall submit for approval to the Deputy Regional Director of the OTS a plan to: (a) reduce the number of employment contracts it has with its officers; (b) reduce the terms of the existing employment contracts to no more than twelve (12) months; and (c) adopt the provisions of 12 C.F.R. Section 563.39 (1990) in all existing employment contracts. All contracts proposed in the future shall enjoy the deliberations of D&N's full Board and said deliberative process shall be documented in the Board's minutes and included in the submission to the OTS for approval.

10. D&N shall not execute any termination agreements with any directors, officers or employees without the documented authorization of its Board and the prior written approval of the Deputy Regional Director of the OTS, except pursuant to a plan adopted by the Board of Directors and approved by the Deputy Regional Director of OTS.

11. Within thirty (30) days of the date of this Order, D&N, through its Board, shall review the settlement terms of the separation agreement with Walker Aaron and provide the Deputy Regional Director of the OTS with a written report of its conclusions and any proposed corrective actions. No settlement shall be agreed to with Mr. Aaron without prior approval of the Deputy Regional Director of OTS. The Board is also directed to provide the Deputy Regional Director of the OTS with a quarterly update of the status of the resulting legal action(s), along with estimates of the cost of any anticipated out-of-court settlement with Mr. Aaron. Such updates shall be submitted to the OTS quarterly within thirty (30) days of the close of each calendar quarter.

12. D&N shall obtain for its Board an independent review by its external accountants of the propriety of the accounting for costs associated with termination agreements entered into by D&N since January 1, 1989. Within thirty (30) days of the date of this Order, the Board shall provide the Deputy Regional Director of the OTS with a copy of its accountant's review of this matter.

13. D&N shall not violate Section 563.41 of the OTS Regulations.

14. D&N shall immediately terminate the practice of purchasing prospective employees residences without the prior approval of the Deputy Regional Director of OTS. Any proposal to incorporate this benefit as part of an effort to attract competent management shall be fully and conspicuously

disclosed in writing to the Deputy Regional Director of OTS as part of the overall compensation/incentive plan with other appropriate information in seeking approval for new officer appointments.

15. D&N shall not retain the services of any person, corporation, partnership or other entity as a consultant whose services has not been retained prior to the date of this Order without the prior written approval of the Deputy Regional Director of the OTS. This paragraph shall not be deemed to require prior written approval for the retention of legal counsel or the retention of an investment banking firm to assist in compliance with Paragraph 1 of this Order.

HOLDING COMPANY EXPENSES

16. D&N shall not violate Sections 23A and 23B of the Federal Reserve Act, as made applicable to savings associations by Section 11 of the Home Owners' Loan Act as amended by Section 301 of FIRREA. Any payment of the expenses of D&N Financial Corporation or any successor company by D&N shall be documented in the minutes of the Board of Directors of D&N and said documentation shall include a consideration of compliance with the aforementioned statutes.

INVESTMENT PORTFOLIO/RESTRUCTURING

17. Within sixty (60) days of the effective date of this Order, D&N shall submit a plan, for approval by the Deputy Regional Director of the OTS, for restructuring the D&N portfolio of investment securities. Such plan must document strategies to: (a) reduce interest rate risk exposure; (b) increase core income; (c) decrease operating expenses; and (d) improve capital to an acceptable level. Such plan shall incorporate specific strategies to deal

with: (a) residuals; (b) IO's; (c) PO's; (d) other derivative products as defined in OTS Thrift Bulletin 13; and (e) interest rate risk exchange agreements. Should D&N elect to retain interest rate exchange agreements and/or derivatives as hedging instruments, the Board shall require that monthly reports be submitted to it monitoring the effectiveness of the hedges (using both market value and net interest income correlation) and to monitor how the actual performance of the derivatives and/or interest rate exchange agreements compares to the projections and hedged assets. Copies of such reports shall be submitted to the Deputy Regional Director of the OTS within seven (7) days of their submission to the Board.

18. Within thirty (30) days of the effective date of this Order, D&N shall dispose of its investment in all debt warrants it owns which are unauthorized investments pursuant to 12 C.F.R. Section 563.175(c)(1990).

19. Within thirty (30) days of the effective date of this Order, D&N's Board shall retain an external consultant to:

(a) analyze all derivative securities and recommend strategies for disposal of those securities which are considered inappropriate for the long term needs of D&N.

(b) analyze all interest rate exchange agreements and advise the Board as to an appropriate long-term strategy concerning these contracts.

(c) review and validate the current MVPE model and its assumptions developed by D&N. The consultant shall be requested to make suggestions or recommendations as appropriate.

The consultant's reports and recommendations shall be presented to the Board within thirty (30) days of the date of this Order. Copies of the consultant's report shall immediately be sent to the Deputy Regional Director of the OTS and the Regional Director of the FDIC. The consultant will provide all necessary documentation to support the conclusions and recommendations.

20. Within sixty (60) days of the date of this Order, D&N shall prepare and submit a plan, for approval by the Deputy Regional Director of the OTS, to improve the institution's liquidity and reduce its dependence on volatile liabilities. Volatile liabilities include, but are not limited to, funds obtained through: (a) short term borrowings; (b) reverse repurchase agreements; (c) dollar rolls; (d) brokered deposits; or (e) certificates of deposit in amounts of over \$90,000.

21. D&N shall immediately cease and desist from purchasing any high risk mortgage derivative securities, as described in OTS Thrift Bulletin #TB-12.

22. Should D&N elect to retain hedges and/or derivatives, the Board shall require that monthly reports be submitted to it monitoring the effectiveness of the hedges (using both market value and net interest income correlation) and to monitor how the actual performance of the derivative compares to the projections. Copies of such reports shall be submitted to the Deputy Regional Director of the OTS within seven (7) days of their submission to the Board.

23. D&N shall immediately account for its "short swaps" on a mark to market basis. A written report of the Board's decisions on this matter shall be submitted to the Deputy Regional Director of the OTS within seven (7) days of such determinations.

24. Within sixty (60) days of the date of this Order, the Board shall adopt an amended Interest Rate Risk Policy for approval by the Deputy Regional Director of the OTS. The amended policy must, at minimum address the deficiencies outlined in the OTS Report of the October 15, 1990 Examination at Page 41.

POLICIES

25. D&N's Board shall immediately proceed to revise policies for conflict

of interests, lending, interest-rate-risk management, deposit pricing, and secondary market activities, appraisal practices, single-family construction lending, and classification of assets, and within ninety (90) days of the date of this Order shall submit said policies to the Deputy Regional Director of the OTS for approval. The revised policies shall address all suggested corrections and relevant deficiencies identified in the Report of the October 15, 1990 OTS Examination. D&N shall comply with all policies and procedures amended or adopted pursuant to this Order except as otherwise may be required by law as supported by a legal opinion acceptable to the Deputy Regional Director of OTS from counsel for D&N. Changes in such policies require the prior written approval of the Deputy Regional Director of OTS.

ASSET QUALITY

26. Within the earlier of thirty (30) days of the hiring of a new chief lending officer or sixty (60) days from the date of this Order, D&N, through its Board, shall develop and submit a plan to reduce the level of classified assets, for approval by the Deputy Regional Director of the OTS.

27. D&N shall immediately write off all losses identified in the OTS Report of the October 15, 1990 Examination. All future losses must be written off immediately when they are identified through internal review processes or OTS determined classification.

28. D&N, through its Board, shall review the adequacy of valuation allowances quarterly, and shall increase the level of valuation allowances as they or the OTS determine to be appropriate. Copies of the Board's deliberations on the adequacy of valuation allowances shall be submitted to the OTS quarterly within seven (7) days of the ratification of the minutes of the first Board of Directors meeting immediately following the close of each

quarter.

29. D&N shall immediately establish general valuation allowances at least equal to \$12,500,000.00 and shall not allow general valuation allowances to fall below that level without the prior written approval of the Deputy Regional Director of the OTS.

30. D&N shall not accept applications for commercial non-real estate loans.

31. D&N shall not accept applications for loans on the security of income producing properties; provided, however, that with the prior written approval of the Board of Directors, D&N may accept purchase money notes up to \$2.5 million per loan to finance the sale of real estate owned by reason of foreclosure or deed in lieu of foreclosure. D&N shall apply to the Deputy Regional Director of the OTS for approval to make purchase money loans to finance the sale of real estate owned in amounts at or in excess of \$2.5 million.

32. D&N shall limit renewals, modifications, or refinancings of existing loans secured by income producing real estate to an aggregate amount of \$8 million per calendar year; provided that D&N shall not advance any new funds in connection with such renewal, modification, or refinancing without the prior written approval of the Deputy Regional Director. This number may be reduced or increased upon written notice to D&N in the discretion of the Deputy Regional Director of OTS.

33. Within thirty (30) days of the date of this Order, the Board shall prepare and submit to the Deputy Regional Director of the OTS and the Regional Director of the FDIC a report listing loans and real estate owned secured by or consisting of Hotel/Motel properties and mini-warehouse properties. This report shall identify, as applicable, the loan number,

balance, contractual status, internal classification status, and maturity date. Within thirty (30) days of the end of each calendar quarter, this report shall be updated and the update submitted to the Deputy Regional Director of the OTS and the Regional Director of the FDIC.

34. Within seven (7) days following review of its internal loan classification report by the Board of Directors at the first meeting following the end of each calendar quarter, D&N shall submit such report to the Deputy Regional Director of the OTS. This report shall specifically explain any upgrade in individual classifications from the previous quarter or the classifications reported in the OTS Report of the October 15, 1990 Examination.

35. Within thirty (30) days of the date hereof, D&N, through its Board, shall adopt a revised asset classification policy for approval by the Deputy Regional Director of the OTS. The revised policy shall include, but need not be limited to, the following:

(a) Guidelines for the calculation of general valuation allowances.

(b) Specific classification guidelines for: residential loans, real estate owned, other repossessed property, investments in subsidiaries, letters of credit, accrued interest receivable, and contingent liabilities. Furthermore, the guidelines for the classification of consumer loans should be included within the policy. Currently, the criteria is included within the consumer lending policy.

(c) Appropriate guidance regarding the use of net realizable value (NRV) and fair value (FV) calculations. Furthermore, the policy shall state the circumstances in which losses above what is minimally required shall be established. The Policy shall require documentation (for each loan reviewed) that FASB 5 and 15 have been reviewed for in-substance foreclosure considerations.

36. The Board shall direct management to immediately treat the following loans as in-substance foreclosures.

<u>Net Loan Borrower</u>	<u>Reference Balance *</u>	<u>OTS Exam Report Page</u>
VMS Realty	\$11,526,392	A - 12.18
Ramada zero coupon bond	7,200,000	A - 12.3
JMR/Walton Boulevard	2,984,431	A - 12.21
Jackson Properties	1,699,474	A - 12.25
Brunswick Apartments	1,236,750	A - 12.12
Hayes Associates	775,000	A - 12.14
P & S Hospital	<u>659,084</u>	A - 12.15
Total (7)	\$26,081,131	

* Net of existing specific valuation allowances and any additional losses identified by the examiner.

37. Within thirty (30) days of the date of this Order, D&N, through its Board, shall re-assess the role of the Chief Review Appraiser, and present a written report of its findings and proposed actions to the Deputy Regional Director of the OTS. In that report, the Board shall document its conclusions relative to:

(a) utilizing an independent, qualified fee appraiser for the review of appraisals on major assets; or

(b) hiring a staff appraiser, to be located in the Troy office, who has sufficient experience in analyzing the types of properties in which the D&N's commercial loans are concentrated.

CAPITAL DISTRIBUTIONS

38. D&N shall not declare, or pay any capital distributions of any type without the prior written approval of the Deputy Regional Director of the OTS.

BRANCH/DEPOSIT SALES

39. D&N shall not enter into any legally binding agreement to sell any of its branches or deposits except an agreement subject to written approval of

the Deputy Regional Director of the OTS.

SUBSIDIARIES

40. The Board shall ensure that each service corporation is adequately capitalized at a level which is sufficient to assure continued operations independent of the parent.

41. D&N shall take the steps described in the October 15, 1990 Examination to maintain the separate corporate identity of D&N Mortgage Corporation and D&N's other subsidiaries.

REPORTING

42. D&N shall, upon the request of the Deputy Regional Director of the OTS, furnish written progress reports to the Deputy Regional Director of the OTS or the Regional Director of the FDIC detailing the form and manner of any action taken to secure compliance with this Order and the results thereof. All progress reports and other written responses to this Order shall be reviewed by D&N's Board and made a part of the minutes of the Board meeting.

43. The Board of Directors shall, at each regular meeting, formally resolve that, to the best of its knowledge and belief, and based on a prudent review of management reports, during the previous calendar month the Savings Association and its subsidiaries complied with each condition of this Order except as otherwise stated. The resolution shall specify in detail how, if at all, full compliance was found not to exist. The resolution further shall set forth any exceptions to any conditions of this Order approved by the Deputy Regional Director. Within seven (7) days of ratification by the Board of the minutes of each prior regular Board of Directors meeting, the Savings Association shall submit to the Deputy Regional Director a copy of the minutes

of each Board of Directors meeting (and minutes of any committee or subsidiary board of directors meeting), the aforementioned resolution, and the management report(s) of the Savings Association. The provided materials shall include all schedules and information provided to the Board for its review and any attachments to the minutes; provided, however, that nothing in this Order shall be construed as requiring D&N to provide to the OTS materials which are subject to attorney-client privilege. Each director shall at such time either provide the Deputy Regional Director with certification that, to the best of his or her knowledge and belief, and based upon a prudent review, the above-referenced resolution is accurate, or provide the Deputy Regional Director with a written statement providing in detail the reason(s) for disagreement with the resolution.

DEFINITIONS

44. As used in this Order, the term "savings association" shall have the meaning as set forth in Section 2(4) of the Home Owners' Loan Act, as amended ("HOLA").

45. As used in this Order, the term "Deputy Regional Director" shall mean the Deputy Regional Director of the Indianapolis Office of the Central Region of OTS or any other official designated to perform the function by the Regional Director of OTS for the Central Region or by the Director of OTS or its successor

46. As used in this Order, the term "Board of Directors" or "Board" shall mean the Board of Directors of D&N Bank, A Federal Savings Bank

47. Reference in this Order to provisions of statutes, regulations, and OTS memoranda shall be deemed to include references to successor provisions as applicable.

48. All technical words or terms used in this Order, for which meanings are not specified or otherwise provided by the provisions of this Order, shall, insofar as applicable, have meanings as defined in Chapter V of Title 12 of the Code of Federal Regulations ("C.F.R."), HOLA, and Federal Deposit Insurance Corporation Act, as amended ("FDIC Act"). Any such technical words or terms used in this Order and undefined in said C.F.R., HOLA, FDIC Act, or OTS memoranda shall have meanings that are in accordance with the best custom and usage in the savings and loan industry.

49. The terms and provisions of this Order shall be binding upon and inure to the benefit of the parties hereto and their successors in interest.

50. Materials required to be sent to the OTS pursuant to this Order shall be mailed to: Deputy Regional Director, Office of Thrift Supervision, 8250 Woodfield Crossing Boulevard, Suite 305, Indianapolis, Indiana 46240.

NO WAIVER PROVISIONS

51. This Order does not preclude the OTS from pursuing enforcement actions, including, but not limited to, removal and prohibition orders, civil money penalties, or personal cease and desist orders against any individuals.

52. This Order does not preclude the OTS from pursuing enforcement actions, including, but not limited to, cease and desist orders and civil money penalties against D&N for violation of the Truth in Lending Act.

OFFICE OF THRIFT SUPERVISION

BY

/S/

~~Stuart M. Brauman~~
Regional Director
Central Region