

SUPERVISORY AGREEMENT

This Supervisory Agreement (Agreement) is made this 21st day of June, 2010 by and through the Board of Directors (Board) of Sterling Federal Bank, F.S.B., Sterling, Illinois, OTS Docket No. 00073 (Association) and the Office of Thrift Supervision (OTS), acting by and through its Regional Director for the Central Region (Regional Director);

WHEREAS, the OTS, pursuant to 12 U.S.C. § 1818, has the statutory authority to enter into and enforce supervisory agreements to ensure the establishment and maintenance of appropriate safeguards in the operation of the entities it regulates; and

WHEREAS, the Association is subject to examination, regulation and supervision by the OTS; and

WHEREAS, based on its examination of the Association, the OTS finds that the Association has engaged in unsafe or unsound practices and/or violations of law or regulation; and

WHEREAS, in furtherance of their common goal to ensure that the Association addresses the unsafe or unsound practices and/or violations of law or regulation identified by the OTS in the October 27, 2009 Report of Examination (2009 ROE), the Association and the OTS have mutually agreed to enter into this Agreement.

WHEREAS, on June 21, 2010, the Association's Board, at a duly constituted meeting, adopted a resolution (Board Resolution) that authorizes the Association to enter into this Agreement and directs compliance by the Association and its directors, officers, employees, and other institution-affiliated parties with each and every provision of this Agreement.

NOW THEREFORE, in consideration of the above premises, it is agreed as follows:

Business Plan.

1. By July 30, 2010, the Association shall submit to the Regional Director an updated business plan for the period beginning July 1, 2010 through December 31, 2012 (Business Plan) that is acceptable to the Regional Director and addresses all corrective actions set forth in the 2009 ROE. At a minimum, the Business Plan shall conform to applicable laws, regulations, and regulatory guidance and include:

- (a) establishment of a minimum Tier 1 (Core) Capital Ratio and Total Risk-Based Capital Ratio commensurate with the Association's risk profile;
- (b) detailed capital preservation and enhancement strategies with date specific narrative goals;
- (c) operating strategies to achieve increased core deposits and realistic core earnings throughout the term of the Business Plan;
- (d) detailed quarterly financial projections (balance sheet, income statement, and statement of cash flows), including Tier 1 (Core) and Total Risk-Based Capital Ratios, for the period beginning July 1, 2010 and ending December 31, 2012; and
- (e) detailed assumptions used for all financial projections such as:
the assumed interest rate scenarios; assumptions used for noninterest income and noninterest expense; assumptions used to determine disposition of real estate owned (REO); assumptions used to determine the allowance for loan and lease losses (ALLL); assumptions for loan origination rates, using recent experience and taking into consideration current national and regional economic conditions; and assumptions supporting the cost of funds projections.

2. Upon receipt of written notification from the Regional Director that the Business Plan is acceptable, the Association shall implement and adhere to the Business Plan. A copy of the Business Plan shall be provided to the Regional Director within five (5) days after Board approval.

3. Any proposed material deviations¹ from or changes to the Business Plan shall be submitted for the prior, written non-objection of the Regional Director. Requests for any material deviations or changes must be submitted at least sixty (60) days before a proposed change is implemented.

4. By September 30, 2011, and each September 30th thereafter, while this Agreement is effective, the Business Plan shall be updated and submitted to the Regional Director pursuant to Paragraphs 1 through 3 above incorporating the Association's budget plan and profit projections for the next two (2) fiscal years taking into account any revisions to the Association's loan, investment and operating policies.

5. Within forty-five (45) days after the close of each quarter, beginning with the quarter ending September 30, 2010, the Board shall review written quarterly variance reports on the Association's compliance with its Business Plan (Variance Reports). The Board's review of Variance Reports and compliance with the Business Plan shall include the internal and external risks affecting the Association's ability to successfully implement the Business Plan. The minutes of the Board meeting shall fully document the Board's review and discussion. The Variance Reports shall:

¹ A deviation shall be considered material under this Paragraph when the Association: (a) engages in any activity, line of business, or operation that is inconsistent with the Business Plan; (b) exceeds the level of any activity or growth contemplated in the Business Plan by more than ten percent (10%); or (c) falls below or fails to meet the target amounts established in the Business Plan by more than ten percent (10%).

- (a) identify variances in the Association's actual performance during the preceding quarter as compared to the projections set forth in the Business Plan;
 - (b) contain an analysis and explanation of identified variances; and
 - (c) discuss the specific measures taken or to be taken by the Association to address identified variances.
6. A copy of each Variance Report shall be provided to the Regional Director within five (5) days after Board review.

Concentrations of Private Label Residential Mortgage-Backed Securities.

7. Within thirty (30) days, the Association shall revise its concentration limit for private label residential mortgage-backed securities (PLMBS) to ensure that the limit addresses the corrective action in the 2009 ROE relating to concentration of PLMBS.
8. Effective immediately, the Association shall perform stress testing of the PLMBS in its available-for-sale (AFS) portfolio on at least a quarterly basis in order to determine how potential negative changes in the performance of the underlying mortgage collateral could impact future cash flows of the PLMBS. The Association's stress testing shall analyze separately the subset of PLMBS collateralized by Alt-A mortgage loans and include a review of the quarterly analysis prepared by the issuer of the PLMBS.
9. Within forty-five (45) days after the end of each quarter, beginning with the quarter ending June 30, 2010, the Association shall submit to the Board and the Regional Director a status report on its PLMBS, both in the AFS portfolio and the held-to-maturity (HTM) portfolio (PLMBS Status Report). The PLMBS Status Report shall include:

- (a) a breakdown of the PLMBS by nationally recognized statistical rating organization (NRSRO) rating (current quarter and previous quarter);
- (b) book value and market value at the end of the quarter;
- (c) number and dollar amount of PLMBS classified at the end of the quarter;
- (d) amount of other-than-temporary-impairment charges made during the quarter;
- (e) amount of loss provisions established during the quarter for the PLMBS portfolio broken down by AFS and HTM portfolio; and
- (f) data pertaining to any sales of PLMBS during the quarter (including gains and/or losses).

Commercial Lending Policy.

10. Effective immediately, the Association shall not originate, participate in, or acquire commercial loans, secured and unsecured, until such time as the Association has complied with all requirements of Paragraph 12 below and received written notification of acceptance by the Regional Director pursuant to Paragraph 13 below.

11. The Association may fund commercial loans-in-process and legally binding loan commitments outstanding as of the Effective Date of this Agreement and shall submit a list of such obligations and commitments to the Regional Director within thirty (30) days of the Effective Date of this Agreement.

12. Within sixty (60) days, the Association shall revise its commercial loan policies, procedures, practices, and controls (Commercial Loan Policy) to ensure that the Commercial Loan Policy addresses all corrective actions in the 2009 ROE relating to commercial lending.

The Commercial Loan Policy shall comply with applicable laws, regulations and regulatory

guidance.

13. Within sixty (60) days, the Association shall submit its Commercial Loan Policy to the Regional Director for review and comment. Upon receipt of written notification from the Regional Director that the Commercial Loan Policy is acceptable, the Association shall implement and adhere to the Commercial Loan Policy. The Board's review of the Commercial Loan Policy shall be documented in the Board meeting minutes. A copy of the Commercial Loan Policy shall be provided to the Regional Director within five (5) days of adoption by the Board.

Allowance for Loan and Lease Losses.

14. Within forty-five (45) days, the Association shall revise its policies, procedures, and methodology relating to the timely establishment and maintenance of an adequate allowance for loan and lease losses (ALLL) level (ALLL Policy) to ensure that the ALLL Policy addresses all corrective actions set forth in the 2009 ROE relating to ALLL. The ALLL Policy shall comply with applicable laws, regulations, and regulatory guidance.

Appointment of Chief Financial Officer.

15. Within thirty (30) days, the Board shall approve and submit to the Regional Director written job descriptions, including qualifications, of the proposed duties and responsibilities of a Chief Financial Officer (CFO) for the Association. Qualifications for the CFO position shall include, at a minimum, experience in directing the accounting policies, procedures, and internal controls of a bank of comparable size, effectively managing the relationship with external auditors, and preparing annual business plans in accordance with sound banking practices.

16. Within thirty (30) days of receipt of any comments from the Regional Director, the Board shall revise the written job descriptions and qualifications based on such comments and

implement recruitment plans to identify qualified candidates for the CFO position.

17. Within one hundred twenty (120) days, the Board shall select a qualified CFO who shall be subject to the prior written non-objection of the Regional Director in accordance with Paragraph 25 below. The CFO selected by the Board shall be vested with sufficient executive authority to fulfill the duties and responsibilities of the job position and shall have an appropriate work history of responsibility for the position. The submission to the Regional Director required by Paragraph 25 below with respect to the proposed CFO shall include a written statement of the Board's reasons for selecting the proposed individual for the position.

Management and Director Compensation.

18. Within thirty (30) days, the Board shall designate a committee to monitor and coordinate the Association's compliance with Paragraph 19 below and the completion of all corrective actions required in the 2009 ROE relating to compensation practices at the Association (Oversight Committee). The Oversight Committee shall be comprised of two (2) or more directors, all of whom shall be independent² directors.

19. Within ninety (90) days, the Oversight Committee appointed pursuant to Paragraph 18 above shall develop a written, comprehensive director and executive compensation policy that complies with 12 C.F.R. §§ 563.39 and 563.161(b), and 12 C.F.R. Part 570 – Appendix A

² For purposes of this Agreement, an individual who is "independent" with respect to the Association shall be any individual who:

- (a) is not employed in any capacity by the Association or its subsidiaries, other than as a director;
- (b) is not related by blood or marriage to any officer or director of the Association or any of its subsidiaries, and who does not otherwise share a common financial interest with any such officer, director or shareholder;
- (c) is not indebted, directly or indirectly, to the Association or any of its subsidiaries, including the indebtedness of any entity in which the individual has a substantial financial interest; and
- (d) has not served as a consultant, advisor, underwriter, or legal counsel to the Association or any of its subsidiaries.

(Compensation Policy). For the purposes of Paragraphs 18 and 19, “compensation” refers to any and all salaries, bonuses, incentive compensation, deferred compensation, pension benefits, health or welfare plan benefits, post-termination benefits, and director fees. In addition to defining appropriate levels of director fees and executive compensation, the Compensation Policy shall, at a minimum, consider the following:

- (a) the combined value of all cash and non-cash benefits provided to each Senior Executive Officer³ and each Director;
- (b) a comparison of each Senior Executive Officer’s total compensation with the compensation received by officers with similar responsibilities in similar financial institutions based upon such factors as asset size, geographic location, and the complexity of the loan portfolio or other assets;
- (c) the financial condition of the Association;
- (d) a requirement that all incentive compensation incorporate measurable qualitative and profitability performance standards for the Association’s Directors and Senior Executive Officers; and
- (e) whether present Senior Executive Officers are capable of implementing the Board’s directives and policies, operating within the constraints of laws and regulations, and operating the Association in a prudent manner.

20. Within ninety (90) days, the Oversight Committee shall submit its Compensation Policy to the Regional Director for review and comment. Upon receipt of written notification from the Regional Director that the Compensation Policy is acceptable, the Association shall implement and adhere to the Compensation Policy. The Board’s review of the Compensation Policy shall

³ The term “Senior Executive Officer” is defined at 12 C.F.R. § 563.555.

be documented in the Board meeting minutes. A copy of the final Compensation Policy shall be provided to the Regional Director within five (5) days after approval by the Board.

Flood Insurance.

21. Within sixty (60) days, the Association shall revise its policies, procedures and systems related to flood insurance (Flood Program) to ensure that the Flood Program addresses all corrective actions set forth in the 2009 ROE relating to flood insurance and complies with all applicable laws, regulations and regulatory guidance, including the requirements of the National Flood Insurance Act of 1968 and the Flood Disaster Protection Act of 1973, as amended, 42 U.S.C. §§ 4001-4129, as implemented by Part 572 of the OTS Rules and Regulations, 12 C.F.R. Part 572.

22. Within thirty (30) days, the Association shall implement corrective actions to ensure that all loans that do not comply with the Association's Flood Program, including those loans noted in the 2009 ROE, comply with the Flood Laws and Regulations.

Growth.

23. Effective immediately, the Association shall not increase its total assets during any quarter in excess of an amount equal to net interest credited on deposit liabilities during the prior quarter without the prior written non-objection of the Regional Director. The growth restriction imposed by this Paragraph shall remain in effect until the Regional Director reviews and approves the Association's Business Plan as required under Paragraph 2 of this Agreement.

Severance and Golden Parachute Payments.

24. Effective immediately, the Association shall not make any golden parachute payment⁴ unless, with respect to each such payment, the Association has complied with the requirements

⁴ The term "golden parachute payment" is defined at 12 C.F.R. § 359.1(f).

of 12 C.F.R. Part 359.

Directorate and Management Changes.

25. Effective immediately, the Association shall comply with the prior notification requirements for changes in directors and Senior Executive Officers set forth in 12 C.F.R. Part 563, Subpart H.

Employment Contracts and Compensation Arrangements.

26. Effective immediately, the Association shall not enter into any new contractual arrangement or renew, extend, or revise any contractual arrangement relating to compensation or benefits for any Senior Executive Officer or director of the Association, unless it first provides the Regional Director with not less than thirty (30) days prior written notice of the proposed transaction. The notice to the Regional Director shall include a copy of the proposed employment contract or compensation arrangement or a detailed, written description of the compensation arrangement to be offered to such Senior Executive Officer or director, including all benefits and perquisites. The Board shall ensure that any contract, agreement, or arrangement submitted to the Regional Director fully complies with the requirements of 12 C.F.R. Part 359, 12 C.F.R. §§ 563.39 and 563.161(b), and 12 C.F.R. Part 570 – Appendix A.

Third Party Contracts.

27. Effective immediately, the Association shall not enter into any arrangement or contract with a third party service provider that is significant to the overall operation or financial condition of the Association⁵ or outside the Association's normal course of business unless, with respect to each such contract, the Association has: (a) provided the Regional Director with a

⁵ A contract will be considered significant to the overall operation or financial condition of the Association where the annual contract amount equals or exceeds two percent (2%) of the Association's total capital, where there is a foreign service provider, or where it involves information technology that is critical to the Association's daily operations without regard to the contract amount.

minimum of thirty (30) days prior written notice of such arrangement or contract and a written determination that the arrangement or contract complies with the standards and guidelines set forth in OTS Thrift Bulletin 82a; and (b) received written notice of non-objection from the Regional Director.

Effective Date.

28. This Agreement is effective on the Effective Date as shown on the first page.

Duration.

29. This Agreement shall remain in effect until terminated, modified or suspended, by written notice of such action by the Regional Director.

Time Calculations.

30. Calculation of time limitations for compliance with the terms of this Agreement run from the Effective Date and shall be based on calendar days, unless otherwise noted.

Submissions and Notices.

31. All submissions to the OTS that are required by or contemplated by the Agreement shall be submitted within the specified timeframes.

32. Except as otherwise provided herein, all submissions, requests, communications, consents or other documents relating to this Agreement shall be in writing and sent by first class U.S. mail (or by reputable overnight carrier, electronic facsimile transmission or hand delivery by messenger) addressed as follows:

(a) **To: the OTS**

Regional Director
Office of Thrift Supervision
One South Wacker Drive, Suite 2000
Chicago, Illinois 60606
Facsimile: (312) 917-5001

(b) **To: the Association**

Chairman of the Board
Sterling Federal Bank, F.S.B.
110 East 4th Street
Sterling, Illinois 61081
Facsimile: (815) 626-6921

No Violations Authorized.

33. Nothing in this Agreement shall be construed as allowing the Association, its Board, officers or employees to violate any law, rule, or regulation.

OTS Authority Not Affected.

34. Nothing in this Agreement shall inhibit, estop, bar or otherwise prevent the OTS from taking any other action affecting the Association if at any time the OTS deems it appropriate to do so to fulfill the responsibilities placed upon the OTS by law.

Other Governmental Actions Not Affected.

35. The Association acknowledges and agrees that its execution of the Agreement is solely for the purpose of resolving the matters addressed herein, consistent with Paragraph 34 above, and does not otherwise release, discharge, compromise, settle, dismiss, resolve, or in any way affect any actions, charges against, or liability of the Association that arise pursuant to this action or otherwise, and that may be or have been brought by any governmental entity other than the OTS.

Miscellaneous.

36. The laws of the United States of America shall govern the construction and validity of this Agreement.

37. If any provision of this Agreement is ruled to be invalid, illegal, or unenforceable by the decision of any Court of competent jurisdiction, the validity, legality, and enforceability of the

remaining provisions hereof shall not in any way be affected or impaired thereby, unless the Regional Director in his or her sole discretion determines otherwise.

38. All references to the OTS in this Agreement shall also mean any of the OTS's predecessors, successors, and assigns.

39. The section and paragraph headings in this Agreement are for convenience only and shall not affect the interpretation of this Agreement.

40. The terms of this Agreement represent the final agreement of the parties with respect to the subject matters thereof, and constitute the sole agreement of the parties with respect to such subject matters.

Enforceability of Agreement.

41. This Agreement is a "written agreement" entered into with an agency within the meaning and for the purposes of 12 U.S.C. § 1818.

Signature of Directors/Board Resolution.

42. Each Director signing this Agreement attests that he or she voted in favor of a Board Resolution authorizing the consent of the Association to the issuance and execution of the Agreement. This Agreement may be executed in counterparts by the directors after approval of execution of the Agreement at a duly called board meeting. A copy of the Board Resolution authorizing execution of this Agreement shall be delivered to the OTS, along with the executed original(s) of this Agreement.

WHEREFORE, the OTS, acting by and through its Regional Director, and the Board of the Association, hereby execute this Agreement.

STERLING FEDERAL BANK, F.S.B.
Sterling, Illinois

OFFICE OF THRIFT SUPERVISION

_____/s/

John I. Schilling, Chairman

By: _____/s/

Daniel T. McKee
Regional Director, Central Region

_____/s/

Ronald D. Hoffman, Vice-Chairman

_____/s/

Curtis D. Dahlgren, Director

_____/s/

Catherine M. Paone, Director

_____/s/

David L. Schreiner, Director

_____/s/

Raymond P. Sharp, Director

_____/s/

Michael W. Shoger, Director

_____/s/

Rita E. Smith, Director

_____/s/

John C. Ybarra, Director