FEDERAL DEPOSIT INSURANCE CORPORATION

WASHINGTON, DC

In the Matter of **STATE BANK OF AURORA** **AURORA, MINNESOTA** **(Insured State Nonmember Bank)**	**)** **)** **)** **)** **)** **)** **)** **)**	**ORDER TO CEASE AND DESIST** **FDIC-09-026b**

State Bank of Aurora, Aurora, Minnesota (“Bank”), having been advised of its right to a NOTICE OF CHARGES AND OF HEARING detailing the unsafe or unsound banking practices alleged to have been committed by the Bank, and its right to a hearing on those charges under section 8(b) of the Federal Deposit Insurance Act (“Act”), 12 U.S.C. § 1818(b), and having waived those rights, entered into a STIPULATION AND CONSENT TO THE ISSUANCE OF AN ORDER TO CEASE AND DESIST (“CONSENT AGREEMENT”) dated March 18, 2009, with counsel for the Federal Deposit Insurance Corporation (“FDIC”), whereby, solely for the purpose of this proceeding and without admitting or denying any unsafe or unsound banking practices, the Bank consented to the issuance of the following ORDER TO CEASE AND DESIST (“ORDER”) by the FDIC.

The FDIC considered the matter and determined that it had reason to believe that the Bank had engaged in unsafe and unsound banking practices. The FDIC, therefore, accepted the CONSENT AGREEMENT and issued the following:

ORDER TO CEASE AND DESIST

IT IS HEREBY ORDERED, that the Bank, its institution-affiliated parties, as that term is defined in section 3(u) of the Act, 12 U.S.C. § 1813(u), and its successors and assigns, cease and desist from the following unsafe or unsound banking practices:

A. Operating with management whose policies and practices are detrimental to the Bank and jeopardize the safety of its deposits.

B. Operating with a board of directors that has failed to provide adequate supervision over and direction to the management of the Bank.

C. Operating with an inadequate level of capital protection for the kind and quality of assets held and/or appropriate to the risk inherent in the activities engaged in by the Bank.

D. Operating with an inadequate allowance for loans and lease losses for the volume, kind, and quality of loans and leases held, and failing to make provision for an adequate allowance for possible loan and lease losses.

E. Engaging in hazardous lending and lax collection practices, including, but not limited to:

1. the failure to obtain adequate collateral;

2. the extension of credit with inadequate diversification of risk;

3. the failure to properly underwrite and administer its loan portfolio; and

4. other poor credit administration practices.

F. Operating with an inadequate loan policy.

G. Operating with inadequate liquidity in light of the Bank's asset and liability mix.

H. Operating with an inadequate asset/liability and/or funds management policy.

I. Operating with inadequate earnings.

IT IS FURTHER ORDERED, that the Bank, its institution-affiliated parties, and its successors and assigns, take affirmative action as follows:

1. Qualified Management.

(a) From the effective date of this ORDER, the Bank shall have qualified management. Each member of management shall have the requisite knowledge, skills, ability and experience, giving consideration to the size and complexity of the Bank, to operate the Bank in a safe and sound manner and in compliance with applicable laws and regulations, as well as to restore the Bank to a satisfactory financial condition. Each member of management shall be provided appropriate written authority from the board of directors to implement the provisions of this ORDER.

(b) Immediately, and periodically during the life of this ORDER, but no less frequently than annually, the board of directors shall assess management on its ability to:

(i) comply with the requirements of this ORDER, all applicable State and Federal laws and regulations, FDIC and Federal Financial Institutions Examination Council policy statements, and the Bank’s approved policies and procedures; and

(ii) restore and thereafter maintain the Bank in a safe and sound condition, including, but not limited to, capital adequacy, asset quality, earnings, management effectiveness, liquidity, sensitivity to market risks, information technology, and Bank Secrecy Act/Anti-Money Laundering compliance.

2. Assessment of Qualified Management.

(a) Within 60 days from the effective date of this ORDER, the board of directors, or a committee appointed by the board, shall analyze and assess the Bank’s management and staffing performance and needs. The analysis and assessment shall be summarized in a written report (“Management Report”). At a minimum, the Management Report shall:

(i) Identify the type and number of officer positions needed to manage and supervise the affairs of the Bank, detailing any vacancies or additional needs and giving appropriate consideration to the size and complexity of the Bank and the Bank’s business/strategic plan required by this ORDER;

(ii) Identify the type and number of staff positions needed to carry out the Bank's business/strategic plan, detailing any vacancies or additional needs;

(iii) Present a clear and concise description of the relevant knowledge, skills, abilities, and experience necessary for each officer position, including delegations of authority and performance objectives;

(iv) Identify training and development needs;

(v) Identify and establish Bank committees needed to provide guidance and oversight to management; and

(vi) Evaluate the current and past performance of all existing Bank officers, indicating whether the individuals are competent and qualified to perform present and anticipated duties, adhere to the Bank's established policies and practices, and operate the Bank in a safe and sound manner.

(b) Within 10 days of completion of the Management Report, the board will provide a copy of the Management Report to the Regional Director of the FDIC's Kansas City Regional Office ("Regional Director") and the Deputy Commissioner for the Minnesota Department of Commerce (collectively, "Supervisory Authorities"), and will complete its review of the Management Report, which shall be recorded in the minutes of the meeting of the board of directors.

(c) Within 30 days of receipt of the Management Report, the board will develop a written Management Plan that incorporates the findings of the report, a plan of action in response to each recommendation contained in the Management Report, and a time frame for completing each action. A copy of the Management Plan and any subsequent modification thereto shall be immediately submitted to the Supervisory Authorities for review and comment. Within 30 days from receipt of any comment from the Regional Director, and after consideration of such comment, the board of directors shall approve the Management Plan which approval shall be recorded in the minutes of the meeting of the board. Thereafter, the Bank and its directors, officers and employees shall implement and follow the Management Plan and any modifications thereto. It shall remain the responsibility of the board to fully implement the plan within the specified time frames. In the event the plan, or any portion thereof, is not implemented, the board shall immediately advise the Supervisory Authorities, in writing, of specific reasons for deviating from the Management Plan. At a minimum, the Management Plan shall:

(i) Contain a recitation of the recommendations included in the Management Report;

(ii) Incorporate a plan to provide any necessary training and development for all employees;

(iii) Establish procedures to periodically review and update the Management Plan, as well as periodically review and assess the performance of each officer; and

(iv) Contain a current management succession plan.

(d) The Bank shall notify the Supervisory Authorities in writing of any resignations and/or terminations of any members of its board of directors and/or any of its officers within 15 days of the event. The Bank shall also establish procedures to ensure compliance with section 32 of the FDI Act, 12 U.S.C. § 1831i and Subpart F of Part 303 of the FDIC's Rules and Regulations, 12 C.F.R. §§ 303.100 through 303.103. In addition, the Bank shall notify the Supervisory Authorities in writing when it proposes to add any individual to the Bank's board of directors or employ any individual as a senior executive officer. The notification must be received at least 30 days before such addition or employment is intended to become effective and should include a description of the background and experience of the individual(s) to be added or employed.

3. <u>Minimum Capital Requirements</u>.

(a) While this ORDER is in effect, the Bank shall have and maintain the following minimum capital levels (as defined in Part 325 of the FDIC's Rules and Regulations, 12 C.F.R. Part 325), after establishing an appropriate allowance for loan and lease losses:

(i) Tier 1 capital at least equal to eight (8.0) percent of total assets; and

(ii) total risk-based capital at least equal to Eleven (11.0) percent of risk-weighted assets ("capital ratios").

(b) If either capital ratio falls below the established minimum, within 30 days of such determination, the Bank shall submit a written plan to the Supervisory Authorities, describing the means and timing by which the Bank shall increase such ratio(s) up to or in excess of the established minimum(s). Within 30 days of receipt of any comment from the Regional Director, and after due consideration of any recommended changes, the board of directors shall approve the written plan, which approval shall be recorded in the board meeting minutes. Thereafter, the Bank shall implement and full comply with the written plan.

(c) For purposes of this ORDER, all terms relating to capital shall be calculated according to the methodology set forth in Part 325 of the FDIC's Rules and Regulations.

4. Restrictions on Dividends.

The Bank shall not declare or pay any cash dividend or capital distribution without the prior written approval of the Regional Director.

5. <u>Charge-off of Adversely Classified Assets</u>.

(a) Within 30 days of the effective date of this ORDER, the Bank shall eliminate from its books, by charge-off or collection, all assets or portions of assets classified "Loss" in the FDIC's October 27, 2008, Report of Examination ("Report of Examination") that have not been previously collected or charged off.

(b) Elimination or reduction of assets through the proceeds of other loans or extensions of credit made by the Bank is not considered collection for purposes of this ORDER.

6. <u>Reduction of Adversely Classified Loans</u>.

(a) Within 60 days of the effective date of this ORDER, the Bank shall develop a written plan to reduce the Bank's risk exposure in each loan in excess of $150,000 classified "Substandard" in the Report of Examination. For purposes of this ORDER, "reduce" means to collect, charge off, or improve the quality of a loan so as to warrant its removal from adverse classification by the Supervisory Authorities. In developing the plans required by this provision, the Bank shall, at a minimum, review, analyze, and document the financial position of the borrower, including source of repayment, repayment ability, and alternative repayment sources, as well as the value and accessibility of any pledged or assigned collateral, and any possible actions to improve the Bank's collateral position.

(b) The plans required by this provision shall also include, but not be limited to, the following:

(i) specific action plans intended to reduce the Bank’s risk exposure in each classified loan;

(ii) a requirement that monthly written progress reports be submitted to the board of directors; and

(iii) a requirement that the board of directors review the monthly progress reports and record a notation of the review in the minutes of the board.

(c) The board of directors shall approve the plans, and record the approval in the board meeting minutes. Thereafter, the Bank shall implement and fully comply with the plans.

7. Restrictions on Advances to Adversely Classified Borrowers.

(a) The Bank shall not extend, directly or indirectly, any additional credit to, or for the benefit of, any borrower who has a loan or other extension of credit or obligation with the Bank that has been, in whole or in part, charged off or classified "Substandard" in the Report of Examination and is uncollected. The Bank shall not be prohibited from renewing, after collecting in cash all interest and fees due from a borrower, any credit already extended to the borrower.

(b) The Bank shall not be prohibited from extending additional credit to any borrower if the Bank’s failure to extend further credit to a particular borrower would be detrimental to the best interests of the Bank. The Bank shall not extend further credit to any such borrower, whether in the form of a renewal, extension, or further advance of funds, unless additional credit shall have been approved in advance by the Bank’s board of directors, or a designated committee thereof, who, after thorough review, shall have concluded and fully documented in its minutes that:

(i) the failure to extend such credit would be detrimental to the best interests of the Bank, with an explanation of why it would be detrimental;

(ii) the extension of such credit would improve the Bank’s position, including an explanatory statement of how the Bank’s position would be improved; and

(iii) an appropriate workout plan has been developed and will be implemented in conjunction with the additional credit to be extended.

A copy of the board’s or committee’s conclusions and approval shall be retained in the borrower’s credit file and be made part of the board meeting minutes.

8. Concentrations of Credit.

(a) Within 60 days of the effective date of this ORDER, the Bank shall develop a written plan (“Concentration Plan”) intended to systematically reduce and monitor the Bank’s concentration in commercial real estate assets to an amount which is commensurate with the Bank's business strategy, management expertise, and financial condition. The Concentration Plan shall establish an appropriate concentration risk limit for the commercial real estate portfolio, as well as concentration risk limits for each segment of the portfolio with common risk characteristics or sensitivities to economic, financial, or business developments. Concentration risk limits will be expressed as a percentage of Total Capital.

(b) The board of directors shall review, on a monthly basis, the level and trend of concentrations, actual levels compared to levels targeted in the Concentration Plan, and reports that describe the state of and changes in commercial real estate market conditions in the geographic areas in which the Bank lends.

(c) Immediately after development, the Concentration Plan shall be submitted to the Supervisory Authorities for review and comment. Within 30 days of receipt of any comment from the Regional Director, and after consideration of any recommended changes, the board of directors shall approve the Concentration Plan, which approval shall be recorded in the minutes of the board. Thereafter, the Bank shall fully implement the Concentration Plan. The Concentration Plan shall be reviewed at least annually and amended as appropriate to manage the risk in the commercial real estate portfolio.

9. Implementation of Loan Policy.

Within 60 days from the effective date of this ORDER, the board of directors of the Bank shall review and revise the Bank’s written loan policies and procedures to address the comments and criticisms in the Report of Examination. The Bank’s revised loan policies and procedures shall be provided to the Supervisory Authorities for review and comment. Within 30 days of receipt of any comment from the Regional Director, and after consideration of any recommended changes the Bank shall approve the loan policies and procedures, which approval shall be recorded in the minutes of the board of directors meeting. Thereafter, the Bank shall implement and fully comply with the revised loan policies. In the event the Bank considers making a loan that would not conform with the Bank’s loan policies, the loan shall receive prior review and approval by the Bank’s board of directors. The reason for non-conformance and the board’s prior review and approval shall be documented in the board’s minutes and in the loan file for that loan.

10. Maintenance of Allowance for Loan and Lease Losses.

(a) Within 30 days from the date of this ORDER, the board of directors shall make a provision which will replenish the allowance for loan and lease losses (“allowance”) for the loans charged off as a result of the most recent examination and reflect the potential for further losses in the remaining loans or leases classified “Substandard” in the Report of Examination as well as all other loans and leases in its portfolio.

(b) Within 90 days from the effective date of this ORDER, the board shall establish a comprehensive policy and methodology for determining the appropriateness of the allowance. The policy shall provide for a review of the allowance at least once each calendar quarter in order that the results of the review conducted by the board may be properly reported in the quarterly Reports of Condition and Income. Such reviews shall, at a minimum, be made in accordance with the Federal Financial Institutions Examination Council’s Instructions for the Reports of Condition and Income, the Interagency Statement of Policy on the Allowance for Loan and Lease Losses, other applicable regulatory guidance that addresses the adequacy of the Bank’s allowance, and any analysis of the Bank’s allowance provided by the Supervisory Authorities;

(c) A deficiency in the allowance shall be remedied in the calendar quarter in which it is discovered by a charge to current operating earnings prior to any Tier 1 capital determinations required by this ORDER and prior to the Bank’s submission of its Report of Condition and Income. The board of directors shall thereafter maintain an adequate allowance.

(d) The Bank shall submit the policy to the Supervisory Authorities for review and comment. Within 30 days from receipt of any comment from the Regional Director, and after due consideration of any recommended changes, the Bank shall approve the policy, which approval shall be recorded in the minutes of the board of directors meeting. Thereafter, the Bank shall implement and fully comply with the policy.

11. <u>Formulation and Adoption of Business/Strategic Plan</u>.

(a) Within 60 days after the effective date of this ORDER, the Bank shall formulate and adopt a comprehensive business/strategic plan covering at least an operating period of three years. The plan required by this paragraph shall contain:

(i) an assessment of the Bank's current financial condition;

(ii) a description and assessment of the Bank's market area and a discussion of the economic forecast pertaining to the market area;

(iii) a description of the Bank's business strategy, including the specific products and services that will be offered, the markets from which customers will be solicited, and details regarding the use of any third-parties to offer products or services or generate loans or deposits;

(iv) financial goals for asset growth, capital adequacy, and earnings; and

(v) pro forma financial statements for the next three years.

(b) The Bank shall submit the business/strategic plan to the Supervisory Authorities for review and comment. Within 30 days of receipt of all such comments from the Regional Director and after consideration of any recommended changes, the Bank shall approve the plan, which approval shall be recorded in the minutes of the meeting of the board of directors. The Bank shall thereafter implement and follow the plan.

12. <u>Profit and Budget Plan</u>.

(a) Within 60 days of the effective date of this ORDER, and within the first 30 days of each calendar year thereafter, the board of directors shall develop a written profit plan ("Profit Plan") consisting of goals and strategies, consistent with sound banking practices, and taking into account the Bank's other written plans, policies, or other actions required by this ORDER.

(b) The Profit Plan shall include, at a minimum:

(i) realistic and comprehensive budgets for all categories of income and expense items;

(ii) a description of the operating assumptions that form the basis for, and adequately support, material projected revenue and expense components;

(iii) coordination of the Bank's loan, investment, funds management, and operating policies; strategic plan, and allowance for loan and lease loss methodology with the profit and budget planning;

(iv) a budget review process to monitor the revenue and expenses of the Bank whereby actual performance is compared against budgetary projections not less than quarterly;

(v) recording the results of the budget review and any actions taken by the Bank as a result of the budget review in the minutes of the board of directors; and

(vi) the individual(s) responsible for implementing each of the goals and strategies of the Profit Plan.

(c) Immediately after development, the Profit Plan and any subsequent modification thereto shall be submitted to the Supervisory Authorities for review and comment. Within 30 days of receipt of any comment from the Regional Director, and after consideration of any recommended changes, the board of directors shall approve the Profit Plan, which approval shall be recorded in the minutes of the meeting of the board. Thereafter, the Bank shall fully implement the Profit Plan and any subsequently approved modification.

13. Contingency Funding Plan.

(a) Within 60 days from the effective date of this ORDER, the board of directors of the Bank shall develop a written contingency funding plan (“liquidity plan”). The liquidity plan shall be updated on a regular basis and should, at a minimum, help management to monitor liquidity risk, ensure that an appropriate amount of liquid assets is maintained, measure and project funding requirements during various scenarios, and manage access to funding sources. Specifically, the liquidity plan should address the tightening of access to, or the imposition of additional requirements on, established credit lines as a result of the deteriorating asset quality.

(b) The Bank shall submit the liquidity plan to the Supervisory Authorities for review and comment. Within 30 days of the receipt of any comments from the Regional Director, and after consideration of all such comments, the board shall approve the liquidity plan, which approval shall be recorded in the minutes of the meeting of the board of directors. Thereafter, the Bank shall implement and follow the liquidity plan.

14. Disclosure.

The Bank shall send, or otherwise furnish, to its shareholders a description of this ORDER (i) in conjunction with the Bank’s next shareholder communication, and (ii) in conjunction with its notice or proxy statement preceding the Bank’s next shareholder meeting. The description shall fully describe the ORDER in all material respects. The description and any accompanying communication, statement, or notice shall be sent to the FDIC, Division of Supervision and Consumer Protection, Accounting and Securities Disclosure Section, 550 17th Street, N.W., Room F-6066, Washington, D.C. 20429 for review at least 20 days prior to dissemination to shareholders. Any changes requested by the FDIC shall be made prior to dissemination of the description, communication, notice, or statement.

15. Program for Monitoring Bank's Compliance with Order.

Within 60 days of the effective date of this ORDER, the board of directors shall adopt and implement a program for monitoring the Bank's compliance with this ORDER.

16. Progress Reports.

After 90 days, but no later than 120 days from the effective date of this ORDER, the Bank shall furnish a written progress report to the Supervisory Authorities, detailing the form, manner, and results of any actions taken to secure compliance with this ORDER. Thereafter, the Bank shall furnish written progress reports upon request by the Supervisory Authorities. The written progress reports shall provide cumulative detail of the Bank's progress toward achieving compliance with each provision of the ORDER.

This ORDER shall be effective on the date of issuance.

The provisions of this ORDER shall be binding upon the Bank, its institution-affiliated parties, and any successors and assigns thereof. The provisions of this ORDER shall remain effective and enforceable except to the extent that, and until such time as, any provision has been modified, terminated, suspended, or set aside by the FDIC.

Issued Pursuant to Delegated Authority.

Dated: _March 19, 2009________________

By:

/s/________________________
Mark S. Moylan
Deputy Regional Director
Kansas City Regional Office