

**FEDERAL DEPOSIT INSURANCE CORPORATION  
WASHINGTON, D.C.  
and  
STATE OF MINNESOTA  
DEPARTMENT OF COMMERCE**

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	)	
<b>In the Matter of</b>	)	
	)	<b>CONSENT ORDER</b>
<b>PEOPLES STATE BANK OF</b>	)	
<b>MADISON LAKE</b>	)	<b>FDIC-11-185b</b>
<b>MADISON LAKE, MINNESOTA</b>	)	
	)	
<b>(Insured State Nonmember Bank)</b>	)	
_____	)	

The Federal Deposit Insurance Corporation ("FDIC") is the appropriate Federal banking agency for Peoples State Bank of Madison Lake, Madison Lake, Minnesota ("Bank"), under 12 U.S.C. § 1813(q). The State of Minnesota, Department of Commerce, is the appropriate State banking authority for the Bank under Minnesota Statutes §§ 46.01 - 46.04 (2010) (and collectively, with the FDIC, "Supervisory Authorities").

The Bank, by and through its duly elected and acting board of directors ("Board"), has executed a "Stipulation to the Issuance of a Consent Order" ("Stipulation"), dated June 7, 2011 that is accepted by the Supervisory Authorities. With the Stipulation, the Bank has consented, without admitting or denying any charges of unsafe or unsound banking practices to

the issuance of this Consent Order ("ORDER") by the Supervisory Authorities.

Having determined that the requirements for issuance of an order under 12 U.S.C. § 1818(b) and Minnesota state law have been satisfied, the Supervisory Authorities each hereby order that:

**1. Assessment of Management.**

(a) From the effective date of this ORDER, the Bank shall take action to have and maintain qualified management.

(b) Within 30 days from the effective date of this ORDER, the Board shall engage an independent third party ("Consultant") acceptable to the Supervisory Authorities, and that possesses appropriate expertise and qualifications to analyze and assess performance and needs of the Bank's management and staff.

(c) The Bank shall provide the Supervisory Authorities with a copy of the proposed engagement letter or contract with the Consultant for review before it is executed. The contract or engagement letter, at a minimum, shall include:

(i) a description of the work to be performed under the contract or engagement letter, the fees for each significant element of the engagement, and the aggregate fee;

(ii) the responsibilities of the Consultant;

(iii) an identification of the professional standards covering the work to be performed;

(iv) identification of the specific procedures to be used when carrying out the work to be performed;

(v) the qualifications of the Consultant's employee(s) who are to perform the work;

(vi) the time frame for completion of the work;

(vii) any restrictions on the use of the reported findings;

(viii) a provision for unrestricted examiner access to workpapers;

(ix) a certification that the Consultant and any employees are not affiliated in any manner with the Bank; and

(x) a requirement that the Consultant's analysis and assessment shall be summarized in a written report to the Board ("Consultant's Report") within 90 days of engagement.

(d) Within 30 days of receipt of the Consultant's Report, the Board will develop a written Management Plan that addresses the findings of the Consultant's Report, a plan of action in response to each recommendation contained in the Consultant's Report, and a time frame for completing each action. At a minimum, the Management Plan shall:

(i) contain a recitation of the recommendations included in the Consultant's Report or otherwise communicated to the Bank, along with a copy of any report(s) prepared by any other outside consultants;

(ii) 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;

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

(iv) identify the authorities, responsibilities, and accountabilities attributable to each position, as well as the appropriateness of the authorities, responsibilities, and accountabilities, giving due consideration to the relevant knowledge, skills, abilities, and experience of the incumbent (if any) and the existing or proposed compensation;

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

(vi) identify the appropriate level of current and deferred compensation to each officer and staff position;

(vii) evaluate the current and past performance of all existing Bank officers and staff, 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;

(viii) establish requirements and methodologies to periodically evaluate each individual's job performance;

(ix) identify and establish Bank committees needed to provide guidance and oversight to management;

(x) establish a plan to terminate, rotate, or reassign officers and staff as necessary, as well as recruit and retain qualified personnel consistent with the Board's analysis and assessment of the Bank's staffing needs;

(xi) identify training and development needs, and incorporate a plan to provide such training and development;

(xii) contain a current organizational chart that identifies all existing and proposed officer and staff positions, delineates related lines of authority and accountability, and establishes a written plan for addressing any identified needs;

(xiii) contain a current management succession plan;

(xiv) contain a procedure to ensure compliance with section 32 of the Act, 12 U.S.C. § 1831i, when applicable to changes/additions in directors and senior executive officers;  
and

(xv) establish procedures to annually review and update the Management Plan, as well as review and assess the performance of each officer and staff member.

(e) A copy of the Consultant's Report and the Management Plan and any subsequent modification thereto shall be submitted to the Supervisory Authorities, for review and comment. Within 30 days from receipt of any comment from the Supervisory Authorities and after consideration of all such comments, the Board shall approve the Management Plan which approval shall be recorded in the Board's minutes. 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.

**2. Charge-off of Adversely Classified Assets.**

(a) Within 10 days from the effective date of the ORDER, and within 10 days after the receipt of any future reports of examination of the Bank from either of the Supervisory Authorities, the Bank shall eliminate from its books, by charge-off or collection, all assets or portions of assets classified

"Loss" in the FDIC January 31, 2011, Report of Examination ("Report of Examination"), and in such future reports 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.

**3. Reduction of Adversely Classified Assets.**

(a) Within 60 days from the effective date of this ORDER and within 60 days after the receipt of any future reports of examination of the Bank from either of the Supervisory Authorities, the Bank shall formulate written plans to reduce the Bank's risk exposure in each asset in excess of \$100,000 adversely classified as "Substandard" or "Doubtful" in the Report of Examination or in such future reports of examination. For purposes of this provision, "reduce" means to collect, charge off, or improve the quality of an asset so as to warrant its removal from adverse classification by the Supervisory Authorities.

(b) In developing the plans mandated by this paragraph, the Bank shall, at a minimum, and with respect to each loan or lease, review, analyze, and document the financial position of the borrower, including sources of repayment and repayment

ability, as well as the value and accessibility of any pledged or assigned collateral, and any possible actions to improve the Bank's collateral position.

(c) The plans mandated by this provision shall include a requirement that monthly written progress reports be submitted by Bank management to the Board, and a requirement that the Board review the progress reports and record the review in the Board's minutes.

(d) The Board shall approve the plans, which approval shall be recorded in the Board's minutes. Thereafter, a copy of the plan or portion thereof that pertains to a specific borrower shall be maintained in the borrower's credit file, and the Bank shall implement and fully comply with the plan.

**4. Restrictions on Advances to Adversely Classified Borrowers.**

(a) While this ORDER is in effect, 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 adversely classified "Substandard" or "Doubtful," either internally or in the Report of Examination and is uncollected, or classified "Substandard" or "Doubtful" in any future reports of examination from either of the Supervisory Authorities and is uncollected. The requirements of this



paragraph shall not prohibit the Bank from renewing, after collecting in cash all interest and fees due from a borrower, any credit already extended to the borrower.

(b) Subparagraph (a) of this provision shall not apply if the Bank's failure to extend further credit to a particular borrower would be detrimental to the best interests of the Bank. Prior to extending additional credit pursuant to this subparagraph (b), whether in the form of a renewal, extension, or further advance of funds, such additional credit shall be approved by the Board, who shall conclude that:

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

(ii) the extension of such credit would improve the Bank's position, with an explanatory statement of why the Bank's position would improve; and

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

(c) The conclusions and approval shall be made a part of minutes of the Board, with a copy retained in the borrower's credit file.

**5. Loan Policy, Underwriting, and Credit Administration.**

(a) Within 90 days of the effective date of this ORDER, the Board shall review and revise its written loan policy and credit administration procedures ("Revised Loan Policies") to address the loan policy, underwriting, and credit administration deficiencies and recommendations presented on the Examination Conclusions and Comments pages of the Report of Examination.

(b) The Bank shall approve the Revised Loan Policies, which approval shall be recorded in the Board's minutes. Thereafter, the Bank shall implement and fully comply with the Revised Loan Policies. The Bank shall provide a copy of the Revised Loan Policies to the Supervisory Authorities with the first progress report required by this ORDER.

(c) In the event the Bank considers making a loan that would not conform with the Bank's Revised Loan Policies, the loan shall receive prior review and approval by the Board. The reason for nonconformance and the Board's review and approval shall be documented in the minutes of the Board or committee and in the loan file for that loan.

**6. Implementation of Loan Review Program.**

(a) Within 60 days of the effective date of this ORDER, the Board shall develop a written program of independent loan review that will provide for a periodic review of the Bank's

loan portfolio and the identification and categorization of problem credits. At a minimum, the written program shall provide for:

(i) prompt identification of loans with credit weaknesses that warrant the special attention of management, including the name of the borrower, amount of the loan, reason why the loan warrants special attention, and assessment of the degree of risk that the loan will not be fully repaid according to its terms;

(ii) prompt identification of all outstanding balances and commitments attributable to each obligor identified under the requirements of subparagraph (i), including outstanding balances and commitments attributable to related interests of such obligors, including the obligor of record, relationship to the primary obligor identified under subparagraph (i), and an assessment of the risk exposure from the aggregate relationship;

(iii) identification of trends affecting the quality of the loan portfolio and potential problem areas;

(iv) assessment of the overall quality of the loan portfolio;

(v) identification of credit and collateral documentation exceptions;

(vi) identification and status of violations of laws, rules, or regulations with respect to the lending function;

(vii) identification of loans that are not in conformance with the Bank's lending policy or any of the requirements of this ORDER;

(viii) identification of loans to directors, officers, principal shareholders, and their related interests; and

(ix) periodic written reports, but in no event less than quarterly, providing the information developed in (i) through (viii) above to the Board. The reports should also describe the action(s) taken by management with respect to problem credits.

(b) The Board shall approve the written program, which approval shall be recorded in the Board's minutes. Thereafter, the Bank shall implement and fully comply with the written program. A copy of the written program shall be provided to the Supervisory Authorities with the first progress report required by this ORDER.

(c) Upon implementation, a copy of each report submitted to the Board, as well as documentation of the actions taken by the Bank or recommendations to the Board that address identified deficiencies in specific loan relationships or the Bank's policies, procedures, strategies, or other elements of the Bank's lending activities, as well as any resulting determinations, shall be recorded and retained in the Board's minutes.

7. **Allowance for Loan and Lease Losses (ALLL).**

(a) Within 30 days, the Board shall revise Bank's written policy and methodology for determining the ALLL to address the comments and criticisms in the Report of Examination, and shall amend the Bank's December 31, 2010 Call Report to reflect an appropriate ALLL as described in the Report of Examination. The written policy shall provide for a review of the ALLL at least once each calendar quarter in order that the findings of the Board may be properly reported in the Bank's Call Reports. Such reviews shall, at a minimum, be made in accordance with the Call Report Instructions, the Interagency Statement of Policy on the Allowance for Loan and Lease Losses, other applicable regulatory guidance that addresses the appropriateness of the Bank's ALLL, and any analysis of the Bank's ALLL provided by either of the Supervisory Authorities.

(b) A deficiency in the Bank's ALLL 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 Call Report. The Board shall thereafter maintain an appropriate ALLL and fully comply with the policy.

**8. Minimum Capital Requirements.**

(a) While this ORDER is in effect, the Bank shall have and maintain the following minimum capital ratios (as defined in Part 325 of the FDIC's Rules and Regulations), after establishing an appropriate ALLL:

(i) Tier 1 "leverage capital ratio" at least equal to 8.0 percent;

(ii) "Total risk-based capital ratio" at least equal to 11.0 percent.

(b) In the event any ratio is or becomes less than the minimum required by subparagraph (a) of this provision, the Bank shall immediately notify the Supervisory Authorities and within 30 days shall: (1) increase capital in an amount sufficient to comply with subparagraph (a), or (2) submit a written plan to the Supervisory Authorities for review and comment, describing in detail the primary means and timing by which the Bank shall increase its capital ratios up to or in excess of the minimum requirements of subparagraph (a) above, as well as a contingency plan in the event the primary sources of capital are not available. Within 30 days of receipt of any such comments from the Supervisory Authorities, and after consideration of all such comments, the Board shall approve the written plan, which approval shall be recorded in the Board's minutes. Thereafter, the Bank shall implement and fully comply with the written plan.

(c) Any increase in Tier 1 capital necessary to meet the requirements of subparagraph (a) of this provision may not be accomplished through a deduction from the ALLL.

**9. Restrictions on Dividends.**

While this ORDER is in effect, the Bank shall not declare or pay any dividends without the prior written approval of the Supervisory Authorities.

**10. Liquidity Policy and Practices.**

(a) Within 90 days from the effective date of this ORDER, the Board shall review and revise the Bank's liquidity policy to address the recommendations made under the Liquidity heading in the Examination Conclusions and Comments pages of the Report of Examination. The liquidity policy shall incorporate the guidance contained in Financial Institution Letter 13-2010, dated April 5, 2010, entitled *Funding and Liquidity Risk Management*. Thereafter, the Bank shall implement and fully comply with the revised liquidity policy.

(b) The Board shall approve the revised liquidity policy, which approval shall be recorded in the Board's minutes. Thereafter, the Bank shall implement and fully comply with the liquidity policy. A copy of the revised liquidity policy shall

be provided to the Supervisory Authorities with the first progress report required by this ORDER.

**11. Funds Management and Interest Rate Risk.**

Within 90 days from the effective date of this ORDER, the Board shall review and revise the Bank's Asset/Liability Management Policy to address the recommendations made under the Sensitivity to Market Risk heading in the Examination Conclusions and Comments pages of the Report of Examination. The policy shall incorporate the guidance contained in the Joint Agency Policy Statement on Interest Rate Risk. Thereafter, the Bank shall implement and fully comply with the revised policy. A copy of the revised policy shall be provided to the Supervisory Authorities with the first progress report required by this ORDER.

**12. Business/Strategic Plan and Profit and Budget Plan.**

(a) Within 90 days from the effective date of this ORDER and within 60 days from the first day in each calendar year thereafter, the Board shall develop a written three-year business/strategic plan and one-year profit and budget plan, covering the overall operation of the Bank and its goals and strategies, consistent with sound banking practices, and taking



into account the Bank's other written plans, policies, or other actions as required by this ORDER.

(b) The business/strategic plan shall provide specific objectives for asset growth or reduction, loan portfolio mix, market focus, earnings projections, capital needs, and liquidity position. The profit and budget plan shall include goals and strategies for improving the earnings of the Bank. The budget shall include a description of the operating assumptions that form the basis for, and adequately support, major projected income and expense components.

(c) The Board shall approve the business/strategic plan and the profit and budget plan, which approval shall be recorded in the Board's minutes. Thereafter, the Bank shall implement and fully comply with the policies. A copy of the business/strategic plan and the profit and budget plan shall be provided to the Supervisory Authorities with the first progress report required by this ORDER.

**13. Correction of Special Mention Items and Technical Exceptions.**

(a) Within 90 days from the effective date of this ORDER, and within 60 days after receipt of any future reports of examination by either of the Supervisory Authorities, the Bank shall:

(i) address the deficiencies cited for assets listed on the "Items Listed for Special Mention" pages of the Report of Examination; and

(ii) correct the exceptions listed on the "Assets with Credit Data or Collateral Documentation Exceptions" pages of the Report of Examination.

(b) For any deficiency or exception that cannot be corrected in a manner consistent with safe and sound banking practices, the Bank shall document the reason for such inability in the borrower's credit file, and the Board, shall review and include a copy of the documentation in the Board's minutes.

(c) Quarterly progress reports detailing each outstanding special mention item and technical exception, and the Bank's plan for corrective action shall be submitted to the Board for review in connection with the Bank's periodic risk analysis. The report shall be made part of, and the review noted, in the Board's minutes.

(d) From the effective date of this ORDER, the Bank shall ensure that the necessary supporting documentation is obtained and evaluated before any credit or loan is extended.

**14. Elimination and/or Correction of Violations of Laws, Rules, and Regulations.**

(a) Within 90 days after the effective date of this ORDER, and within 60 days after receipt of any future reports of examination of the Bank by either of the Supervisory authorities, the Bank shall submit plans of action to the Supervisory Authorities for review and comment that address all apparent violations of law, rules, and regulations, cited in the Report of Examination, and such future reports of examinations.

(b) The plans of action required by this paragraph shall:

- (i) detail corrective actions taken and planned to correct, eliminate, and/or address, and prevent the recurrence of all apparent violations of law, rules, and regulations, detailed in the respective report of examination; and
- (ii) require progress reports submitted to the Board for review on at least a quarterly basis detailing each outstanding violation and the status of the Bank's plan for corrective action.

(c) The Board shall approve the plans of action and record such approval in the Board's minutes. Thereafter, the Bank shall follow the plans of action and shall document in the Board's minutes all actions taken to implement the plans of action required by this paragraph. A copy of those plans of action shall be provided to the Supervisory Authorities with the first progress report required by this ORDER.

**15. Disclosure of Order to Sole Shareholder.**

Following the effective date of this ORDER, the Bank shall provide a copy or otherwise furnish a description of this ORDER to its sole shareholder, (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.

**16. Progress Reports Detailing Compliance with ORDER.**

(a) During the last calendar week of August 2011, and within 30 days of the end of each calendar quarter thereafter, the Bank shall furnish written progress reports to the Supervisory Authorities detailing the form, manner, and results of any actions taken to secure compliance with this ORDER. Such written progress reports shall provide cumulative detail of the Bank's progress toward achieving compliance with each provision of the ORDER, including at a minimum:

(i) actions taken or in-process for addressing each provision;

(ii) results of the corrective actions taken;

(iii) the Bank's status of compliance with each provision of the ORDER; and

(iv) appropriate supporting documentation.

(b) Progress reports may be discontinued when the Supervisory Authorities have, in writing, released the Bank from making additional reports.

**MISCELLANEOUS**

The provisions of this ORDER shall not bar, estop, or otherwise prevent the FDIC, Minnesota Department of Commerce, or any other federal or state agency or department from taking any other action against the Bank or any of the Bank's current or former institution-affiliated parties.

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 and Minnesota Department of Commerce.

Issued Pursuant to Delegated Authority

Dated: June 22, 2011

FEDERAL DEPOSIT INSURANCE CORPORATION

By:

/s/

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Mark S. Moylan  
Deputy Regional Director

STATE OF MINNESOTA  
DEPARTMENT OF COMMERCE

By:

/s/

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Kevin M. Murphy  
Deputy Commissioner