

FEDERAL DEPOSIT INSURANCE CORPORATION

WASHINGTON, D.C.

AND

STATE OF ILLINOIS

DEPARTMENT OF FINANCIAL AND PROFESSIONAL REGULATION

DIVISION OF BANKING

SPRINGFIELD, ILLINOIS

_____ )	
In the Matter of )	CONSENT ORDER
)	
FARMERS STATE BANK OF SUBLETTE )	
SUBLETTE, ILLINOIS )	FDIC-11-520b
)	2011-DB-59
( ILLINOIS CHARTERED )	
INSURED NONMEMBER BANK )	
_____ )	

Farmers State Bank of Sublette, Sublette, Illinois ("Bank"), having been advised of its right to a NOTICE OF CHARGES AND OF HEARING detailing the unsafe or unsound banking practices and violations of law or regulation alleged to have been committed by the Bank, and of its right to a hearing on the charges under section 8(b) of the Federal Deposit Insurance Act ("Act"), 12 U.S.C. § 1818(b), and under 38 Ill. Adm. Code, § 392 et seq., regarding hearings before the Illinois Department of Financial and Professional Regulation, Division of Banking, ("Division"), and having waived those rights, entered into a STIPULATION AND CONSENT TO THE ISSUANCE OF A CONSENT ORDER

("STIPULATION") with representatives of the Federal Deposit Insurance Corporation ("FDIC") and the Division, dated January 5, 2012, whereby, solely for the purpose of this proceeding and without admitting or denying the charges of unsafe or unsound banking practices and violations of law or regulation relating to Capital, Asset Quality, Management, Earnings, and Sensitivity to Market Risk, the Bank consented to the issuance of a CONSENT ORDER ("ORDER") by the FDIC and the Division.

The FDIC and the Division considered the matter and determined that they had reason to believe the Bank had engaged in unsafe or unsound banking practices and therefore accepted the STIPULATION.

Having also determined that the requirements for issuance of an order under 12 U.S.C. § 1818(b) and Section 48(6), 205 ILCS 5/48(6), have been satisfied, the FDIC and the Division **HEREBY ORDER** 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, take affirmative action as follows:

MANAGEMENT

1. Within sixty (60) days from the effective date of this Order, the Bank shall have and retain qualified management. At a minimum, such management shall include a new President/Chief Executive Officer with proven ability in managing a bank of

comparable size and experience in upgrading and managing a bank with similar problems and an appropriate level of lending, collection, and loan supervision experience for the type and quality the Bank's existing loan portfolio. Management shall be provided the necessary written authority to implement the provisions of this ORDER. The qualifications of management shall be assessed on its ability to:

- (i) Comply with the requirements of this Order;
- (ii) Operate the Bank in a safe and sound manner;
- (iii) Comply with applicable laws, rules, and regulations; and
- (iv) Restore all aspects of the Bank to a safe and sound condition, including capital adequacy, asset quality, management effectiveness, earnings, liquidity, and sensitivity to interest rate risk.

#### BOARD COMPOSITION AND PARTICIPATION

2. (a) Within ninety (90) days of the effective date of this ORDER, the Bank shall retain two additional directors who are independent with respect to the Bank. "Independent with respect to the Bank" shall mean an individual who is not:

- (i) Employed in any capacity by the Bank, any of its subsidiaries, or affiliated organizations; and
- (ii) Related by blood or marriage to an officer or director of the Bank or its affiliates, and who does not otherwise share a common financial interest with such officer or director;
- (iii) Indebted, directly or indirectly, to the Bank or any of its affiliates, including the indebtedness of any entity in which the individual has a substantial financial interest, in an amount exceeding ten percent of the Bank's total Tier 1 capital and allowance for loan and lease losses.

(b) As of the effective date of this ORDER, the Bank's board of directors shall increase its participation in the affairs of the Bank, assuming full responsibility for the approval of sound policies and objectives and for the supervision of all of the Bank's activities, consistent with the role and expertise commonly expected for directors of banks of comparable size. This participation shall include meetings to be held no less frequently than monthly at which, at a minimum,

the following areas shall be reviewed and approved: reports of income and expenses; new, overdue, renewal insider, charged off, and recovered loans; investment activity; operating policies; individual committee reports; audit reports; internal control reviews including management's responses; reconciliation of general ledger accounts; and compliance with this ORDER. Board minutes shall document these reviews and approvals, including the names of any dissenting directors.

(c) During the life of this ORDER, the board of directors shall take action to ensure that complete and accurate minutes of the board and committee meetings are maintained, and the minutes adequately address the areas covered in this ORDER; and that management reports are sufficient to provide the Board with timely and adequate information necessary for making business decisions on the basis of fully informed and meaningful deliberation.

(d) Within thirty (30) days from the effective date of this ORDER, the Bank's board of directors shall develop, adopt, and implement a program that will provide for monitoring of the Bank's compliance with this ORDER. This shall include a committee that consists of at least three outside board members.

(e) Following the required date of compliance with subparagraph (b) above, the Bank's board of directors shall

review the Bank's compliance with this ORDER and record its review in the minutes of each regularly scheduled monthly board of directors' meeting. The minutes will describe what was discussed, how the Board intends to comply with each point in the ORDER that is not yet in compliance, and note the review of any regulatory letters that have been received having anything to do with the ORDER.

DIRECTORS AND SENIOR EXECUTIVE OFFICERS

3. During the life of the ORDER, prior to the addition of any individual to the board of directors or the employment of any individual as a senior executive officer, the Bank shall request and obtain the Division's written approval. For purposes of this ORDER, "senior executive officer" is defined as in section 32 of the Act ("**section 32**"), 12 U.S.C. § 1831 (i), and section 303.101 (b) of the FDIC Rule and Regulations, 12 C.F.R. § 303.101 (b).

CONSOLIDATED REPORTS OF CONDITION AND INCOME

4. (a) During the life of this Order, the Bank shall file with the FDIC Consolidated Reports of Condition and Income which accurately reflect the financial condition of the Bank as of the date of each such Report. Amended Reports of Condition and Income must be filed if previously submitted Reports were not filed in accordance with the Instructions for Preparation of Consolidated Reports of Condition and Income.

(b) In addition, and during the life of this ORDER, the Bank shall file with the FDIC Consolidated Reports of Condition and Income that accurately reflect the financial condition of the Bank as of the reporting period specified. In particular, such Reports shall incorporate any adjustment in the Bank's books made necessary or appropriate as a consequence of any FDIC or Division examination of the Bank during that Reporting period.

#### VIOLATIONS

5. (a) Within thirty (30) days from the effective date of this ORDER, the Bank shall eliminate and/or correct all violations of law, rule, and regulation listed in the Joint Report of Examination as of June 24, 2011 ("**Report**").

(b) Within thirty (30) days from the effective date of this ORDER, the Bank shall implement procedures to ensure future compliance with all applicable laws, rules, and regulations.

#### POLICY CONTRAVENTIONS

6. (a) Within thirty (30) days from the effective date of this ORDER, the Bank shall eliminate and/or correct all contraventions of statements of policy cited in the Report.

(b) Within thirty (30) days from the effective date of this ORDER, the Bank shall implement procedures to ensure future compliance with all applicable statements of policy.

#### GROWTH PLAN

7. During the life of this ORDER, the Bank shall not increase its total assets by more than three (3%) percent during any consecutive three-month period without providing, at least thirty (30) days prior to its implementation, a growth plan to the Division and Regional Director of the FDIC's Chicago Regional Office ("**Regional Director**"). Such growth plan, at a minimum, shall include the funding source to support the projected growth, as well as the anticipated use of funds. This growth plan shall not be implemented without the prior written consent of the Division and Regional Director. In no event shall the Bank increase its total assets by more than twelve (12%) percent annually. For the purpose of this paragraph, "total assets" shall be defined as in the Federal Financial Banks Examination Council's Instructions for the Consolidated Reports of Condition and Income.

#### CAPITAL

8. (a) Within sixty (60) days from the effective date of this ORDER the Bank shall have and maintain its level of Tier 1 capital as a percentage of its total assets ("**capital ratio**") to a minimum of eight percent (8%) and its level of qualifying total capital as a percentage of risk-weighted assets ("**total risk based capital ratio**") at a minimum of twelve percent (12%). For purposes of this ORDER, Tier 1 capital and total assets

shall be calculated in accordance with Part 325 of the FDIC Rules and Regulations ("**Part 325**"), 12 C.F.R. Part 325.

(b) Any subsequent increase in Tier 1 capital may be accomplished by the following:

- (i) The sale of common stock and noncumulative perpetual preferred stock constituting Tier 1 capital under Part 325;
- (ii) The elimination of all or part of the assets classified "Loss" at the Division Examination which began on May 28, 2010, without loss or liability to the Bank, provided any such collection on a partially charged-off asset shall first be applied to that portion of the asset which was not charged off pursuant to this ORDER;
- (iii) The collection in cash of assets previously charged off;
- (iv) The direct contribution of cash by the directors and/or the shareholders of the Bank;
- (v) Any other means acceptable to the Division and Regional Director; or

(vi) Any combination of the above means.

(c) If all or part of any subsequent increase in capital required by this paragraph is to be accomplished by the sale of new securities, the board of directors of the Bank shall adopt and implement a plan for the sale of such additional securities, including the voting of any shares owned or proxies held by or controlled by them in favor of said plan. Should the implementation of the plan involve public distribution of Bank securities, including a distribution limited only to the Bank's existing shareholders, the Bank shall prepare detailed offering materials fully describing the securities being offered, including an accurate description of the financial condition of the Bank and the circumstances giving rise to the offering, and other material disclosures necessary to comply with Federal securities laws. Prior to the implementation of the plan and, in any event, not less than twenty (20) days prior to the dissemination of such materials, the materials used in the sale of the securities shall be submitted to the FDIC's Accounting and Securities Disclosure Section, 550 17<sup>th</sup> Street, N.W., Washington, D.C. 20429 for its review. Any changes requested to be made in the materials by the FDIC shall be made prior to their dissemination.

(d) In complying with the provisions of this paragraph, the Bank shall provide to any subscriber and/or

purchaser of Bank securities written notice of any planned or existing development or other changes which are materially different from the information reflected in any offering materials used in connection with the sale of Bank securities. The written notice required by this paragraph shall be furnished within ten (10) calendar days of the date any material development or change was planned or occurred, which is earlier, and shall be furnished to every purchaser and/or subscriber of the Bank's original offering materials.

(e) Should the Bank be unable to reach the required capital levels within the time frames specified in subparagraph (a) above, within thirty (30) days of receipt of written direction from the Regional Director and the Division, the Bank shall develop, adopt, and implement a written plan to sell or merge itself into another federally insured financial institution. A copy of the plan required by this paragraph shall be submitted to, and determined to be acceptable by, the Regional Director and the Division.

#### ASSET QUALITY

9. (a) Within thirty (30) days from the effective date of this ORDER, the Bank shall formulate a written plan to reduce the exposure in each asset in excess of \$100,000 which is classified "Substandard" or "Doubtful" in the Report. 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 FDIC and Division. In developing the plan mandated by this paragraph, the Bank shall, at a minimum, and with respect to each adversely classified loan or lease, review, analyze, and document the financial position of the borrower, including source of repayment, repayment ability, and alternative repayment sources.

(b) In addition, the plan mandated by this provision shall also include, but not be limited to, the following:

- (i) Establish dollar levels to which the Bank shall reduce delinquencies and classified assets within six (6) and twelve (12) months from the effective date of this ORDER; and
- (ii) Provide for the submission of monthly written progress reports to the Bank's board of directors for review and notation in the minutes of the meetings of the board of directors.

(c) A copy of the plan required by this paragraph shall be submitted to the Division and Regional Director.

(d) While this ORDER remains in effect, the plan shall be revised to include assets which become delinquent by

ninety (90) days or more after the effective date of this ORDER or are adversely classified at any subsequent examinations.

ALLOWANCE FOR LOAN AND LEASE LOSSES

10. (a) Effective immediately upon the effective date of this ORDER, the Bank shall book a provision for the inadequate Allowance for Loan and Lease Losses ("**ALLL**") of at least \$355,000. This amount must be reflected in the March 31, 2011 Report of Condition and Income. Thereafter, the Bank shall ensure that the ALLL is adequately funded at all times.

(b) Within sixty (60) days from the effective date of this ORDER, the Board shall ensure the establishment of a comprehensive policy and methodology for determining the adequacy of the ALLL. The policy shall provide for a review of the ALLL at least once each calendar quarter and be completed at least ten (10) days prior to the end of each 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, ensure compliance with the following:

- (i) The Federal Financial Banks Examination Council's Instructions for the Reports of Condition and Income;
- (ii) The Interagency Statement of Policy on the Allowance for Loan and Lease Losses;

- applicable accounting guidance, including Financial Accounting Standards Board Accounting Standards Codification ("FASB ASC") Subtopic 450-10 and FASB ASC Subtopic 310-10 (which now supersede prior FAS 5 and 114 guidelines; and
- (iii) Other applicable regulatory guidance that addresses the adequacy of the Bank's allowance.

PROHIBITION OF ADDITIONAL LOANS TO CLASSIFIED BORROWERS

11. (a) As of the effective date of this ORDER, the Bank shall not extend, directly or indirectly, any additional credit to, or for the benefit of, any borrower who is already obligated in any manner to the Bank on any extension of credit (including any portion thereof) that has been charged off the books of the Bank or classified "Loss" in the Report, so long as such credit remains uncollected, without the prior written consent of the Regional Director.

(b) As of the effective date of this ORDER, the Bank shall not extend, directly or indirectly, any additional credit to, or for the benefit of, any borrower whose loan or other credit has been classified "Substandard", "Doubtful", or is listed for Special Mention in the Report, and is uncollected unless the Bank's board of directors has adopted, prior to such

extension of credit, a detailed written statement giving the reasons why such extension of credit is in the best interest of the Bank. A copy of the statement shall be signed by each Director, and incorporated in the minutes of the applicable board of directors' meeting. A copy of the statement shall be placed in the appropriate loan file.

LOAN POLICY

12. (a) Within sixty (60) days from the effective date of this ORDER, and annually thereafter, the board of directors of the Bank shall review the Bank's loan policy and procedures for adequacy and, based upon this review, shall make all appropriate revisions to the policy necessary to strengthen lending procedures and abate additional loan deterioration.

(b) The initial revisions to the Bank's loan policy required by this paragraph, at a minimum, shall include provisions which:

- (i) Establish review and monitoring procedures for compliance with the FDIC's regulation on appraisals, 12 C.F.R. Part 323;
- (ii) Designate the Bank's normal trade area;
- (iii) Establish review and monitoring procedures to ensure that all lending personnel are adhering to established

lending procedures and that the  
directorate is receiving timely and fully  
documented reports on loan activity,  
including any deviations from established  
policy;

- (iv) Require a nonaccrual policy in accordance with the Federal Financial Institutions Examination Council's Instructions for the Consolidated Reports of Condition and Income;
- (v) Require accurate reporting of past due loans to the loan committee on at least a monthly basis;
- (vi) Require strict guidelines and review of out-of-territory loans which, at a minimum, shall include complete credit documentation, approval by a majority of the board of directors prior to disbursement of funds, documentation of Bank expertise in the management of the loan or product, and a detailed written explanation of why the loan is in the best interest of the Bank;

- (vii) Establish standards for initiating collection efforts;
- (viii) Prohibit the payment of any loan through the use of overdrafts.

(c) The board of directors shall approve the written loan policy and any subsequent modification thereto, which approval shall be recorded in the minutes of a board of directors' meeting. Thereafter, the Bank shall implement and follow the amended written loan policy.

#### LOAN REVIEW AND GRADING SYSTEM

13. Within sixty (60) days from the date of this ORDER, the Bank shall implement revised comprehensive loan grading and review procedures. The procedures shall require that such loan grading and review will be performed by a qualified individual. The loan review shall at a minimum:

(a) Require periodic confirmation of the accuracy and completeness of the watch list and all risk grades assigned by the Bank's loan officers;

(b) Identify loans or relationships that warrant special attention of management;

(c) Identify violations of law, rules, or regulations and credit and collateral documentation exceptions and track corrective measures;

(d) Review the bank's application of FASB ASC Subtopic 310-10 (which now supersedes prior FAS 114 guidelines); and

(e) Identify loans not in conformance with the Bank's loan policy.

#### LENDING AND COLLECTION POLICIES

14. Immediately from the effective date of this ORDER, the Bank shall implement written lending and collection policies to provide effective guidance and control over the Bank's lending function including legal action to collect the Bank's problem loans.

#### OTHER REAL ESTATE POLICY

15. Within ninety (90) days from the effective date of the ORDER, the board of directors shall develop a written policy for managing the Other Real Estate ("ORE") of the Bank. At a minimum the policy shall provide for:

(a) Documentation that taxes and insurance premiums are paid on a timely basis;

(b) Independent appraisal of each parcel at the time of foreclosure and periodically thereafter, but no more than 12 months from the date of the prior appraisal report;

(c) Evidence that each parcel of ORE is listed with a real estate broker or otherwise made widely available for sale within an appropriate timeframe and at a realistic selling price; and

(d) Requirements for proper accounting, documentation, resale terms, and action plans for the orderly liquidation of ORE from the Bank's books.

CONCENTRATION OF CREDIT

16. Within ninety (90) days from the effective date of this ORDER, the Bank shall formulate, adopt and implement a written plan to reduce and manage the out of territory concentration of credit identified in the Report in a safe and sound manner. At a minimum, the plan must provide for written procedures for the ongoing measurement and monitoring of the concentrations of credit, establish policy guidelines for the portfolio mix, and set limits on concentrations commensurate with the Bank's capital position, safe and sound banking practices, and the overall risk profile of the Bank.

DIVIDEND RESTRICTIONS

17. As of the effective date of this ORDER, the Bank shall not declare or pay any dividend without the prior written consent of the Regional Director and the Division.

LIQUIDITY

18. During the life of this ORDER, the Bank shall submit to the Board for review and to the Regional Director and Division weekly liquidity analysis reports, in the format prescribed by the Regional Director and Division.

PROFIT PLAN AND BUDGET

19. (a) Within sixty (60) days from the effective date of this ORDER, the Bank shall adopt, implement, and adhere to a written profit plan and a realistic, comprehensive budget for all categories of income and expense for calendar years 2011 and 2012. The plans required by this paragraph shall contain formal goals and strategies, consistent with sound banking practices, to reduce discretionary expenses and to improve the Bank's overall earnings, and shall contain a description of the operating assumptions that form the basis for major projected income and expense components.

(b) The written profit plan shall address, at a minimum:

- (i) Realistic and comprehensive budgets;
- (ii) A budget review process to monitor the income and expenses of the Bank to compare actual figures with budgetary projections;
- (iii) Identification of major areas in, and means by which, earnings will be improved; and
- (iv) A description of the operating assumptions that form the basis for and

adequately support major projected income and expense components.

(c) During each monthly board meeting following completion of the profit plans and budgets required by this paragraph, the Bank's board of directors shall evaluate the Bank's actual performance in relation to the plan and budget, record the results of the evaluation, and note any actions taken by the Bank in the minutes of the board of directors' meeting at which such evaluation is undertaken.

(d) A written profit plan and budget shall be prepared for each calendar year for which this ORDER is in effect.

(e) Copies of the plans and budgets required by this paragraph shall be submitted to the Regional Director and the Division.

#### INTEREST RATE RISK AND SENSITIVITY

20. Within ninety (90) days from the effective date of this ORDER, the Bank shall review its written funds management plan and amend as necessary. The Bank shall approve the revised policy, which approval shall be noted in the minutes of the meeting of the board of directors. The policy provisions and sensitivity requirements shall be at a minimum:

(a) Identify personnel responsible for the funds management functions within the Bank;

(b) Revise the risk-based capital ratio (under Objectives and Capital Adequacy) to reflect the minimum risk-based capital ratio called for in the ORDER;

(c) Personnel responsible for funds management and the board are required to attend training on the Baker model until they understand the assumptions that go into the model and how to interpret the model results;

(d) The model shall be adjusted with the proper assumptions so that the EAR rate shock is accurate; and

(e) Management and the Board must list exceptions to the ALCO Policy in the board minutes and address how any exceptions will be corrected with the discussion noted in the minutes.

#### NOTIFICATION OF SHAREHOLDER

21. Following the effective date of this ORDER, the Bank shall send to its shareholder a copy of this ORDER: (1) in conjunction with the Bank's next shareholder communication; or (2) in conjunction with its notice of proxy statement preceding the Bank's next shareholder meeting.

#### PROGRESS REPORTS

22. Within thirty (30) days from the end of each calendar quarter following the effective date of this ORDER, the Bank shall furnish to the Division and Regional Director written progress reports signed by each member of the Bank's board of

directors, detailing the actions taken to secure compliance with the ORDER and the results thereof.

CLOSING PARAGRAPHS

The effective date of this ORDER shall be the date of its issuance by the Division and the FDIC.

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 Division and the FDIC.

Pursuant to delegated authority.

Dated: January 10, 2012.

\_\_\_\_\_/s/\_\_\_\_\_  
M. Anthony Lowe  
Regional Director  
Chicago Regional Office  
Federal Deposit Insurance  
Corporation

\_\_\_\_\_/s/\_\_\_\_\_  
Manuel Flores  
Director  
Illinois Department of Financial  
and Professional Regulation  
Division of Banking