

**#2003-155**

AGREEMENT BY AND BETWEEN  
First National Bank of Paonia  
Paonia, CO  
and  
The Office of the Comptroller of the Currency

First National Bank of Paonia, Paonia, CO (“Bank”) and the Comptroller of the Currency of the United States of America (“Comptroller”) wish to protect the interests of the depositors, other customers, and shareholders of the Bank, and, toward that end, wish the Bank to operate safely and soundly and in accordance with all applicable laws, rules and regulations.

The Comptroller, through his National Bank Examiner, has examined the Bank, and his findings are contained in the Report of Examination for the examination that commenced on August 18, 2003 (“ROE”).

In consideration of the above premises, it is agreed, between the Bank, by and through its duly elected and acting Board of Directors (“Board”), and the Comptroller, through his authorized representative, that the Bank shall operate at all times in compliance with the articles of this Agreement.

ARTICLE I

JURISDICTION

(1) This Agreement shall be construed to be a “written agreement entered into with the agency” within the meaning of 12 U.S.C. § 1818(b)(1).

(2) This Agreement shall be construed to be a “written agreement between such depository institution and such agency” within the meaning of 12 U.S.C. § 1818(e)(1) and 12 U.S.C. § 1818(i)(2).

(3) This Agreement shall be construed to be a “formal written agreement” within the meaning of 12 C.F.R. § 5.51(c)(6)(ii). See 12 U.S.C. § 1831i.

(4) This Agreement shall be construed to be a “written agreement” within the meaning of 12 U.S.C. § 1818(u)(1)(A).

(5) All reports or plans which the Bank or Board has agreed to submit to the Assistant Deputy Comptroller pursuant to this Agreement shall be forwarded to the:

Until December 5, 2003, send to:

Assistant Deputy Comptroller  
Denver Field Office  
1099 18th Street, Suite 2650  
Denver, CO 80202

After December 5, 2003, send to:

Assistant Deputy Comptroller  
Denver Field Office  
1225 17<sup>th</sup> Street, Suite 450  
Denver, CO 80202-5534

## ARTICLE II

### COMPLIANCE COMMITTEE

(1) Within fifteen (15) days, the Board shall appoint a Compliance Committee of at least three (3) directors, of which no more than one (1) shall be employees of the Bank or any of its affiliates (as the term “affiliate” is defined in 12 U.S.C. § 371c(b)(1)), or a family member of any such person. Upon appointment, the names of the members of the Compliance Committee shall be submitted in writing to the Assistant Deputy Comptroller. The Compliance Committee shall be responsible for monitoring and coordinating the Bank's adherence to the provisions of this Agreement

(2) The Compliance Committee shall meet at least monthly.

(3) Within thirty (30) days of the appointment of the Committee and quarterly thereafter, the Compliance Committee shall submit a written progress report to the Board setting forth in detail:

- (a) actions taken to comply with each Article of this Agreement; and
- (b) the results of those actions.

(4) The Board shall forward a copy of the Compliance Committee's report, with any additional comments by the Board, to the Assistant Deputy Comptroller.

### ARTICLE III

#### ALLOWANCE FOR LOAN AND LEASE LOSSES

(1) The Board shall review the adequacy of the Bank's Allowance for Loan and Lease Losses (“Allowance”) and shall expand their program for the maintenance of an adequate Allowance. This review and program shall be designed in light of the comments on maintaining a proper Allowance found in the Allowance for Loan and Lease Losses booklet, A-ALLL, of the Comptroller’s Handbook, and shall focus particular attention on the following factors not already addressed in your program:

- (a) results of the Bank's internal loan review; and
- (b) documented support for the percentages used in the general pool categories.

(2) Any deficiency in the Allowance shall be remedied in the quarter it is discovered, prior to the filing of the Consolidated Reports of Condition and Income, by additional provisions from earnings. Written documentation shall be maintained indicating the factors considered and conclusions reached by the Board in determining the adequacy of the Allowance.

(3) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the program developed pursuant to this Article.

#### ARTICLE IV

#### CAPITAL PLAN

(1) The Bank shall at least maintain the following capital levels (as defined in 12 C.F.R. Part 3):

- (a) Total risk-based capital at least equal to ten percent (10%) of risk-weighted assets;
- (b) Tier 1 capital at least equal to six and one-half percent (6.5%) of adjusted total assets.<sup>1</sup>

(2) The requirement in this Agreement to meet and maintain a specific capital level means that the Bank may not be deemed to be “well capitalized” for purposes of 12 U.S.C. § 1831o and 12 C.F.R. Part 6 pursuant to 12 C.F.R. § 6.4(b)(1)(iv).

(3) Within ninety (90) days, the Board shall develop, implement, and thereafter ensure Bank adherence to a three-year capital program. The program shall include:

- (a) specific plans for the maintenance of adequate capital that may in no event be less than the requirements of paragraph (1);

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<sup>1</sup> Adjusted total assets is defined in 12 C.F.R. § 3.2(a) as the average total asset figure used for Call Report purposes minus end-of-quarter intangible assets. As further noted in 12 C.F.R. § 3.2(a), a bank may be required to compute and maintain its leverage ratio on the basis of actual, rather than average total assets. This language would have to be modified to reflect that change.

- (b) projections for growth and capital requirements based upon a detailed analysis of the Bank's assets, liabilities, earnings, fixed assets, and off-balance sheet activities;
- (c) projections of the sources and timing of additional capital to meet the Bank's current and future needs;
- (d) the primary source(s) from which the Bank will strengthen its capital structure to meet the Bank's needs;
- (e) contingency plans that identify alternative methods should the primary source(s) under (d) above not be available; and
- (f) a dividend policy that permits the declaration of a dividend only:
  - (i) when the Bank is in compliance with its approved capital program;
  - (ii) when the Bank is in compliance with 12 U.S.C. §§ 56 and 60;
  - (iii) with prior written approval from the Assistant Deputy Comptroller, which shall be granted or denied within thirty (30) days of the receipt of a dividend request from the Board.

(4) Upon completion, the Bank's capital program shall be submitted to the Assistant Deputy Comptroller for prior determination of no supervisory objection. Upon receiving a determination of no supervisory objection from the Assistant Deputy Comptroller, the Bank shall implement and adhere to the capital program. The Board shall review and update the Bank's capital program on an annual basis, or more frequently if necessary. Copies of the reviews and updates shall be submitted to the Assistant Deputy Comptroller.

(5) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the program developed pursuant to this Article.

## ARTICLE V

### CREDIT AND COLLATERAL EXCEPTIONS

(1) Within ninety (90) days the Board shall obtain current and satisfactory credit information on all loans lacking such information, including those listed in the ROE, in any subsequent Report of Examination, in any internal or external loan review, or in any listings of loans lacking such information provided to management by the National Bank Examiners at the conclusion of an examination.

(2) Within ninety (90) days the Board shall ensure proper collateral documentation is maintained on all loans and correct each collateral exception listed in the ROE, in any subsequent Report of Examination, in any internal or external loan review, or in any listings of loans lacking such information provided to management by the National Bank Examiners at the conclusion of an examination.

(3) Effective immediately, the Bank may grant, extend, renew, alter or restructure any loan or other extension of credit only after:

- (a) documenting the specific reason or purpose for the extension of credit;
- (b) identifying the expected source of repayment in writing;
- (c) structuring the repayment terms to coincide with the expected source of repayment;
- (d) obtaining and analyzing current and satisfactory credit information, including cash flow analysis, where loans are to be repaid from operations;

- (i) Failure to obtain the information in (3)(d) shall require a majority of the full Board (or a delegated committee thereof) to certify in writing the specific reasons why obtaining and analyzing the information in (3)(d) would be detrimental to the best interests of the Bank.
- (ii) A copy of the Board certification shall be maintained in the credit file of the affected borrower(s). The certification will be reviewed by this Office in subsequent examinations of the Bank; and
- (e) documenting, with adequate supporting material, the value of collateral and properly perfecting the Bank's lien on it where applicable.

## ARTICLE VI

### CRITICIZED ASSETS

(1) The Bank shall take immediate and continuing action to protect its interest in those assets criticized in the ROE, in any subsequent Report of Examination, by internal or external loan review, or in any list provided to management by the National Bank Examiners during any examination.

(2) Within ninety (90) days, the Board shall adopt, implement, and thereafter ensure Bank adherence to a written program designed to eliminate the basis of criticism of assets criticized in the ROE, in any subsequent Report of Examination, or by any internal or external loan review, or in any list provided to management by the National Bank Examiners during any examination as "doubtful," "substandard," or "special mention." This program shall include, at a minimum:

- (a) an identification of the expected sources of repayment;

- (b) the appraised value of supporting collateral and the position of the Bank's lien on such collateral where applicable;
- (c) an analysis of current and satisfactory credit information, including cash flow analysis where loans are to be repaid from operations; and
- (d) the proposed action to eliminate the basis of criticism and the time frame for its accomplishment.

(3) Upon adoption, a copy of the program for all criticized assets equal to or exceeding fifty thousand dollars (\$50,000) shall be forwarded to the Assistant Deputy Comptroller.

(4) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the program developed pursuant to this Article.

(5) The Board, or a designated committee, shall conduct a review, on at least a quarterly basis, to determine:

- (a) the status of each criticized asset or criticized portion thereof that equals or exceeds fifty thousand dollars (\$50,000);
- (b) management's adherence to the program adopted pursuant to this Article;
- (c) the status and effectiveness of the written program; and
- (d) the need to revise the program or take alternative action.

(6) A copy of each review shall be forwarded to the Assistant Deputy Comptroller on a quarterly basis in a format similar to Appendix A, attached hereto.

(7) The Bank may extend credit, directly or indirectly, including renewals, extensions or capitalization of accrued interest, to a borrower whose loans or other extensions of credit are

criticized in the ROE, in any subsequent Report of Examination, in any internal or external loan review, or in any list provided to management by the National Bank Examiners during any examination and whose aggregate loans or other extensions exceed fifty thousand dollars (\$50,000) only if each of the following conditions is met:

- (a) the Board or designated committee finds that the extension of additional credit is necessary to promote the best interests of the Bank and that prior to renewing, extending or capitalizing any additional credit, a majority of the full Board (or designated committee) approves the credit extension and records, in writing, why such extension is necessary to promote the best interests of the Bank; and
- (b) a comparison to the written program adopted pursuant to this Article shows that the Board's formal plan to collect or strengthen the criticized asset will not be compromised.

(8) A copy of the approval of the Board or of the designated committee shall be maintained in the file of the affected borrower.

## ARTICLE VII

### LENDING POLICY

(1) Within ninety (90) days, the Board shall review and revise the Bank's written loan policy and construction underwriting standards. In revising the loan policy and underwriting standards, the Board shall refer to the Loan Portfolio Management and Commercial Real Estate and Construction Lending booklets of the Comptroller's Handbook. The loan policy (letters a – o below) and construction underwriting standards (letters p – s below) shall incorporate, but not necessarily be limited to, the following:

- (a) a description of acceptable types of loans;
- (b) a provision that current and satisfactory credit information will be obtained on each borrower;
- (c) maturity scheduling related to the anticipated source of repayment, the purpose of the loan, and the useful life of the collateral;
- (d) maximum ratio of loan value to appraised value or acquisition costs of collateral securing the loan;
- (e) collection procedures, to include follow-up efforts, that are systematically and progressively stronger;
- (f) a definition of the Bank's trade area;
- (g) guidelines and limitations for loans originating outside of the Bank's trade area;
- (h) a limitation on aggregate outstanding loans in relation to other balance sheet accounts;
- (i) distribution of loans by category;
- (j) guidelines for loans to insiders, including a statement that such loans will not be granted on terms more favorable than those offered to similar outside borrowers;
- (k) guidelines and limitations on concentrations of credit;
- (l) a limitation on the type and size of loans that may be made by loan officers without prior approval by the Board or a committee established by the Board for this purpose;

- (m) measures to correct the deficiencies in the Bank's lending procedures noted in any ROE;
- (n) guidelines designed to improve Board oversight of the loan approval process, specifically with regard to credits exhibiting significant risk;
- (o) charge-off guidelines, by type of loan or other asset, including Other Real Estate Owned, addressing the circumstances under which a charge-off would be appropriate and ensuring the recognition of losses within the quarter of discovery; and
- (p) cash flow analyses are performed on construction loan borrowers;
- (q) copies of original invoices are received and retained in file, scrutinized and compared to the construction budget to identify and resolve cost overruns;
- (r) periodic inspections are performed on all construction projects; and
- (s) all construction loans are either in conformity with the Bank's construction loan policies and procedures or in compliance with the Bank's written provisions for exceptions to loan policies and procedures.

(2) Upon adoption, the loan policy and construction underwriting standards shall be implemented, the Board shall thereafter ensure Bank adherence to the policy and underwriting standards, and a copy of the policy and underwriting standards shall be forwarded to the Assistant Deputy Comptroller for review.

(3) Within ninety (90) days, the Board shall develop, implement, and thereafter ensure Bank adherence to systems, which provide for effective monitoring of:

- (a) compliance with the Bank's lending policy and construction underwriting standards, laws, rules, and regulations pertaining to the Bank's lending function;
- (b) a system to track and analyze policy exceptions;
- (c) adequacy of credit and collateral documentation, and
- (d) concentrations of credit.

(4) On a quarterly basis management will provide the Board with a written report including the identification of loans not in conformance with the Bank's lending policies, and exceptions to the Bank's lending policy and underwriting standards.

(5) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the policy and underwriting standards developed pursuant to this Article.

(6) Upon completion, the Board shall submit a copy of the program to the Assistant Deputy Comptroller for review.

## ARTICLE VIII

### LOAN REVIEW CONSULTANT

(1) Within ninety (90) days, the Board shall employ a qualified consultant to perform an ongoing asset quality review of the Bank. The consultant shall be utilized until such time as an ongoing internal asset quality review system is developed by the Board, implemented and demonstrated to be effective.

(2) Prior to the appointment or employment of any individual to this loan review consultant or entering into any contract with a consultant, the Board shall submit the name and

qualifications of the proposed consultant and the proposed terms of employment to the Assistant Deputy Comptroller for a prior determination of no supervisory objection.

(3) Before terminating the consultant's asset quality review services, the Board shall both certify the effectiveness of the internal asset quality review system, and receive prior determination of no supervisory objection from the Assistant Deputy Comptroller.

(4) The requirement to submit information and the provisions for prior determination of no supervisory objection in this Article are based on the authority of 12 U.S.C. § 1818(b) and do not require the Comptroller or the Assistant Deputy Comptroller to complete his/her review and act on any such information or authority within ninety (90) days.

## ARTICLE IX

### MERCHANT PROCESSING POLICY

(1) Within thirty (30) days, the Board shall develop, implement, and thereafter ensure Bank adherence to a written policy governing the Bank's merchant processing activities with any merchant processor. The policy shall address, but not be limited to:

- (a) Procedures to ensure compliance with the contract with ECHO, including but not limited to, Exhibit A of the Bankcard Merchant Marketing and Processing Services Contract dated September 12, 2003;
- (b) underwriting standards for accounts that the bank must assume all the risk; and
- (c) the monthly reports to be received and reviewed from the processor that includes the level of merchant activity, charge-backs, and fraudulent activities for the accounts that the bank would accept all the risk.

(2) Upon completion, the Board shall submit a copy of the policy to the Assistant Deputy Comptroller for review.

(3) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the policies developed pursuant to this Article.

## ARTICLE X

### PARTICIPATIONS PURCHASED

(1) The Bank may grant, purchase, assume or acquire in any manner, directly or indirectly, or as a fiduciary or nominee, any loan, loan participation, loan obligation or other asset, as long as such grant, purchase, assumption, or acquisition is consistent with safe and sound banking practices, the guidelines set forth in Banking Circular 181 (Revised), dated August 2, 1984, and the requirements of 12 C.F.R. Part 34.

## ARTICLE XI

### VIOLATIONS OF LAW

(1) The Board shall immediately take all necessary steps to ensure that Bank management corrects each violation of law, rule or regulation cited in the ROE and in any subsequent Report of Examination. The quarterly progress reports required by Article II of this Agreement shall include the date and manner in which each correction has been effected during that reporting period.

(2) Within ninety (90) days, the Board shall adopt, implement, and thereafter ensure Bank adherence to specific procedures to prevent future violations as cited in the ROE and shall adopt, implement, and ensure Bank adherence to general procedures addressing compliance

management which incorporate internal control systems and education of employees regarding laws, rules and regulations applicable to their areas of responsibility.

(3) Within sixty (60) days of receipt of any subsequent Report of Examination which cites violations of law, rule, or regulation, the Board shall adopt, implement, and thereafter ensure Bank adherence to specific procedures to prevent future violations as cited in the ROE and shall adopt, implement, and ensure Bank adherence to general procedures addressing compliance management which incorporate internal control systems and education of employees regarding laws, rules and regulations applicable to their areas of responsibility.

(4) Upon adoption, a copy of these procedures shall be promptly forwarded to the Assistant Deputy Comptroller.

(5) The Board shall ensure that the Bank has policies, processes, personnel, and control systems to ensure implementation of and adherence to the procedures developed pursuant to this Article.

## ARTICLE XII

### ADMINISTRATIVE APPEALS AND EXTENSIONS OF TIME

(1) If the Bank determines that an exception to any provision of this Agreement is in the best interests of the Bank, or requires an extension of any timeframe within this Agreement, the Board shall submit a written request to the Assistant Deputy Comptroller asking for relief.

(2) Any written requests submitted pursuant to this Article shall include a statement setting forth in detail the special circumstances that prevent the Bank from complying with any provision, that require the Assistant Deputy Comptroller to exempt the Bank from any provision,

or that require an extension of any timeframe within this Agreement. All such requests shall be accompanied by relevant supporting documentation.

(3) The Assistant Deputy Comptroller's decision in granting the request is final and not subject to further review.

### ARTICLE XIII

#### CLOSING

(1) Although the Board has agreed to submit certain programs and reports to the Assistant Deputy Comptroller for review or prior determination of no supervisory objection, the Board has the ultimate responsibility for proper and sound management of the Bank.

(2) It is expressly and clearly understood that if, at any time, the Comptroller deems it appropriate in fulfilling the responsibilities placed upon him by the several laws of the United States of America to undertake any action affecting the Bank, nothing in this Agreement shall in any way inhibit, estop, bar, or otherwise prevent the Comptroller from so doing.

(3) Any time limitations imposed by this Agreement shall begin to run from the effective date of this Agreement. Such time requirements may be extended in writing by the Assistant Deputy Comptroller for good cause upon written application by the Board.

(4) The provisions of this Agreement shall be effective upon execution by the parties hereto and its provisions shall continue in full force and effect unless or until such provisions are amended in writing by mutual consent of the parties to the Agreement or excepted, waived, or terminated in writing by the Comptroller.

(5) In each instance in this Agreement in which the Board is required to ensure adherence to, and undertake to perform certain obligations of the Bank, it is intended to mean that the Board shall:

- (a) authorize and adopt such actions on behalf of the Bank as may be necessary for the Bank to perform its obligations and undertakings under the terms of this Agreement;
- (b) require the timely reporting by Bank management of such actions directed by the Board to be taken under the terms of this Agreement;
- (c) follow-up on any non-compliance with such actions in a timely and appropriate manner; and
- (d) require corrective action be taken in a timely manner of any non-compliance with such actions.

(6) This Agreement is intended to be, and shall be construed to be, a supervisory “written agreement entered into with the agency” as contemplated by 12 U.S.C. § 1818(b)(1), and expressly does not form, and may not be construed to form, a contract binding on the OCC or the United States. Notwithstanding the absence of mutuality of obligation, or of consideration, or of a contract, the OCC may enforce any of the commitments or obligations herein undertaken by the Bank under its supervisory powers, including 12 U.S.C. § 1818(b)(1), and not as a matter of contract law. The Bank expressly acknowledges that neither the Bank nor the OCC has any intention to enter into a contract. The Bank also expressly acknowledges that no OCC officer or employee has statutory or other authority to bind the United States, the U.S. Treasury Department, the OCC, or any other federal bank regulatory agency or entity, or any officer or employee of any of those entities to a contract affecting the OCC’s exercise of its

supervisory responsibilities. The terms of this Agreement, including this paragraph, are not subject to amendment or modification by any extraneous expression, prior agreements or prior arrangements between the parties, whether oral or written.

IN TESTIMONY WHEREOF, the undersigned, authorized by the Comptroller, has hereunto set his/her hand on behalf of the Comptroller.

Signed

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Linda H. Pfortmiller  
Assistant Deputy Comptroller  
Denver Field Office

November 20, 2003

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Date

IN TESTIMONY WHEREOF, the undersigned, as the duly elected and acting Board of Directors of the Bank, have hereunto set their hands on behalf of the Bank.

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|--|---------------------------|
| Signed<br>_____<br>Gerald E. Anderson  | 11-20-03<br>_____<br>Date |
| Signed<br>_____<br>John L. Blair       | 11-20-03<br>_____<br>Date |
| Signed<br>_____<br>John S. Blair       | 11/20/03<br>_____<br>Date |
| Signed<br>_____<br>Jess Campbell       | 11-20-03<br>_____<br>Date |
| Signed<br>_____<br>Gary Duke           | 11-20-03<br>_____<br>Date |
| Signed<br>_____<br>Jack G. Lengemann   | 11/20/03<br>_____<br>Date |
| Signed<br>_____<br>Kenneth G. Mitchell | 11-20-03<br>_____<br>Date |
| _____<br>_____                         | _____<br>_____<br>Date    |
| _____<br>_____                         | _____<br>_____<br>Date    |
| _____<br>_____                         | _____<br>_____<br>Date    |