

UNITED STATES OF AMERICA
DEPARTMENT OF THE TREASURY
COMPTROLLER OF THE CURRENCY

In the Matter of: Merchants Bank of California, National Association Carson, California)))	AA-WE-10-37
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CONSENT ORDER

The Comptroller of the Currency of the United States of America (“Comptroller”), through his National Bank Examiner, has supervisory authority over Merchants Bank of California, National Association, Carson, California (“Bank”).

The Bank, by and through its duly elected and acting Board of Directors (“Board”), has executed a “Stipulation and Consent to the Issuance of a Consent Order,” dated June 22, 2010, that is accepted by the Comptroller. By this Stipulation and Consent, which is incorporated by reference, the Bank has consented to the issuance of this Consent Order (“Order”) by the Comptroller.

Pursuant to the authority vested in it by the Federal Deposit Insurance Act, as amended, 12 U.S.C. § 1818, the Comptroller hereby orders that:

Article I

Compliance Committee

(1) Within five (5) days of this Order, the Board shall appoint a Compliance Committee of at least four (4) directors of which at least two (2) may not 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 and, in the event of a change of the membership, the name of any new member shall be submitted in writing to the Assistant Deputy Comptroller.

(2) The Compliance Committee shall be responsible for monitoring and coordinating the Bank's adherence to the provisions of this Order and shall meet at least monthly.

(3) By no later than July 31, 2010, and by the end of every calendar month thereafter, the Compliance Committee shall submit a written progress report to the Board setting forth in detail:

- (a) a description of the action needed to achieve full compliance with each Article of this Order;
- (b) actions taken to comply with each Article of this Order; and
- (c) the results and status of those actions.

(4) The Board shall provide a summary report of the progress reached in attaining compliance with each Article of this Order to the Assistant Deputy Comptroller within fifteen (15) days of the end of each calendar quarter.

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

Assistant Deputy Comptroller
Southern California North Field Office
550 North Brand Blvd., Suite 500
Glendale, California 91203

(6) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the policies, procedures and programs required by this Order.

Article II

Management And Board Oversight

(1) Within ninety (90) days of this Order, the Board shall take the necessary steps to eliminate the deficiencies in management leadership and Board oversight as described in the

Report of Examination conducted as of September 30, 2009 (the “ROE”), to include specific actions for attaining the necessary management expertise, Board involvement, and the retention of necessary outside consultants to attain compliance with this Order, return the Bank to a safe and sound condition, and ensure compliance with all applicable laws, rules and regulations.

(2) Within ninety (90) days of this Order, the Board shall prepare and submit to the Assistant Deputy Comptroller for a prior written determination of no supervisory objection, a written program designed to eliminate the deficiencies in corporate governance practices, including but not limited to:

- (a) the development of sound operating policies and procedures;
- (b) procedures to ensure accurate regulatory and Board reporting;
- (c) policies and procedures to ensure executive compensation is reasonable and proportionate to services received and are supported by sufficient records to demonstrate the fair value of services received, their direct benefit to the Bank, and the appropriateness of the salary, bonus and other compensation paid;
- (d) the development of sound internal controls to monitor policy adherence;
and
- (e) assigned accountability for these processes.

(3) After the OCC has advised the Bank that it does not take supervisory objection to the corporate governance program required by this Article, the Board shall immediately implement, and shall thereafter ensure adherence to its terms.

(4) Within forty-five (45) days of this Order, the Board shall take the necessary steps to appoint a Chief Operating Officer with the knowledge, skills, and abilities necessary to operate the Bank in a safe and sound manner.

(5) Prior to the appointment or employment of a Chief Operating Officer, or entering into any contract with any person for this position, the Bank must provide the Assistant Deputy Comptroller with written notice as required by 12 C.F.R. § 5.51 (notice forms and instructions in the “Changes in Directors and Senior Executive Officers” and “Background Investigations” booklets of the Comptroller’s Licensing Manual).

(6) The Assistant Deputy Comptroller shall have the power to disapprove the appointment of the proposed new executive officer. However, the lack of disapproval of such individuals shall not constitute an approval or endorsement of them.

(7) Within ninety (90) days of this Order, the Board shall ensure that it maintains qualified, competent management and staff to ensure the Bank operates in a safe and sound manner and in compliance with all applicable laws, rules and regulations.

(8) Within thirty (30) days of this Order, the Board shall develop, adopt, and thereafter adhere to a written policy designed to ensure that management effectively addresses adverse findings contained in compliance reviews, audits, and examinations. The policy shall include, at a minimum:

- (a) a requirement that management responds to any audit or compliance criticisms, and regulatory violations of law, unsafe or unsound banking practices, breaches of fiduciary duty, and Matters Requiring Attention (collectively, “material criticisms”) with a written action plan that contains:

- (i) corrective actions to be taken;
- (ii) deadlines for taking the corrective action; and
- (iii) the individual responsible for making the corrective action;
- (b) formal review and approval by the Board of management's proposed actions to be taken;
- (c) a tracking system that will ensure that material criticisms are reported to the Board and corrected in a timely manner; and
- (d) retention in the Bank's books and records of:
 - (i) all written responses to material criticisms; and
 - (ii) documentation of Board approval of the written responses.

(9) A copy of the policy developed pursuant to Paragraph (7) of this Article shall be forwarded to the Assistant Deputy Comptroller within the month following its adoption by the Board.

Article III

Affiliate Transactions, Regulation O, and Conflicts

(1) The Bank shall not, directly or indirectly, pay money or its equivalent to or for the benefit of, or extend credit in any form to or for the benefit of, its affiliates, or transfer assets between the Bank and its affiliates, or enter into or engage in any transaction that obligates the Bank to do the same, unless:

- (a) the Board has conducted an independent review of the action, that is documented in writing; and
- (b) the Board has determined in writing that it is advantageous for the Bank to engage in such action, and that the action complies with all applicable

laws, rules, regulations, and Comptroller's issuances, including, but not limited to 12 C.F.R. Part 223.

(2) For purposes of this Article, "affiliate" shall have the meaning set forth in 12 C.F.R. § 223.2(a) as if the Bank were a member bank, provided that any subsidiary of the Bank shall be considered an affiliate of the Bank.

(3) Within thirty (30) days of this Order, the Board shall adopt, implement, and thereafter ensure Bank adherence to a written, comprehensive conflict of interest program (including revised policies and procedures) applicable to the Bank's directors, principal shareholders, executive officers, affiliates, and employees ("Insiders") and related interests of such Insiders. The program, in addition to defining a conflict of interest, shall address:

- (a) avoidance of conflicts of interest and breaches of fiduciary duty, and the appearance of conflicts of interest;
- (b) involvement in the loan approval process of Insiders who may benefit directly or indirectly from the decision to grant credit;
- (c) disclosure of actual and potential conflicts of interest to the Board, and periodic disclosure of "related interests" as defined by 12 C.F.R. Part 215;
- (d) requirements for arms-length dealing in any transactions by Insiders, or their related organizations, involving the Bank's sale, purchase, or rental of property and services;
- (e) disclosure of any Insider's material interest in the business of a borrower, an applicant, or other customer of the Bank;
- (f) procedures to ensure compliance with Regulation O, including but not limited to, 12 C.F.R. §§ 215.4 and 215.5; and

(h) restrictions on, and disclosure of receipt of anything of value by Insiders, directly or indirectly, from borrowers, loan applicants, other customers, or suppliers of the Bank.

(4) By no later than December 31, 2010, the Board shall correct the violations of the legal lending limit, Regulation O and Regulation W cited in the ROE, including but not limited to, the repayment of loan number 1105562 in the amount of \$1,450,000 originated on or about June 8, 2001, and any and all renewals or modifications made thereto to such loan.

Article IV

Capital and Strategic Plan

(1) The Bank shall maintain at all times the following minimum capital ratios:

- (a) Tier 1 capital at least equal to nine percent (9%) of adjusted total assets;
and
- (b) total risk-based capital at least equal to twelve percent (12%) of risk-weighted assets.

(2) For purposes of this Article, “Tier 1 capital,” “total risk-based capital,” “adjusted total assets,” and “risk-weighted assets” are as defined in 12 C.F.R. Part 3.

(3) The requirement in this Order to meet and maintain a specific capital level means that the Bank is not to 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).

(4) Effective immediately, the Bank shall only declare dividends when:

- (a) the Bank is in compliance with the Bank’s Three-Year Plan as described below;
- (b) the Bank is in compliance with 12 U.S.C. §§ 56 and 60; and

(c) the Bank has received a prior written determination of no supervisory objection from the Assistant Deputy Comptroller.

(5) Effective as of the date of this Order, the Bank shall not increase its total loans above the amount shown on its books and records as of March 31, 2009 by more than five percent (5%) per annum, until the Bank corrects the deficiencies in Asset Quality described in the ROE, returns the Bank to a satisfactory condition, and the Bank receives a prior written determination of no supervisory objection from the Assistant Deputy Comptroller. For purposes of this Paragraph, the Bank's total loans shall be defined as the amount reported in its Consolidated Report of Condition ("Call Report").

(6) The Board shall take the necessary steps to ensure compliance with the Bank's Three-Year Plan to which the Assistant Deputy Comptroller has previously taken no supervisory objection. The Board shall also periodically (no less than annually) review the Bank's compliance with, and appropriateness of, the Bank's Three-Year Plan and make adjustments as necessary.

Article V

Liquidity Management

(1) Within thirty (30) days of this Order, the Board shall develop and submit for a prior written determination of no supervisory objection, a written liquidity program to ensure the Bank maintains liquidity at a level that is sufficient to sustain the Bank's current operations and to withstand any anticipated or extraordinary demand against its funding base, to include at a minimum:

(a) measures to eliminate reliance upon brokered deposits and to reduce reliance upon credit-sensitive wholesale borrowings;

- (b) measures to increase and maintain sufficient on-balance sheet liquidity;
- (c) the establishment of additional back-up funding sources;
- (d) policies and procedures to ensure the implementation of adequate liquidity planning tools, to include:
 - (i) a review of administrative policies and procedures to ensure they are consistent with the Board's guidance and risk tolerances;
 - (ii) specific balance sheet liquidity targets that are consistent with the tools used to measure performance;
 - (iii) reasonable risk limits to control the level of liquidity risk that incorporate forward-looking risk measurements and liability concentration limits such as limits on the amount of funds that may be sourced from any individual customer or groups of customers, or liability concentration limits by instrument; and
- (e) a contingency funding plan that ensures the Bank can remain liquidity solvent through stressed environments and that includes, at a minimum:
 - (i) management's best estimate of balance sheet changes that may result from a liquidity or credit event;
 - (ii) specific terms or events that trigger enactment of the plan;
 - (iii) necessary management information systems and reporting criteria for use in crisis situations;
 - (iv) management responsibilities for enacting the plan and for taking specific actions once enacted; and

- (v) prioritization of all sources of funding for the various scenarios including asset side funding, liability side funding, and off-balance sheet funding.

(2) After the OCC has advised the Bank that it does not take supervisory objection to the liquidity program required by this Article, the Board shall immediately implement, and shall thereafter ensure adherence to its terms.

Article VI

Credit Underwriting and Administration

(1) Effective as of the date of this Order, the Board shall ensure that all lending officers comply with all laws, rules, regulations, Bank policies and procedures, safe and sound banking practices, and fiduciary duties.

(2) Effective as of the date of this Order, the Bank may not grant, extend, renew, modify or restructure any loan or other extension of credit equal to or exceeding one hundred thousand dollars (\$100,000), without:

- (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 current and satisfactory credit information, including performing and documenting analysis of credit information and a detailed cash flow analysis of all expected repayment sources;

- (e) determining and documenting whether the loan complies with the Bank's Loan Policy and if it does not comply, providing identification of the exception and justification to support waiving the policy exception;
- (f) making and documenting the determinations made regarding the customer's ability to repay the credit on the proposed repayment terms;
- (g) providing an accurate risk assessment grade and proper accrual status for each credit as further described in Article IX;
- (h) documenting, with adequate supporting material, the value of collateral and properly perfecting the Bank's lien on it where applicable; and
- (i) obtaining the written approval of the Bank's Loan Committee or Board.

(3) Within thirty (30) days of this Order, the Board shall take the necessary steps to 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.

(4) Effective as of the date of this Order, 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.

(5) Within thirty (30) days of this Order, the Board shall revise, adopt, implement, and thereafter ensure Bank adherence to a written program of policies and procedures designed to aggregate and track exceptions to the Bank Loan Policy. This includes at a minimum,

monthly Board monitoring of policy exception reports that track aggregate number and dollar amount of loans with material underwriting exceptions by type of loan and loan officer.

(6) Effective as of the date of this Order, the Board shall take the necessary steps to eliminate credit, collateral, and Bank Loan Policy exceptions, to include, at a minimum, the development of a program that makes loan officers accountable for such exceptions and considers such exceptions in the periodic performance reviews and compensation of such loan officers.

Article VII

Commercial Real Estate Risk Management

(1) Effective as of the date of this Order, the Board shall take the necessary steps to ensure that the Bank manages the risk in the Bank's commercial real estate ("CRE") loan portfolio in accordance with the guidelines set forth in OCC Bulletin 2006-46, Concentration in Commercial Real Estate Lending, Sound Risk Management Practices (dated December 6, 2006), and the Commercial Real Estate and Construction Lending, A-CRE, of the *Comptroller's Handbook*, to include, at a minimum:

- (a) the establishment of CRE concentration limits stratified by type, locality and other meaningful measures supported by written analysis;
- (b) monthly monitoring of concentration reports that stratify the CRE portfolio by product type, locality and other meaningful measures;
- (c) strategies and procedures to manage and reduce CRE concentrations to conform with established limits set in Subparagraph (a) of this Article;

- (d) portfolio-level multi-factor stress testing and/or sensitivity analysis to quantify the impact of changing economic conditions on asset quality, earnings, and capital;
- (e) significant individual loan stress testing and/or sensitivity analysis to quantify the impact of changing economic conditions on asset quality, earnings, and capital;
- (f) the establishment of Loan Policy CRE underwriting standards by CRE type that include specific requirements relating to:
 - (i) maximum loan amount and maturity by type of property;
 - (ii) approval authorizations;
 - (iii) minimum file documentation and analysis;
 - (iv) minimum requirements for initial investment and maintenance of hard equity;
 - (v) minimum standards for borrower net worth, property cash flow/debt service, collateral coverage, and guarantor support;
 - (vi) the performance of global cash flow analysis to evaluate the repayment ability of borrowers with multiple projects;
 - (vii) standards for ensuring a complete and accurate assessment of guarantor support;
 - (viii) standards for ensuring that CRE loans have appropriate minimum loan covenants;
 - (ix) minimum standards for the acceptability for using, and defined limits for soft cost and/or interest reserve financing;

- (x) maximum amortization periods and minimum principal curtailment for CRE and construction projects that are not meeting original projections; and
- (xi) procedures for loan closing and disbursement processes, including the supervised disbursement of construction loan proceeds;
- (g) requirements to ensure participations purchased are consistent with sound banking practices, guidelines set forth in Banking Circular 181 (Revised), dated August 2, 1984, and the requirements of 12 C.F.R. Part 34;
- (h) maintenance of proper collateral margins in loans made for the purpose of constructing or developing real estate, including but not limited to, procedures for ensuring that:
 - (i) periodic, meaningful, well-documented, inspections are performed on all construction projects;
 - (ii) draw requests are advanced in accordance with construction progress and budget;
 - (iii) documentation is maintained of project completion versus amount advanced;
 - (iv) lien waivers are obtained from contractors and sub-contractors; and
 - (v) borrower's hard equity is tracked by project;
- (i) standards for when CRE loan policy exceptions are appropriate, what factors should exist to mitigate exceptions, and how the level and trend of exceptions should be documented, tracked and reported to the Board; and

- (j) required periodic reviews that encompass the stress-testing, global cash flow analysis, guarantor support, collateral evaluations and risk rating requirements of this Article.

Article VIII

Appraisal and Evaluation Process

(1) Effective as of the date of this Order, the Board shall ensure Bank adherence to the Bank's written Appraisal and Evaluation policy and procedures.

Article IX

Credit Risk Ratings and Nonaccrual Recognition

(1) Effective as of the date of this Order, the Board shall take the necessary steps to ensure that the risk associated with the Bank's loans is properly reflected and accounted for on the Bank's books and records, to include, at a minimum, the monthly review of all credit relationships that equal or exceed one hundred thousand dollars (\$100,000) by the loan officers to ensure that:

- (a) the Bank's loans and other assets are appropriately and timely risk rated and charged off using a loan grading system that is based upon current facts, existing repayment terms and that is consistent with the guidelines set forth in Rating Credit Risk, A-RCR, of the *Comptroller's Handbook*; and
- (b) the Bank's loans and other assets are timely placed on nonaccrual in accordance with the guidelines set forth in the Call Report;

(2) By no later than July 31, 2010, the Board shall prepare a written program designed to ensure that the Bank complies with Subparagraphs (a) and (b) of this Article, that contains at a minimum:

- (a) immediate and ongoing training for the lending staff with respect to the application of Subparagraphs (a) and (b) of this Article;
- (b) procedures to ensure loan officers are held accountable for failing to appropriately and timely risk rate and/or place loans on nonaccrual, including but not limited to, consideration of loan officer and staff failure to properly risk rate and/or place loans on nonaccrual in periodic performance reviews and compensation.

(3) After the Board has developed the program required by this Article, the Board shall immediately implement, and shall thereafter ensure adherence to its terms.

Article X

Problem Loan Management

(1) Effective as of the date of this Order, the Board 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 sixty (60) days of this Order, the Board shall prepare, adopt and thereafter ensure adherence to, a written program designed to reduce the Bank's criticized assets (the "Problem Assets Program"). The Problem Assets Program shall include or address the following matters:

- (a) aggregate reporting of criticized asset levels by type to the Board or a designated committee thereof every month; and
- (b) specific plans for the reduction of criticized assets by asset type with target reductions by month.

(3) The Board's compliance with Paragraph (2) of this Article shall include the development of procedures for the monthly review and preparation of written determinations by the Board or a designated committee thereof regarding the effectiveness of the responsible officer's efforts to eliminate the weaknesses in each criticized credit relationship totaling one hundred thousand dollars (\$100,000) or more, and that require the preparation of Problem Asset Reports ("PARs" or "PAR") that contain, at a minimum, analysis and documentation of the following:

- (a) an identification of the expected sources of repayment and an analysis of their adequacy;
- (b) the appraised value of supporting collateral and the position of the Bank's lien on such collateral where applicable as well as other necessary documentation to support the collateral valuation;
- (c) an analysis of current and satisfactory credit information, including cash flow analysis where loans are to be repaid from operations;
- (d) the proposed action to eliminate the basis of criticism and the time frame for its accomplishment;
- (e) trigger dates for positive borrower actions or for loan officers to reassess the strategy and enact collection plans;

- (f) a determination of whether the loan is impaired and the amount of the impairment, consistent with FASB Statement of Financial Accounting Standards No. 114, Accounting by Creditors for Impairment of a Loan; and
- (g) for criticized relationships totaling one hundred thousand dollars (\$100,000) or above that were made for the purpose of constructing or developing CRE, the reports shall also include:
 - (i) the initial scheduled maturity date of the loan, number of extensions and/or renewals, and current maturity date;
 - (ii) project development status;
 - (iii) a comparison of development costs to the budgeted amount;
 - (iv) a comparison of sales activity to the original sales projections;
 - (v) amount of initial interest reserve and the amount of any subsequent additions to the reserve;
 - (vi) an assessment of the borrower's global cash flow;
 - (vii) an assessment of any guarantor's global cash flow; and
 - (viii) any other significant information relating to the project.

(4) Effective as of the date of this Order, the Bank may not 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 one hundred thousand dollars (\$100,000), unless each of the following conditions is met:

- (a) the Board or a designated committee thereof 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 Board or a designated committee thereof approves the credit extension and documents in writing, the reasons that such extension is necessary to promote the best interests of the Bank; and
- (b) the Board's formal plan to collect or strengthen the criticized asset will not be compromised by the extension of credit.

Article XI

Allowance For Loan And Lease Losses

(1) Effective as of the date of this Order, the Board shall ensure adherence to written policies and procedures for maintaining an adequate Allowance for Loan and Lease Losses ("Allowance") in accordance with Generally Accepted Accounting Principles ("GAAP"). The Allowance policies and procedures shall be consistent with the guidance set forth in the Federal Financial Institutions Examination Council's "Interagency Policy Statement on the Allowance for Loan and Lease Losses" dated December 13, 2006 (OCC Bulletin 2006-47), and July 20, 2001 (OCC Bulletin 2001-37), and shall at a minimum include:

- (a) procedures for determining whether a loan is impaired and measuring the amount of impairment, consistent with all applicable accounting pronouncements;

- (b) procedures for segmenting the loan portfolio and estimating loss on groups of loans, consistent with all applicable accounting pronouncements;
- (c) procedures for validating the Allowance methodology;
- (d) procedures to ensure that the estimation of credit losses considers the relevant qualitative and environmental factors, with particular focus on the following:
 - (i) trends in the Bank's internal risk ratings, delinquent and nonaccrual loans;
 - (ii) results of the Bank's external loan review;
 - (iii) concentrations of credit in the Bank;
 - (iv) present and prospective economic conditions; and
 - (v) applicable experience of the Bank's lending staff.

(2) The program shall provide for a process for summarizing and documenting, for the Board's review and approval, the amount to be reported in the Call Reports for the Allowance. Any deficiency in the Allowance shall be remedied in the quarter it is discovered, prior to the filing of the Call Report, 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.

Article XII

Consumer Compliance Program

(1) Within thirty (30) days of this Order, the Board shall adopt, implement, and thereafter ensure adherence to a written consumer compliance program designed to ensure that

the Bank is operating in compliance with all applicable consumer protection laws, rules, and regulations. This program shall include at a minimum:

- (a) a written description of the duties and responsibilities of the Compliance officer;
- (b) adequate internal controls to ensure compliance with consumer protection laws, rules, and regulations;
- (c) the preparation of a policies and procedures manual covering all consumer protection laws, rules, and regulations for use by appropriate Bank personnel in the performance of their duties and responsibilities and specifically tailored to your deposit and lending practices;
- (d) timely updates of the written policies and procedures manual to ensure it remains current;
- (e) a formalized risk assessment process and annual audit plan to use in determining the frequency and scope of ongoing compliance monitoring and audit;
- (f) a comprehensive independent audit program to adequately test for compliance with consumer protection laws, rules and regulations;
- (g) procedures to ensure that exceptions noted in the audit reports are corrected and responded to by the appropriate Bank personnel;
- (h) the education and training of all appropriate Bank personnel in the requirements of all applicable federal and state consumer protection laws, rules and regulations;

- (i) procedures for the dissemination of changes in laws, rules, regulations and OCC policy changes to affected Bank personnel; and
 - (j) periodic reporting of the results of the consumer compliance audit to the Board or a committee thereof.
- (2) Upon adoption, a copy of the program shall be forwarded to the Assistant Deputy Comptroller.

Article XIII

BSA Program

- (1) To provide for compliance with the Bank Secrecy Act, as amended (31 U.S.C. §§ 5311 et seq.), the regulations promulgated thereunder at 31 C.F.R. Part 103, as amended, and 12 C.F.R. Part 21, Subparts B and C, and the rules and regulations of the Office of Foreign Assets Control (“OFAC”) (collectively referred to as the “Bank Secrecy Act” or “BSA”), the Board shall, within thirty (30) days of this Order, prepare and submit for a prior written determination of no supervisory objection, a revised BSA program to include, at a minimum:
- (a) the identification of the risks associated with the Bank’s products, services, customers, and geographies served;
 - (b) an evaluation of existing internal controls to mitigate the identified risks;.
 - (c) policies and procedures for the appropriate identification and monitoring of transactions that pose greater than normal risk for compliance with the Bank Secrecy Act;
 - (d) a comprehensive training program for all appropriate operational and supervisory personnel to ensure their awareness of their specific assigned

responsibilities for compliance with the requirements of the Bank Secrecy Act;

- (e) policies and procedures to provide for the Bank's monitoring of suspicious cash, monetary instruments, wire transfers, and other activities for all types of transactions, accounts, customers, products, services, and geographic areas;
- (f) policies and procedures for expanded account-opening procedures for all accounts that pose greater than normal risk for compliance with the Bank Secrecy Act;
- (g) policies and procedures for the maintenance of an integrated, accurate system for all Bank areas to produce periodic reports designed to identify unusual or suspicious activity, including patterns of activity, to monitor and evaluate unusual or suspicious activity, and to maintain accurate information needed to produce these reports;
- (h) periodic independent reviews, not less than each calendar year, of all account documentation for all high risk customers and accounts and the related accounts of those customers at the Bank to determine whether the account activity is consistent with the customer's business or occupation and the stated purpose of the account; and
- (i) an independent, internal audit program designed to ensure compliance with the Bank Secrecy Act in all areas of the Bank, to including scope, testing, and documentation.

(2) Upon receiving a written determination of no supervisory objection from the Assistant Deputy Comptroller, the Board shall immediately implement and thereafter ensure adherence to the Bank's revised BSA program.

Article XIV

Information Technology

(1) Within thirty (30) days of this Order, the Board shall revise the Bank's written Information Security Program to include an alternate processing site in the disaster recovery plan.

(2) Within thirty (30) days of the designation of an alternate backup site as required by Paragraph (1) of this Article, the Board shall take the necessary steps to ensure the alternate processing site and the disaster recovery plan are fully operational.

(3) Effective as of the date the disaster recovery plan is fully operational, the Board shall take the necessary steps to ensure compliance with the Bank's Information Security Program including the revisions required by Paragraphs (1) and (2) of this Article.

Article XV

Internal Audit

(1) Within sixty (60) days of this Order, the Board shall adopt, implement, and thereafter ensure Bank adherence to an independent and comprehensive internal audit program that:

- (a) includes procedures to assist in completing internal operations audits;
- (b) detects irregularities and weak practices in the Bank's operations;
- (c) determines the Bank's level of compliance with all applicable laws, rules and regulations;

- (d) assesses and reports the effectiveness of policies, procedures, controls, and management oversight relating to accounting and financial reporting;
- (e) evaluates the Bank's adherence to established policies and procedures;
- (f) establishes a line of communication for audit reporting issues between the internal auditor, audit committee, and board of directors;
- (g) ensures audit work papers and documentation of conclusions provide a meaningful audit trail and validation for findings and recommendations;
- (h) ensures timely management responses and corrective actions on identified weaknesses; and
- (i) establishes an annual audit plan using a risk-based approach sufficient to achieve these objectives.

(2) The Board's compliance with Paragraph (1) of this Article shall include the development of an audit policy and the performance of a Bank-wide risk assessment to guide the Bank's development of the audit scope and annual coverage.

(3) As part of the audit program required by this Article, the Board shall evaluate the audit reports of any party providing services to the Bank, and shall assess the impact on the Bank of any audit deficiencies cited in such reports.

(4) The Board shall ensure that the audit function is supported by an adequately staffed department or outside firm, with respect to both the experience level and number of the individuals employed.

(5) The Board shall ensure that the audit program is independent. The persons responsible for implementing the internal audit program described above shall report directly to the Board, which shall have the sole power to direct their activities. All reports prepared by the

audit staff shall be filed directly with the Board and/or Board Audit Committee (comprised of at least two external directors) and not through any intervening party.

(6) Upon adoption, a copy of the internal audit program shall be promptly submitted to the Assistant Deputy Comptroller.

Article XVI

External Loan Review

(1) Within thirty (30) days of this Order, the Board shall employ a qualified consultant to perform semi-annual asset quality reviews of the Bank's loan portfolio. The scope of the external loan review shall provide for a written report to be filed with the Board after each review, with the first report due no later than September 30, 2010, and shall use a loan and lease grading system consistent with the guidelines set forth in Rating Credit Risk, A-RCR, of the Comptroller's Handbook. Such reports shall, at a minimum, include comments and conclusions regarding:

- (a) the identification, type, rating, and amount of problem loans and leases;
- (b) the identification and amount of delinquent and nonaccrual loans;
- (c) the identification/status of credit related violations of law or regulation;
- (d) loans not in conformance with the Bank's lending policies;
- (e) credit underwriting and documentation exceptions;
- (f) credit analysis and documentation of such;
- (g) accuracy of internal risk ratings;
- (h) the identity of the loan officer who originated each loan reported in accordance with subparagraphs (b) through (g) of the Article;
- (i) overall credit administration practices; and

(j) completeness and effectiveness of problem loan workout plans.

(2) Prior to the appointment or employment of any individual as loan review consultant or entering into any contract with any consultant, the Board shall submit the name and qualifications of the proposed consultant and the proposed scope and terms of employment to the Assistant Deputy Comptroller for a prior written determination of no supervisory objection. After the OCC has advised the Bank that it does not take supervisory objection to the loan review consultant or the scope of the review, the Board shall immediately engage the loan review consultant pursuant to the proposed terms of the engagement.

(3) The Board or a designated committee shall review the independent loan review reports and ensure that, if appropriate, immediate, adequate, and continuing remedial action, is taken upon the findings noted in the reports.

(4) A copy of the reports submitted to the Board, as well as documentation of the action taken by the Bank to collect or strengthen assets identified as problem credits, shall be maintained in the books and records of the Bank.

(5) The Bank shall not terminate the consultant's asset quality review services without a prior written determination of no supervisory objection from the Assistant Deputy Comptroller.

Article XVII

Violations of Law

(1) The Board shall immediately take the necessary steps to ensure that Bank management corrects each violation of law, rule, or regulation, unsafe or unsound practice, or breach of fiduciary duty, cited in the ROE and in any subsequent Report of Examination or OCC

correspondence. The quarterly progress reports required by Article I of this Order shall include the date and manner in which each correction has been implemented during that reporting period.

(2) Effective as of the date of this Order, the Board shall adopt, implement, and thereafter ensure Bank adherence to specific procedures to prevent future violations, practices, and breaches 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, regulations and duties applicable to their areas of responsibility.

(3) Within sixty (60) days of receipt of any subsequent Report of Examination or other OCC correspondence which cites violations of law, rule, or regulation, unsafe or unsound practice, or breach of fiduciary duty, the Board shall adopt, implement, and thereafter ensure Bank adherence to specific procedures to prevent future citations 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, regulations, and duties applicable to their areas of responsibility.

Article XVIII

Closing

(1) Although the Bank is required to submit certain proposed actions and programs for the review or prior written determination of no supervisory objection of the Assistant Deputy Comptroller, the Board has the ultimate responsibility for proper and sound management of the Bank and the completeness and accuracy of the Bank's books and records.

(2) If, at any time, the Comptroller deems it appropriate in fulfilling the responsibilities placed upon him by the several laws of the United States to undertake any action

affecting the Bank, nothing in this Order shall in any way inhibit, estop, bar or otherwise prevent the Comptroller from so doing.

(3) The provisions of this Order shall remain effective and enforceable, except to the extent that, and until such time as, any provisions of this Order shall have been amended, suspended, waived, or terminated in writing by the Comptroller.

(4) In each instance in this Order in which the Bank or the Board is required to ensure implementation of or adherence to, or to undertake to perform, an obligation of the Bank, the Board shall:

- (a) authorize and adopt such actions on behalf of the Bank as may be necessary or appropriate for the Bank to perform its obligations under this Order;
- (b) require the timely reporting by Bank management of such actions directed by the Board to be taken under the terms of this Order;
- (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 for any non-compliance with such actions.

(5) This Order is intended to be, and shall be construed to be, a final order issued pursuant to 12 U.S.C. § 1818(b), and expressly does not form, and may not be construed to form, a contract binding the Comptroller or the United States.

(6) The terms of this Order, 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 has hereunto set his hand.

/s/

6/23/2010

Richard S. Dixon, Jr.
Assistant Deputy Comptroller
Southern California–North Field Office

Date

**UNITED STATES OF AMERICA
DEPARTMENT OF THE TREASURY
COMPTROLLER OF THE CURRENCY**

In the Matter of:)	
Merchants Bank of California, National Association)	AA-WE-10-37
Carson, California)	

**STIPULATION AND CONSENT TO THE
ISSUANCE OF A CONSENT ORDER**

The Comptroller of the Currency of the United States of America (“Comptroller”) intends to initiate cease and desist proceedings against Merchants Bank of California, National Association, Carson, California (“Bank”), pursuant to 12 U.S.C. § 1818(b) through the issuance of a Notice of Charges for an Order to Cease and Desist for unsafe and unsound banking practices relating to the Bank’s Board and management oversight, credit risk management, loans to insiders and affiliates, liquidity management, and Consumer and BSA compliance.

The Bank, in the interest of compliance and cooperation, consents to the issuance of a Consent Order, dated June 22, 2010 (the “Order”);

In consideration of the above premises, the Comptroller, through his authorized representative, and the Bank, through its duly elected and acting Board of Directors, hereby stipulate and agree to the following:

Article I

Jurisdiction

- (1) The Bank is a national banking association chartered and examined by the Comptroller pursuant to the National Bank Act of 1864, as amended, 12 U.S.C. § 1 et seq.
- (2) The Comptroller is “the appropriate Federal banking agency” regarding the Bank

pursuant to 12 U.S.C. §§ 1813(q) and 1818(b).

(3) The Bank is an “insured depository institution” within the meaning of 12 U.S.C. § 1818(b)(1).

Article II

Agreement

(1) The Bank, without admitting or denying any wrongdoing, hereby consents and agrees to the issuance of the Order by the Comptroller.

(2) The Bank further agrees that said Order shall be deemed an “order issued with the consent of the depository institution” as defined in 12 U.S.C. § 1818(h)(2), and consents and agrees that said Order shall become effective upon its issuance and shall be fully enforceable by the Comptroller under the provisions of 12 U.S.C. § 1818(i). Notwithstanding the absence of mutuality of obligation, or of consideration, or of a contract, the Comptroller may enforce any of the commitments or obligations herein undertaken by the Bank under his supervisory powers, including 12 U.S.C. § 1818(i), and not as a matter of contract law. The Bank expressly acknowledges that neither the Bank nor the Comptroller has any intention to enter into a contract.

(3) The Bank also expressly acknowledges that no officer or employee of the Comptroller has statutory or other authority to bind the United States, the U.S. Treasury Department, the Comptroller, or any other federal bank regulatory agency or entity, or any officer or employee of any of those entities to a contract affecting the Comptroller’s exercise of his supervisory responsibilities.

Article III

Waivers

- (1) The Bank, by signing this Stipulation and Consent, hereby waives:
 - (a) the issuance of a Notice of Charges pursuant to 12 U.S.C. § 1818(b);
 - (b) any and all procedural rights available in connection with the issuance of this Order;
 - (c) all rights to a hearing and a final agency decision with regard to the issuance of this Order pursuant to 12 U.S.C. § 1818(i), 12 C.F.R. Part 19;
 - (d) all rights to seek any type of administrative or judicial review with regard to the issuance of this Order; and
 - (e) any and all rights to challenge or contest the validity of the Order.

Article IV

Other Action

- (1) The Bank agrees that the provisions of this Stipulation and Consent shall not inhibit, estop, bar, or otherwise prevent the Comptroller from taking any other action affecting the Bank if, at any time, it deems it appropriate to do so to fulfill the responsibilities placed upon him by the several laws of the United States of America.

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

<u>/s/</u> Richard S. Dixon, Jr. Assistant Deputy Comptroller Southern California–North Field Office	<u>6/23/2010</u> Date
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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.

<u>/s/</u> Rod Garza	<u>6/22/2010</u> Date
<u>/s/</u> Janice Hall	<u>6/22/2010</u> Date
<u>/s/</u> Daniel Roberts	<u>6/22/2010</u> Date
<u>/s/</u> Theodore K. Roberts	<u>6/22/2010</u> Date
<u>/s/</u> Philip Scott	<u>6/22/2010</u> Date
<u>/s/</u> Dale Young	<u>6/22/2010</u> Date
<u>/s/</u> Arnold Coggeshall	<u>6/22/2010</u> Date