

UNITED STATES OF AMERICA
BEFORE THE
BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D.C.

STATE OF MARYLAND
COMMISSIONER OF FINANCIAL REGULATION
BALTIMORE, MARYLAND

Written Agreement by and among

BANK OF THE EASTERN SHORE
Cambridge, Maryland

FEDERAL RESERVE BANK
OF RICHMOND
Richmond, Virginia

and

STATE OF MARYLAND
COMMISSIONER OF FINANCIAL
REGULATION
Baltimore, Maryland

Docket No. 10-161-WA/RB-SM

WHEREAS, in recognition of their common goal to maintain the financial soundness of the Bank of the Eastern Shore, Cambridge, Maryland (the “Bank”), a state-chartered bank that is a member of the Federal Reserve System, the Bank, the Federal Reserve Bank of Richmond (the “Reserve Bank”), and the State of Maryland Commissioner of Financial Regulation (the “Commissioner”) have mutually agreed to enter into this Written Agreement (the “Agreement”); and

WHEREAS, on August 12, 2010, the board of directors of the Bank, at a duly constituted meeting, adopted a resolution authorizing and directing Harold S. Robbins to enter into this Agreement on behalf of the Bank, and consenting to compliance with each and

every provision of this Agreement by the Bank and its institution-affiliated parties, as defined in Section 3(u) of the Federal Deposit Insurance Act, as amended (the “FDI Act”)(12 U.S.C. § 1813(u)).

NOW, THEREFORE, the Bank, the Reserve Bank, and the Commissioner agree as follows:

Board Oversight

1. Within 60 days of this Agreement, the board of directors of the Bank shall submit to the Reserve Bank and the Commissioner a written plan to strengthen board oversight of the management and operations of the Bank. The plan shall, at a minimum, address, consider, and include:

(a) The actions that the board of directors will take to improve the Bank’s condition and maintain effective control over, and supervision of, the Bank’s senior management and major operations and activities, including but not limited to, lending and credit administration, loan grading and loan review, capital, liquidity, and earnings;

(b) the responsibility of the board of directors to monitor management’s adherence to approved Bank policies and procedures, and to require management to document exceptions thereto;

(c) a description of the information and reports that will be regularly reviewed by the board of directors in its oversight of the operations and management of the Bank, including information on the Bank’s adversely classified assets, allowance for loan and lease losses (“ALLL”), capital, earnings, and liquidity;

(d) steps to enhance board and committee minutes;

(e) the responsibility of the board of directors to consistently attend scheduled meetings; and

(f) a formal management succession plan.

New Management

2. Within 60 days of this Agreement, the Bank shall take such actions as are necessary to employ a permanent full-time chief lending officer with demonstrated knowledge and experience in the management and operations of a bank, and in connection, therewith, shall comply with the notice provisions of Section 32 of the FDI Act (12 U.S.C. § 1831i) and Subpart H of Regulation Y of the Board of Governors (12 C.F.R. §§ 225.71 *et seq.*).

Credit Risk Management

3. Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Commissioner an acceptable written plan to strengthen credit risk management practices.

The plan shall, at a minimum, address, consider, and include:

(a) The responsibility of the board of directors to establish appropriate risk limits;

(b) periodic review and revision of risk limits to address changes in market conditions;

(c) timely and accurate identification and quantification of credit risk within the loan portfolio;

(d) strategies to minimize credit losses and reduce the level of problem assets;

and

(e) management's monitoring and resolution of problem assets.

Lending and Credit Administration

4. Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Commissioner an acceptable revised plan to strengthen the Bank's lending and credit administration practices that shall, at a minimum, address, consider, and include:

- (a) Evaluation of aggregate cash flow and alternative repayment sources when assessing the financial strength of a borrower or guarantor;
- (b) procedures for the periodic analyses during the term of the loan of:
 - (i) the borrower's repayment sources, global cash flow, and overall debt service ability; and
 - (ii) the value of any collateral;
- (c) standards for interest-only loans;
- (d) establishment of loan workout practices consistent with the Interagency Policy Statement on Prudent Commercial Real Estate Loan Workouts, dated October 30, 2009 (SR 09-7);
- (e) procedures for approving and monitoring technical exceptions; and
- (f) timely and accurate reporting of nonaccrual loans and troubled debt restructurings.

Loan Documentation

5. Within 60 days of this Agreement, the Bank shall take all steps necessary to correct the documentation and credit information deficiencies in the Bank's loan files listed in the report of examination commencing February 22, 2010 and conducted by the Reserve Bank and the Commissioner ("Report of Examination"). In all cases where the Bank is unable to obtain needed documentation or credit information, the Bank shall document the actions taken to

secure the information and the reasons the information could not be obtained. The Bank shall maintain this documentation in the related credit file for supervisory review.

Loan Grading and Loan Review

6. Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Commissioner an acceptable written program for the effective grading of the Bank's loan portfolio. The program shall provide for policies, procedures, and processes for the timely and ongoing grading of loans. The program shall, at a minimum, address, consider, and include:

- (a) Standards and criteria for assessing the credit quality of loans, including a discussion of the factors used to assign appropriate risk grades to loans;
- (b) procedures for the early identification of problem loans;
- (c) procedures to re-evaluate the grading of loans in the event of material changes in the borrower's performance or the value of the collateral;
- (d) procedures to evaluate the grading of all loans assigned less than a pass grade at least quarterly;
- (e) designation of the person(s) responsible for the grading of loans;
- (f) controls to ensure staff's consistent application and adherence to the loan grading system; and
- (g) a mechanism for reporting to senior management and the board of directors, at least monthly, that at a minimum: summarizes the Bank's loan grades; describes trends in asset quality; identifies the loans that are nonperforming, adversely graded, or identified as needing special attention, describes the status of those loans, and describes the actions taken, or to be taken, by management for strengthening of the quality of any such loans.

7. Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Commissioner an acceptable written program for the effective, ongoing review of the Bank's loan portfolio by a qualified independent party or by qualified staff that is independent of the Bank's lending function. The program shall provide for policies and procedures for the timely identification and categorization of problem loans, and processes to detect weaknesses in the Bank's loan approval, monitoring, and grading process. The program shall, at a minimum, address, consider, and include:

- (a) The scope, depth, and frequency of the independent loan review;
- (b) clearly defined responsibilities for the loan review function; and
- (c) an objective and timely assessment of the overall quality of the loan portfolio and the accuracy of assigned loan grades.

8. The board of directors, or a committee thereof, shall evaluate the loan review report(s) and take appropriate steps to ensure that management takes prompt action to address findings noted in the report(s).

Appraisal and Appraisal Review Program

9. Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Commissioner an acceptable written program for real estate appraisals and appraisal reviews that shall, at a minimum, address, consider, and include:

- (a) Procedures to ensure that appraisals conform to accepted appraisal standards, as defined in the Uniform Standards of Professional Appraisal Practice, and comply with the requirements of Subpart G of Regulation Y of the Board of Governors of the Federal Reserve System (the "Board of Governors") (12 C.F.R. Part 225, Subpart G) made applicable to state member banks by Section 208.50 of Regulation H of the Board of Governors

(12 C.F.R. § 208.50), and the Interagency Appraisal and Evaluation Guidelines, dated October 27, 1994 (SR 94-55);

(b) procedures to ensure that appraisals are conducted by an independent party selected from the Bank's approved list of appraisers;

(c) written standards for when reappraisals and reevaluations must be conducted, including, but not limited to, when new funds are advanced or when changes in market conditions or the condition of the collateral or project occur; and

(d) enhanced appraisal review procedures to ensure the quality and timeliness of appraisals.

Asset Improvement

10. The Bank shall not, directly or indirectly, extend, renew, or restructure any credit to or for the benefit of any borrower, including any related interest of the borrower, whose loans or other extensions of credit are criticized in the Report of Examination or in any subsequent report of examination, without the prior approval of a majority of the full board of directors or a designated committee thereof. The board of directors or its committee shall document in writing the reasons for the extension of credit, renewal, or restructuring, specifically certifying that: (i) the Bank's risk management policies and practices for loan workout activity are acceptable; (ii) the extension of credit is necessary to improve and protect the Bank's interest in the ultimate collection of the credit already granted and maximize its potential for collection; (iii) the extension of credit reflects prudent underwriting based on reasonable repayment terms and is adequately secured; and all necessary loan documentation has been properly and accurately prepared and filed; (iv) the Bank has performed a comprehensive credit analysis indicating that the borrower has the willingness and ability to repay the debt as supported by an adequate

workout plan, as necessary; and (v) the board of directors or its designated committee reasonably believes that the extension of credit will not impair the Bank's interest in obtaining repayment of the already outstanding credit and that the extension of credit or renewal will be repaid according to its terms. The written certification shall be made a part of the minutes of the meetings of the board of directors or its committee, as appropriate, and a copy of the signed certification, together with the credit analysis and related information that was used in the determination, shall be retained by the Bank in the borrower's credit file for subsequent supervisory review. For purposes of this Agreement, the term "related interest" is defined as set forth in Section 215.2(n) of Regulation O of the Board of Governors (12 C.F.R. § 215.2(n)).

11. (a) Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Commissioner an acceptable written plan designed to improve the Bank's position through repayment, amortization, liquidation, additional collateral, or other means on each loan or other asset in excess of \$250,000, including other real estate owned ("OREO"), that: (i) is past due as to principal or interest more than 90 days as of the date of this Agreement; (ii) is on the Bank's problem loan list; or (iii) was adversely classified in the Report of Examination. In developing the plan for each loan, the Bank shall, at a minimum, review, analyze, and document the financial position of the borrower, including source of repayment, repayment ability, and alternative repayment sources, as well as the value and accessibility of any pledged or assigned collateral, and any possible actions to improve the Bank's collateral position.

(b) Within 30 days of the date that the Bank acquires OREO or that any additional loan, relationship, or other asset in excess of \$250,000 becomes past due as to principal or interest for more than 90 days, is on the Bank's problem loan list, or is adversely classified in any subsequent report of examination of the Bank, the Bank shall submit to the

Reserve Bank and the Commissioner an acceptable written plan to improve the Bank's position on such loan, relationship, or asset.

(c) Within 30 days after the end of each calendar quarter thereafter, the Bank shall submit a written progress report to the Reserve Bank and the Commissioner to update each asset improvement plan, which shall include, at a minimum, the carrying value of the loan or other asset and changes in the nature and value of supporting collateral, along with a copy of the Bank's current problem loan list, a list of all loan renewals and extensions without full collection of interest in the last quarter, and past due/non-accrual report.

Allowance for Loan and Lease Losses

12. (a) Within 10 days of this Agreement, the Bank shall eliminate from its books, by charge-off or collection, all assets or portions of assets classified "loss" in the Report of Examination that have not been previously collected in full or charged off. Thereafter the Bank shall, within 30 days from the receipt of any federal or state report of examination, charge off all assets classified "loss" unless otherwise approved in writing by the Reserve Bank and the Commissioner.

(b) Within 60 days of this Agreement, the Bank shall review and revise its ALLL methodology consistent with relevant supervisory guidance, including the Interagency Policy Statements on the Allowance for Loan and Lease Losses, dated July 2, 2001 (SR 01-17 (Sup)) and December 13, 2006 (SR 06-17), and the findings and recommendations regarding the ALLL set forth in the Report of Examination, and submit a description of the revised methodology to the Reserve Bank and the Commissioner. The revised ALLL methodology shall be designed to maintain an adequate ALLL and shall address, consider, and include, at a minimum, the reliability of the Bank's loan grading system, the volume of criticized loans,

concentrations of credit, the current level of past due and nonperforming loans, past loan loss experience, evaluation of probable losses in the Bank's loan portfolio, including adversely classified loans, and the impact of market conditions on loan and collateral valuations and collectability.

(c) Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Commissioner an acceptable written program for the maintenance of an adequate ALLL. The program shall include policies and procedures to ensure adherence to the revised ALLL methodology and provide for periodic reviews and updates to the ALLL methodology, as appropriate. The program shall also provide for a review of the ALLL by the board of directors on at least a quarterly calendar basis. Any deficiency found in the ALLL shall be remedied in the quarter it is discovered, prior to the filing of the Consolidated Reports of Condition and Income, by additional provisions. The board of directors shall maintain written documentation of its review, including the factors considered and conclusions reached by the Bank in determining the adequacy of the ALLL. During the term of this Agreement, the Bank shall submit to the Reserve Bank and the Commissioner, within 30 days after the end of each calendar quarter, a written report regarding the board of directors' quarterly review of the ALLL and a description of any changes to the methodology used in determining the amount of ALLL for that quarter.

Capital Plan

13. Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Commissioner an acceptable written plan to maintain sufficient capital at the Bank. This plan shall, at a minimum, address, consider, and include:

(a) The Bank's current and future capital needs, including compliance with the Capital Adequacy Guidelines for State Member Banks: Risk-Based Measure and Tier 1

Leverage Measure, Appendices A and B of Regulation H of the Board of Governors (12 C.F.R. Part 208, App. A and B);

(b) the adequacy of the Bank's capital, taking into account the volume of classified credits, concentrations of credit, ALLL, current and projected asset growth, and projected retained earnings; and

(c) the source and timing of additional funds to fulfill the Bank's future capital requirements.

14. The Bank shall notify the Reserve Bank and the Commissioner, in writing, no more than 30 days after the end of any quarter in which any of the Bank's capital ratios (total risk-based, Tier 1, or leverage) fall below the approved capital plan's minimum ratios. Together with the notification, the Bank shall submit an acceptable written plan that details the steps the Bank will take to increase its capital ratios to or above the approved capital plan's minimums.

Liquidity and Funds Management

15. Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Commissioner an acceptable revised written contingency funding plan that, at a minimum, identifies available sources of liquidity and includes adverse scenario planning.

Business Plan and Budget

16. (a) Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Commissioner a written business plan for 2011 to improve the Bank's earnings and overall condition. The plan, at a minimum, shall provide for or describe:

(i) a realistic and comprehensive budget for 2011 including income statement and balance sheet projections; and

(ii) a description of the operating assumptions that form the basis for, and adequately support, major projected income, expense, and balance sheet components.

(b) During the term of this Agreement, a business plan and budget for each calendar year subsequent to 2011 shall be submitted to the Reserve Bank and the Commissioner at least 60 days prior to the beginning of that calendar year.

Dividends

17. (a) The Bank shall not declare or pay any dividends without the prior written approval of the Reserve Bank, the Director of the Division of Banking Supervision and Regulation of the Board of Governors, and the Commissioner.

(b) Any request to declare or pay dividends must be consistent with the Board of Governors' Policy Statement on the Payment of Cash Dividends by State Member Banks and Bank Holding Companies, dated November 14, 1985 (Federal Reserve Regulatory Service, 4-877 at page 4-323) and Maryland Code Annotated Financial Institutions §3-307 Cash Dividends, and §3-308 Stock Dividends. All requests for prior approval shall be received by the Reserve Bank and the Commissioner at least 30 days prior to the proposed dividend declaration date and shall contain, at a minimum, current and projected information on earnings, capital, asset quality, and loan loss reserve needs of the Bank.

Compliance with Laws and Regulations

18. The Bank shall immediately take all necessary steps to correct all violations of law and regulation cited in the Report of Examination. In addition, the board of directors of the Bank shall take the necessary steps to ensure the Bank's future compliance with all applicable laws and regulations.

19. In appointing any new director or senior executive officer, or changing the responsibilities of any senior executive officer so that the officer would assume a different senior executive officer position, the Bank shall comply with the notice provisions of Section 32 of the FDI Act and Subpart H of Regulation Y of the Board of Governors.

20. The Bank shall comply with the restrictions on indemnification and severance payments of Section 18(k) of the FDI Act (12 U.S.C. § 1828(k)) and Part 359 of the Federal Deposit Insurance Corporation's regulations (12 C.F.R. Part 359).

Compliance with the Agreement

21. (a) Within 10 days of this Agreement, the board of directors of the Bank shall appoint a committee (the "Compliance Committee") to monitor and coordinate the Bank's compliance with the provisions of this Agreement. The Compliance Committee shall include a majority of outside directors who are not executive officers or principal shareholders of the Bank, as defined in Sections 215.2(e)(1) and 215.2 (m)(1) of Regulation O of the Board of Governors (12 C.F.R. §§ 215.2(e)(1) and 215.2(m)(1)). At a minimum, the Compliance Committee shall meet at least monthly, keep detailed minutes of each meeting, and report its findings to the board of directors of the Bank.

(b) Within 30 days after the end of each calendar quarter following the date of this Agreement, the Bank shall submit to the Reserve Bank and the Commissioner written progress reports detailing the form and manner of all actions taken to secure compliance with this Agreement and the results thereof.

Approval and Implementation of Plans and Programs

22. (a) The Bank shall submit written plans, programs, and an engagement letter that are acceptable to the Reserve Bank and the Commissioner within the applicable time periods set forth in paragraphs 3, 4, 6, 7, 9, 11(a), 11(b), 12(c), 13, 14, and 15 of this Agreement.

(b) Within 10 days of approval by the Reserve Bank and the Commissioner, the Bank shall adopt the approved plans and programs. Upon adoption, the Bank shall promptly implement the approved plans and programs and thereafter fully comply with them.

(c) During the term of this Agreement, the approved plans and programs shall not be amended or rescinded without the prior written approval of the Reserve Bank and the Commissioner.

Communications

23. All communications regarding this Agreement shall be sent to:

- (a) Eugene W. Johnson, Jr.
Vice President
Federal Reserve Bank of Richmond
P.O. Box 27622
Richmond, VA 23261-7622
- (b) Teresa M. Louro
Assistant Commissioner for Bank Supervision
State of Maryland Commissioner of Financial Regulation
500 North Calvert Street
Room 402
Baltimore, Maryland 21202
- (c) Harold S. Robbins
Chairman of the Board and President
Bank of the Eastern Shore
301 Crusader Road
Cambridge, Maryland 21613

Miscellaneous

24. Notwithstanding any provision of this Agreement, the Reserve Bank and the Commissioner may, in their sole discretion, grant written extensions of time to the Bank to comply with any provision of this Agreement.

25. The provisions of this Agreement shall be binding upon the Bank and its institution-affiliated parties, in their capacities as such, and their successors and assigns.

26. Each provision of this Agreement shall remain effective and enforceable until stayed, modified, terminated, or suspended in writing by the Reserve Bank and the Commissioner.

27. The provisions of this Agreement shall not bar, estop, or otherwise prevent the Board of Governors, the Reserve Bank, the Commissioner, or any other federal or state agency from taking any other action affecting the Bank or any of their current or former institution-affiliated parties and their successors and assigns.

28. Pursuant to Section 50 of the FDI Act (12 U.S.C. § 1831aa), this Agreement is enforceable by the Board of Governors under Section 8 of the FDI Act (12 U.S.C. § 1818).

IN WITNESS WHEREOF, the parties have caused this Agreement to be executed as of the 31st day of August, 2010.

BANK OF THE EASTERN SHORE

By: /s/ Harold S. Robbins

FEDERAL RESERVE BANK OF
RICHMOND

By: /s/ Eugene W. Johnson, Jr.
Eugene W. Johnson, Jr.
Vice President

STATE OF MARYLAND
COMMISSIONER OF FINANCIAL
REGULATION

By: /s/ Teresa M. Louro
Teresa M. Louro
Assistant Commissioner