

UNITED STATES OF AMERICA

BEFORE

THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

WASHINGTON, D.C.

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Written Agreement by and among )  
 )  
FIRST SECURITY BANCSHARES, INC. )  
Lake Park, Iowa )  
 )  
SECURITY STATE BANK ) Docket Nos. 99-015-WA/RB-BHC  
Milford, Iowa ) 99-015-WA/RB-SMB  
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FEDERAL RESERVE BANK OF CHICAGO )  
Chicago, Illinois )  
\_\_\_\_\_ )

WHEREAS, in recognition of their common goal to restore and maintain the financial soundness of First Security Bancshares, Inc., Lake Park, Iowa ("Bancshares"), a registered bank holding company, and Bancshares's subsidiary, the Security State Bank, Milford, Iowa (the "Bank"), a State chartered bank that is a member of the Federal Reserve System, Bancshares, the Bank, and the Federal Reserve Bank of Chicago (the "Reserve Bank"), have mutually agreed to enter into this Written Agreement (the "Agreement");

WHEREAS, this Agreement is being executed in accordance with the Rules Regarding Delegation of Authority of the Board of Governors of the Federal Reserve System (the "Board of Governors"), specifically 12 C.F.R. 265.11(a)(15), and the Reserve Bank has received the prior approval of the Director of the Division of Banking Supervision and Regulation (the "Director") and the General Counsel of the Board of Governors to enter into this Agreement with Bancshares and the Bank; and

WHEREAS, on August 6, 1999, the boards of directors of Bancshares and the Bank, at duly constituted meetings, adopted resolutions authorizing and directing their boards to enter into this Agreement on behalf of Bancshares and the Bank, respectively, and consented to compliance with each and every applicable provision of this Agreement by Bancshares and the Bank and their institution-affiliated parties, as defined in sections 3(u) and 8(b)(3) of the Federal Deposit Insurance Act, as amended (the "FDI Act") (12 U.S.C. 1813 (u) and 1818 (b)(3)).

NOW, THEREFORE, before the taking of any testimony or adjudication of or finding on any issue of fact or law herein, and without this Agreement constituting an admission of any allegation made or implied by the Board of Governors or the Reserve Bank, and solely for the purpose of settling this matter without further proceedings, Bancshares, the Bank and the Reserve Bank hereby agree as follows:

1. Bancshares and the Bank shall not declare or pay any dividends without the prior written approval of the Reserve Bank and the Director. Requests for approval shall be received by the Reserve Bank at least 30 days prior to the proposed dividend declaration date and shall contain, but not be limited to, current and projected information on earnings, cash flow, capital levels, and asset quality of the Bank.

2. Bancshares shall not, directly or indirectly, increase its borrowings or incur any debt without the prior written approval of the Reserve Bank. All requests for prior written approval shall contain, but not be limited to, a statement regarding the purpose of the debt, the terms of the debt, and the planned source(s) for debt repayment and an analysis of the cash flow resources available to meet such debt repayment.

3. Bancshares shall not, directly or indirectly, purchase or redeem any of its stock or make, affirm, or ratify any commitment to purchase or redeem any of its stock without the prior written approval of the Reserve Bank.

4. (a) Bancshares shall not, directly or indirectly, enter into, participate, or in any other manner engage in any financial transaction with the Bank or any institution-affiliated party of Bancshares or the Bank or any related interest thereof. In addition, Bancshares shall not make any cash payments of any nature in excess of \$250 to any individual or entity without the prior written approval of the Reserve Bank.

(b) Any request for prior approval pursuant to this paragraph shall be accompanied by documentation adequate to provide the Reserve Bank with the details of each proposed payment or transaction, including a full description of the proposal, the purpose for the payment or transaction, the amounts involved, the benefits to be derived by Bancshares or the Bank and other such matters that may be pertinent.

(c) For the purposes of this Agreement, the terms:

(i) "Financial transaction" shall include, but is not limited to: an extension of credit (as defined in section 215.3 of Regulation O of the Board of Governors (12 CFR 215.3)), the payment of money, a contract or payment for services, or the direct or indirect payment of any obligation of, on behalf of, or for the benefit of any institution-affiliated party of Bancshares or the Bank or any related interest thereof; and (ii) "related interest" shall be defined as set forth in section 215.2(n) of Regulation O of the Board of Governors (12 CFR 215.2(n)).

5. (a) By September 20, 1999, the Bank's board of directors shall conduct a review of the functions and performance of the officers of the Bank, and shall forward to the Reserve Bank its written findings and conclusions along with a written description of any management changes that may be proposed as a result of the review. The review shall focus on an assessment of the duties performed by each officer and the ability of each officer to perform competently his or her assigned duties. The primary purpose of this review shall be to aid in the development of a management structure that is suitable to the Bank's needs and is adequately staffed by qualified and trained personnel. At a minimum, the qualifications of management shall be assessed for its ability to restore and maintain all aspects of the Bank to a safe and sound condition, and comply with the requirements of this Agreement. The review shall also include, at a minimum, the following:

(i) Identification of both the type and number of officer positions needed to manage properly and supervise the lending function of the Bank;

(ii) an evaluation of each officer to determine whether the individual possesses the ability, experience and other qualifications required to perform present and anticipated duties, including the ability to provide appropriate oversight of the lending function, to adhere to the Bank's established policies and procedures, and to restore and maintain the Bank in a safe and sound condition; and

(iii) a plan of action to recruit, hire, or appoint any additional or replacement personnel with the requisite ability, experience and other qualifications of those officer positions identified as a result of the review required by paragraph 5(a) of this Agreement.

(b) Prior to the election or appointment of any director or senior executive officer during the term of this Agreement, the Bank shall provide notice to the Reserve Bank of such election or appointment as required by Subpart H of Regulation Y of the Board of Governors (12 C.F.R. 225, Subpart H).

6. Within 30 days of this Agreement, Bancshares and the Bank shall submit to the Reserve Bank an acceptable joint written plan to maintain a satisfactory capital position for the Bank. The plan shall, at a minimum, address and consider: (a) the Bank's current and future capital requirements, including compliance with the Capital Adequacy Guidelines of the Board of Governors for State Member Banks, Risk Based Measures and Tier 1 Leverage Measures (12 C.F.R. Part 208, App. A and B); (b) the volume of the Bank's adversely classified assets; (c) the Bank's anticipated level of retained earnings; (d) the growth of the Bank's assets and its relationship to the Bank's capital ratios; and (e) the source and timing of additional funds to fulfill the Bank's future capital requirements, considering the Bank's level of concentrations of credit and the adequacy of the allowance for loan and lease losses.

7. By September 20, 1999, the Bank shall submit to the Reserve Bank acceptable revised written loan policies and procedures to address all aspects of the Bank's current or planned future lending activities. The revised loan policies and procedures shall include, at a minimum:

(a) underwriting standards for all loans; (b) guidelines for a credit and cash flow analysis to be performed on each new extension of credit as well as renewals or extensions of existing loan accounts, to permit full assessment of the borrower's financial capacity and the documentation of such analysis; (c) requirements for preparing a written analysis of each proposed extension of credit in excess of \$50,000, including, without limitation, source of repayment, collateral value and verification, character of the borrower, the borrower's financial condition, and a review of the proposed extension of credit's compliance with the Bank's loan policies and procedures, as amended pursuant to this Agreement; (d) guidelines on the collateral requirements for all loans; (e) credit approval limits for Bank lending officers and procedures for subsequent review by the board of directors; and (f) the prohibition of capitalizing interest earned but not collected for extensions of credit that are being renewed, extended, modified, or in any way renegotiated.

8. By September 20, 1999, the Bank shall develop and submit to the Reserve Bank acceptable written loan review procedures designed to identify and categorize problem credits and provide work-out strategies for minimizing the Bank's risk exposure from these identified problem credits and assess the overall quality of the Bank's loan portfolio. The loan review procedures shall, at a minimum, include the following: (a) a detailed description of the risk grades to be assigned to each loan; (b) the designation of the individual(s) responsible for determining initial loan grades; (c) the timing of the assignment of the loan grades; (d) the types and dollar amounts of loans that will be graded; (e) the requirements outlined in Attachment 1 of the Interagency Policy Statement on the Allowance for Loans and Lease Losses, issued December 21, 1993, addressing the minimum requirements relating to "Loan Review Systems" and "Credit Grading;" (f) development of an adequate internal loan review grading report detailing the number of credits and dollar amounts by grade; (g) development of an internal Watch List for all extensions of credit adversely classified, past due 90 days or more, or possessing, in the judgment of Bank management, more than a normal degree of risk; (h) procedures requiring that all loans adversely classified by examiners at future examinations and visitations be incorporated into the Bank's loan review program and listed on the Bank's Watch List; and (i) a mechanism for reporting quarterly to the Bank's board of directors the status of each Watch List item and the action(s) taken by Bank management to improve the Bank's position on each Watch List item.

9. By October 20, 1999, the Bank shall take all necessary steps to correct all documentation and credit information deficiencies in the Bank's loan files identified in the State of Iowa Division of Bank's Report of Examination, dated March 10, 1999, (the "Report of Examination"), including, but not limited to, obtaining accurate and current financial and cash flow statements and appraisals on credits lacking such information.

10. (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 previously been collected in full or charged off.

(b) The Bank shall continue to maintain, through charges to current operating income, an adequate allowance for loan and lease losses (the "ALLL"). The adequacy of the ALLL shall be determined in light of the current level of nonperforming loans, the current level of concentrations of credit within the loan portfolio of the Bank, past loss experience, evaluation of the potential for losses in the loan portfolio of the Bank, current economic conditions and examiners criticisms or other comments contained in the Report of Examination and any subsequent report of examination, and the Requirements of the Interagency Policy Statement on the Allowance for Loan and Leases Losses, dated December 21, 1993. A written record shall be maintained indicating the methodology used in determining the amount of the ALLL needed.

11. The Bank shall not, directly or indirectly, (a) extend any additional credit to or for the benefit of any borrower, including any related interest of the borrower, who is obligated in any manner to the Bank on any extension of credit or portion thereof that has been charged off by the Bank or classified "Loss" in the Report of Examination or in any subsequent report of examination, as long as such credit remains uncollected; and (b) extend any additional credit to any borrower whose line of credit has been classified "Doubtful" or "Substandard" in the Report of Examination or in any subsequent report of examination, without the prior approval of the Bank's board of directors, which shall document the reasons for the additional advances, specifically certifying that: (i) the additional extension of credit is necessary to protect the Bank's interest in the ultimate collection of the credit already granted; or (ii) the additional credit is in full compliance with the Bank's written loan policy and the Bank's legal lending limit, and is adequately secured, a thorough credit analysis has been performed indicating that the additional extension of credit is reasonable and justified, all necessary documentation (including title and lien documents) have been properly and accurately reported and filed, and that the Bank has a satisfactory appraisal of the collateral supporting the extension of credit, that the extension will not impair the Bank's interest in obtaining repayment of the already outstanding credit, and the board of directors reasonably believes that the additional extension of credit will be repaid according to its terms. The board of directors' certification, together with the credit analysis and related information that was used in the determination, shall be maintained by the Bank for subsequent supervisory review.

12. By August 20, 1999, the Bank shall submit to the Reserve Bank an acceptable written plan designed to improve the Bank's position on each loan in excess of \$25,000 that was past due as to principal or interest in excess of 90 days as of the date of this Agreement and on each asset in excess of \$25,000, including other real estate, that was adversely classified or listed as special mention by examiners in the Report of Examination, through amortization, repayment, liquidation, additional collateral or other means, whichever may be appropriate. This plan shall not be amended or rescinded without the prior written approval of the Reserve Bank, except that the plan shall be amended periodically to cover loans or other assets in excess of \$25,000 that have been adversely classified or listed for special mention in any subsequent report of examination or visitation of the Bank or loans that are past due as to principal or interest for more than 90 days as of the date of each subsequent examination or visitation.

13. Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank an acceptable written policy and procedures to monitor, control and reduce concentrations of credit in the Bank's portfolio, as identified in the Report of Examination.

14. (a) The Bank shall immediately take all necessary steps consistent with sound banking practices, to eliminate and/or correct all violations of State and Federal laws, rules, and regulations cited in the Report of Examination and sections 215.4 and 215.5 of Regulation O of the Board of Governors (12 C.F.R. 215.4 and 215.5) and section 23A of the Federal Reserve Act (12 U. S. C. 371c).

(b) The Bank shall not engage, directly or indirectly, in any violation of State and Federal laws, rules and regulations cited in the Report of Examination or sections 215.4 and 215.5 of Regulation O and section 23A of the Federal Reserve Act (12 U. S. C. 371c).

15. (a) By August 20, 1999, the Bank shall submit to the Reserve Bank a written strategic plan for the remainder of 1999 and for 2000, consisting of goals and strategies for improving the earnings of the Bank, which shall include, but not be limited to, the identification of the major areas in and means by which the Bank will seek to improve its operational performance.

(b) By August 20, 1999, the Bank shall submit to the Reserve Bank a realistic and comprehensive budget for the remainder of 1999 and a preliminary budget for 2000, which shall, at a minimum, provide for: (i) monthly estimates of all material income and expense items; (ii) establishment of a review process to monitor the actual income and expenses of the Bank in comparison to budgetary projections and a review of this comparison by the board of directors on a monthly basis; (iii) semiannual revision of projected financial statements, including year-end balance sheet and income statement for the Bank; and (iv) a description of the operating assumptions that form the basis for, and adequately support, major projected income and expense components, including salaries and other expenses associated with any officers or directors, the Bank's deferred tax position, and provisions needed to establish and maintain adequate loan loss reserves.

(c) A final written strategic plan and budget for each calendar year after 1999 shall be submitted to the Reserve Bank at least one month prior to the beginning of that calendar year.

16. (a) The plans, policies and procedures required by paragraphs 6, 7, 8, 12, and 13 hereof shall be submitted to the Reserve Bank for review and approval. The Reserve Bank may comment on the plans, policies, and procedures. Acceptable plans, policies, and procedures shall be submitted to the Reserve Bank within the required time periods set forth in this Agreement. Where applicable, Bancshares and the Bank shall adopt all approved plans, policies, and procedures within 10 days of approval by the Reserve Bank and then shall fully comply with them. During the term of this Agreement, where applicable, Bancshares and the Bank shall not amend or rescind the approved plans, policies, and procedures without the prior written approval of the Reserve Bank.

(b) The boards of directors of Bancshares and the Bank shall review all plans, policies, and procedures annually, and review compliance with all plans, policies and procedures on at least a quarterly basis.

17. Within 30 days of the end of each calendar quarter (September 30, December 31, March 31, and June 30) following the date of this Agreement, Bancshares and the Bank shall furnish to the Reserve Bank written progress reports detailing the form and manner of all actions taken to secure compliance with this Agreement and the results thereof.

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

(a) Mr. Jeffrey A. Jensen  
Director - Iowa  
Federal Reserve Bank of Chicago – Iowa Branch  
400 Locust Street  
Des Moines, Iowa 50309

(b) Mr. Marvin J. Kuehl  
Chairman  
First Security Bancshares, Inc.  
113 Market Street, P.O. Box 128  
Lake Park, Iowa 51347

(c) Mr. Robert Goeken  
President and CEO  
Security State Bank  
P.O. Box 166  
Hartley, Iowa 51346

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

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

21. Notwithstanding any provision of this Agreement to the contrary, the Reserve Bank may, in its sole discretion, grant written extensions of time to Bancshares and the Bank to comply with any provision of this Agreement.

22. The provisions of this Agreement shall not bar, estop or otherwise prevent the Board of Governors, the Reserve Bank, or any Federal or State agency or department from taking any other action affecting Bancshares or the Bank or any of their current or former institution-affiliated parties.

23. This Agreement is a "written agreement" for the purposes of section 8 of the FDI Act (12 U.S.C. 1818).

IN WITNESS HEREOF, the parties have caused this Agreement to be executed as of the 6 day of August, 1999.

Federal Reserve Bank of Chicago  
By: [Signature]

Security State Bank  
By: [Signature]

First Security Bancshares, Inc.  
By: [Signature]

The undersigned directors of Bancshares each acknowledges having read the foregoing Agreement and approves of the consent thereto by Bancshares.

[Signature] [Signature]  
Marvin Kuehl Kevin Kuehl

[Signature] [Signature]  
Robert Goeken Paul Albrecht

The undersigned directors of the Bank each acknowledges having read the foregoing Agreement and approves of the consent thereto by the Bank.

[Signature] [Signature]  
Marvin Kuehl Robert Goeken

[Signature] [Signature]  
Duane Kolpin Wally Tschopp

[Signature]  
Keith Weber