

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

_____ )	
In the Matter of )	
CACHE VALLEY BANKING COMPANY )	Docket Nos. 07-003-B-HC
Logan, Utah )	07-003-B-SM
_____ )	
CACHE VALLEY BANK )	Cease and Desist Order Issued
Logan, Utah )	Upon Consent Pursuant to the
_____ )	Federal Deposit Insurance Act,
_____ )	as Amended
_____ )	

WHEREAS, the Board of Governors of the Federal Reserve System (the “Board of Governors”), Cache Valley Banking Company (“Cache Valley”), a registered bank holding company, and its subsidiary bank, the Cache Valley Bank, Logan, Utah (the “Bank”), a state chartered bank that is a member of the Federal Reserve System, have the common goal to restore and maintain the financial soundness of the Bank;

WHEREAS, on April 19, 2004, Cache Valley and the Bank entered into a Written Agreement with the Federal Reserve Bank of San Francisco (the “Reserve Bank”) and the Utah State Department of Financial Institutions (the “UDFI”) designed to correct certain deficiencies at the Bank relating to safety and soundness (the “2004 Written Agreement”);

WHEREAS, the Bank has taken steps to comply with the 2004 Written Agreement but has not yet fully complied with all of the provisions of the 2004 Written Agreement;

WHEREAS, after execution of the 2004 Written Agreement the Reserve Bank and the UDFI identified additional safety and soundness deficiencies at the Bank;

WHEREAS, the Board of Governors, Cache Valley, and the Bank have mutually agreed to enter into this consent Cease and Desist Order (the “Order”); and

WHEREAS, on March 8, 2007, the boards of directors of Cache Valley and the Bank, at duly constituted meetings, adopted resolutions authorizing and directing N. George Daines, chairman of the board of directors of Cache Valley, and J. Gregg Miller, president and chief executive officer of the Bank, to enter into this Order on behalf of Cache Valley and the Bank, respectively, and consenting to compliance by Cache Valley and the Bank, and their respective 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)), with each and every applicable provision of this Order and waiving any and all rights that Cache Valley and the Bank may have pursuant to section 8 of the FDI Act (12 U.S.C. § 1818) to: (i) a hearing for the purpose of taking evidence on any matters set forth in this Order; (ii) judicial review of this Order; (iii) contest the issuance of this Order by the Board of Governors pursuant to section 8 of the FDI Act; and (iv) challenge or contest, in any manner, the basis, issuance, validity, terms, effectiveness or enforceability of this Order or any provisions hereof.

NOW, THEREFORE, IT IS HEREBY ORDERED that, pursuant to sections 8(b)(1) and (3) of the FDI Act, Cache Valley, the Bank, and their respective institution-affiliated parties shall cease and desist and take affirmative action as follows:

**Board Oversight**

1. Within 30 days of this Order, the board of directors of the Bank shall submit to the Reserve Bank an acceptable written plan, including timeframes and actions, to strengthen board oversight of the management and operations of the Bank and improve the overall condition 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, at a minimum:

(i) the credit risk management program, including loan underwriting, documentation, internal loan grading, and administration;

(ii) the accounting and regulatory reporting functions, including, but not limited to, proper accounting and reporting of the Bank's assets and liabilities and the Bank's transactions with institution-affiliated parties; and

(iii) compliance programs;

(b) the addition of an outside director to the loan committee. For the purposes of this Order, the term: (i) "outside director" is defined as an individual, not an employee or executive officer of Cache Valley or the Bank, who owns less than 10 percent of the outstanding voting stock of Cache Valley or the Bank and who is not related in any manner to any shareholder who owns 10 percent or more of the outstanding voting stock of Cache Valley or the Bank or any related interest of such a shareholder; and (ii) "executive officer" is defined as set forth in section 215.2(e) of Regulation O of the Board of Governors (12 C.F.R. § 215.2(e));

(c) actions to ensure that regular progress reports on problem loan collections are submitted to the board of directors;

(d) the responsibility of the board of directors to monitor management's adherence to approved policies and procedures, and applicable laws and regulations;

(e) measures to ensure that the deliberations and actions of the board of directors and its committees are fully documented in complete, detailed minutes, including but not limited to, the review of transactions involving institution-affiliated parties, their immediate

families, as defined in section 225.41(b)(3) of Regulation Y of the Board of Governors (12 C.F.R. § 225.41(b)(3)), and related interests, as defined in section 215.2(n) of Regulation O of the Board of Governors (12 C.F.R. § 215.2(n));

(f) a formal process for (i) tracking regulatory, audit, and external loan review findings and (ii) resolving findings through corrective action plans, which include timetables for taking the corrective action;

(g) documentation in the minutes of the board of directors or its committees of the approval of any compensation, other than routine directors' fees, paid to any member of the board of directors, including the purpose and criteria for continuance of such compensation;

(h) a process to ensure timely approval by the board of directors of new or revised policies and prompt implementation of such policies by management following approval; and

(i) establishment of clear lines of authority to address the deficiencies related to segregation of duties noted in the report of the examination of the Bank conducted jointly by the Reserve Bank and the UDFI, commenced on July 10, 2006 (the "2006 Report of Examination").

### **Conflicts of Interest Policy**

2. Within 30 days of this Order, Cache Valley and the Bank shall submit to the Reserve Bank an enhanced written code of ethics and conflicts of interest policy which applies to all directors, officers, and employees of Cache Valley and the Bank. The enhanced code of ethics and conflicts of interest policy shall address, at a minimum, the fiduciary duties of all directors, officers, and employees of Cache Valley and the Bank and the avoidance of conflicts of interest, in particular in the administration of loans to insiders, shareholders, and their

immediate families and any transaction from which any such individual may derive personal benefit.

3. Within 30 days of this Order, Cache Valley and the Bank shall submit to the Reserve Bank an acceptable written plan to improve compliance with the code of ethics and conflicts of interest policy by all directors, officers, and employees of Cache Valley and the Bank. The plan shall provide, at a minimum, for:

(a) Policies and procedures to require the written disclosure to the board of directors of Cache Valley or the Bank, as appropriate, of any actual or potential conflict of interest of any Cache Valley or Bank officer, director, employee, or principal shareholder;

(b) policies and procedures for complying with Regulation O of the Board of Governors, which restricts credit that a member bank may extend to its executive officers, directors, and principal shareholders and their related interests (12 C.F.R. Part 215);

(c) internal controls that monitor compliance with the code of ethics and conflicts of interest policy and report any noncompliance or exceptions to the approved policy to the board of directors of Cache Valley and the Bank, as appropriate; and

(d) training for all directors, officers, and employees of Cache Valley and the Bank provided on a regular basis regarding the enhanced code of ethics and conflicts of interest policy of Cache Valley and the Bank and the requirements of Regulation O of the Board of Governors regarding loans to insiders.

4. Within 30 days of the approval by the Reserve Bank of the plan required by paragraph 3 of this Order, the boards of directors of Cache Valley and the Bank shall retain an acceptable independent consultant to provide the training required by paragraph 3. The terms of the contract with the consultant shall require that the training sessions commence within 60 days

of the retention of the consultant. Cache Valley and the Bank shall retain copies of all training materials and lists of training attendance for future supervisory review.

### **Loan Policies and Procedures**

5. Within 60 days of this Order, the Bank shall submit revised written loan policies and procedures that are acceptable to the Reserve Bank and that address, at a minimum:

(a) The deficiencies noted in the 2006 Report of Examination regarding loan policies and procedures, including but not limited to construction and agricultural loan policies and procedures;

(b) requirements for reporting exceptions to the Bank's loan policies to the board of directors;

(c) the identification, monitoring, and periodic reporting to the board of directors of the aggregate obligations of borrowers who are related through common control (as defined in section 215.2(c) of Regulation O of the Board of Governors (12 C.F.R. § 215.2(c)) and Utah Code Annotated, Section 7-1-103(5)), shared collateral, a shared repayment source, or shared proceeds to ensure compliance with lending limits applicable to related interests;

(d) requirements under Generally Accepted Accounting Principles ("GAAP") and instructions for Reports of Condition and Income for properly reporting nonaccrual loans and leases and the timely recognition of losses;

(e) real estate valuation and appraisal requirements, including, at a minimum:

(i) Guidelines on when real estate appraisals and other valuations of loan collateral are required;

(ii) procedures to conduct appraisal reviews and evaluations prior to the booking date of the loan;

(iii) enhanced documentation to support the use or deviation from comparable values and the derivation of final reconciled values;

(iv) procedures for determining the market value of foreclosed collateral; and

(v) compliance with the Interagency Statements on Independent Appraisal and Evaluation Functions dated October 28, 2003, and Appraisal and Evaluation Guidelines dated October 27, 1994, as well as the requirements of Subpart G of Regulation Y of 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 Board of Governors' Guidelines for Real Estate Appraisal Policies and Review.

### **Loan Review**

6. Within 60 days of this Order, the Bank shall revise the Bank's engagement letter for the conduct of external loan reviews to ensure that such reviews focus on key issues and evaluate internal loan grading. The Bank shall submit the revised engagement letter to the Reserve Bank for approval.

### **Asset Improvement**

7. (a) Within 60 days of this Order, the Bank shall submit to the Reserve Bank 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 \$100,000 that was past due as to principal or interest more than 90 days as of the date of this Order, is on the Bank's watch list, or that was adversely classified or listed as special mention in the 2006 Report of Examination.

(b) Within 30 days of the date that any additional loan or other asset in excess of \$100,000 becomes past due as to principal and interest for more than 90 days, is adversely classified internally by the Bank, or is adversely classified or listed for special mention in any subsequent report of examination or visitation of the Bank, the Bank shall submit to the Reserve Bank an acceptable written plan to improve the Bank's position on such loan or asset.

(c) The plan for each loan or other asset shall be formally approved by the Bank's loan committee and shall, at a minimum, include:

- (i) The current status of the loan or other asset, including book and nonbook carrying value;
- (ii) financial analysis that is based on current cash flows and collateral valuations;
- (iii) proposed actions to improve, reduce, or eliminate the loan or other asset, including collection or sale of collateral, and realistic time frames for such actions; and
- (iv) where appropriate, the borrower's acknowledgement of and response to the plan.

(d) Within 30 days of the end of the next calendar quarter following the due date for submission of the initial asset improvement plans, and within 30 days of the end of each calendar quarter thereafter, the Bank shall submit a written progress report to the Reserve Bank to update the asset improvement plan, which shall include, at a minimum, the carrying value of the loan or other asset, changes in the nature and value of supporting collateral, and a copy of the Bank's current internal watch list, loan renewal and extension report, and past due/non-accrual loan report.

### **Loan Administration**

8. Within 60 days of this Order, the board of directors of the Bank shall take such actions as are necessary to employ (i) a permanent, full-time officer with the requisite ability, experience, and other qualifications to competently manage the loan administration function and (ii) a permanent, full-time officer with the requisite ability, experience, and other qualifications to competently manage the collection and problem loan workout function.

9. Within 30 days of this Order, the board of directors of the bank shall submit to the Reserve Bank an acceptable written plan that details the actions that the board of directors

proposes to take in order to strengthen the loan administration function and enhance its independence. The plan shall, at a minimum, address, consider, and include:

- (a) Reporting lines within the Bank designed to ensure the independence of the loan administration function from the lending department;
- (b) controls to ensure appropriate segregation of duties among lending, loan administration, and collection and problem loan workout;
- (c) controls to limit access to the Bank's accounting system; and
- (d) steps to reduce loan documentation and loan administration exceptions and to maintain appropriate, current loan documentation.

#### **Allowance for Loan and Lease Losses**

10. (a) The Bank shall continue to maintain, through charges to current operating income, an adequate valuation reserve for loan and lease losses (the "ALLL"). The adequacy of the ALLL shall be determined in light of the volume of criticized loans, the current level of past due and nonperforming loans, past loan loss experience, evaluation of the probable losses in the Bank's loan portfolio, including the potential for the existence of unidentified losses in loans adversely classified, the imprecision of loss estimates, the requirements of the Interagency Policy Statement on the Allowance for Loan and Lease Losses dated July 2, 2001 and December 13, 2006, and examiners' criticisms noted in the 2006 Report of Examination.

(b) The Bank shall conduct, at least on a calendar quarterly basis, an assessment of its ALLL and, within 30 days of the end of each calendar quarter, shall submit to the Reserve Bank the quarterly assessment, including the methodology used in determining the

amount of ALLL for that quarter. The Bank shall maintain for subsequent supervisory review documentation to support the methodology used for each quarterly assessment.

### **Compliance with Laws and Regulations**

11. The board of directors of the Bank shall immediately take all necessary steps to correct the violations of law cited in the 2006 Report of Examination. In addition, the board of directors shall take steps designed to ensure that the Bank complies with all applicable laws and regulations in the future.

### **Regulatory Communications and Cooperation**

12. Cache Valley and the Bank shall ensure that all personnel and agents of Cache Valley and the Bank fully cooperate with the Reserve Bank in all regulatory matters, including, but not limited to, providing complete and prompt access to all documentation requested by examiners as needed to fulfill regulatory and supervisory responsibilities.

### **Appointment of New Officers and Directors, and Severance and Indemnification Payments**

13. Cache Valley and the Bank 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 in the appointment of directors and senior executive officers and with the restrictions on severance payments and indemnification of section 18(k) of the FDI Act (12 U.S.C. § 1828) and Part 359 of the Federal Deposit Insurance Corporation's regulations (12 C.F.R. Part 359).

### **Dividends**

14. (a) Cache Valley and the Bank shall not declare or pay any dividends without the prior written approval of the Reserve Bank and the Director of the Division of Banking Supervision and Regulation of the Board of Governors. All requests for prior 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 consolidated earnings, and cash flow, capital, asset quality, and ALLL needs of the Bank.

(b) Cache Valley shall not take dividends or any other form of payment representing a reduction in capital from the Bank without the prior written approval of the Reserve Bank.

### **Debt and Stock Redemption**

15. (a) Cache Valley shall not, directly or indirectly, 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.

(b) Cache Valley and the Bank shall not redeem any stock without the prior written approval of the Reserve Bank.

### **Compliance with Order**

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

boards of directors monthly. Copies of the Compliance Committee's minutes shall be provided to the Reserve Bank monthly.

(b) Within 30 days after the end of each calendar quarter (March 31, June 30, September 30, and December 31) following the date of this Order, the boards of directors of Cache Valley and the Bank shall submit to the Reserve Bank written progress reports detailing the form and manner of all actions taken to secure compliance with this Order and the results thereof. Management responses to any audit reports prepared by internal and external auditors shall be included with the progress reports. Such reports may be discontinued when the corrections required by this Order have been accomplished and the Reserve Bank has, in writing, released Cache Valley and the Bank from making further reports.

#### **Approval, Implementation, and Progress Reports**

17. (a) Cache Valley and the Bank, as appropriate, shall submit written plans, policies, procedures, and an engagement letter acceptable to the Reserve Bank within the applicable time periods set forth in paragraphs 1, 3, 4, 5, 6, 7, and 9 of this Order.

(b) Within 10 days of approval by the Reserve Bank, Cache Valley and the Bank, as appropriate, shall adopt the approved plans, policies, procedures, and engagement letter. Upon adoption, Cache Valley and the Bank, as appropriate, shall implement the approved plans, policies, procedures, and engagement letter, and thereafter fully comply with them.

(c) During the term of this Order, the approved plans, policies, procedures, and engagement letter shall not be amended or rescinded without the prior written approval of the Reserve Bank.

## Communications

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

(a) Kenneth R. Binning  
Director, Applications & Enforcement  
Federal Reserve Bank of San Francisco  
101 Market Street, Mail Stop 615  
San Francisco, California 94105

(b) J. Gregg Miller  
President and Chief Executive Officer  
Cache Valley Bank  
101 N. Main Street  
P.O. Box 3227  
Logan, Utah 84321-4525

(c) N. George Daines  
Chairman of the Board  
Cache Valley Banking Company  
c/o Barrett & Daines  
108 N. Main Street  
Logan, Utah 84321

19. With the concurrence of the UDFI, the 2004 Written Agreement is hereby terminated.

20. Notwithstanding any provision of this Order to the contrary, the Reserve Bank may, in its sole discretion, grant written extensions of time to Cache Valley and the Bank to comply with any provision of this Order.

21. The provisions of this Order shall be binding upon Cache Valley and the Bank, and all of their institution-affiliated parties, in their capacities as such, and their successors and assigns.

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

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

By order of the Board of Governors of the Federal Reserve System effective this 20th day of March, 2007.

CACHE VALLEY BANKING COMPANY

BOARD OF GOVERNORS OF  
THE FEDERAL RESERVE SYSTEM

By: (SIGNED)  
N. George Daines  
Chairman of the Board of Directors

By: (SIGNED)  
Jennifer J. Johnson  
Secretary of the Board

CACHE VALLEY BANK

By: (SIGNED)  
J. Gregg Miller  
President and Chief Executive Officer