

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

STATE OF MONTANA
DIVISION OF BANKING AND FINANCIAL INSTITUTIONS
HELENA, MONTANA

Written Agreement by and among

RAVALLI COUNTY BANKSHARES, INC.
Hamilton, Montana

RAVALLI COUNTY BANK
Hamilton, Montana

FEDERAL RESERVE BANK OF MINNEAPOLIS
Minneapolis, Minnesota

and

MONTANA DIVISION OF BANKING AND
FINANCIAL INSTITUTIONS
Helena, Montana

Docket Nos. 09-176-WA/RB-HC
09-176-WA/RB-SM

WHEREAS, in recognition of their common goal to maintain the financial soundness of Ravalli County Bankshares, Inc., Hamilton, Montana (“Bankshares”), a registered bank holding company, and its subsidiary bank, Ravalli County Bank, Hamilton, Montana (the “Bank”), a state chartered bank that is a member of the Federal Reserve System, Bankshares, the Bank, the Federal Reserve Bank of Minneapolis (the “Reserve Bank”), and the Montana Division of Banking and Financial Institutions (the “Division”) have mutually agreed to enter into this Written Agreement (the “Agreement”); and

WHEREAS, on March 2, 2010, Bankshares' and the Bank's boards of directors, at duly constituted meetings, adopted resolutions authorizing and directing Charles Shonkwiler to consent to this Agreement on behalf of Bankshares and the Bank, respectively, and consenting to compliance with each and every applicable provision of this Agreement by Bankshares, 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, Bankshares, the Bank, the Reserve Bank, and the Division 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 Division 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 major operations and activities, including but not limited to, credit risk management, credit administration, processes to mitigate risks associated with credit concentrations, and earnings;

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

(c) the establishment of measures to ensure Bank staff's adherence to approved policies and procedures; and

(d) 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, capital, earnings, and liquidity.

Management Plan

2. Within the earlier of 60 days of receipt of the report of the independent consultant or 75 days after this Agreement, the board of directors of the Bank shall submit to the Reserve Bank and the Division a written management plan, based on the findings and conclusions of the management review that was recently conducted by an independent consultant, that describes the specific actions that the board of directors will take to strengthen the Bank's management and to hire, as necessary, additional or replacement personnel.

Credit Risk Management

3. Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Division 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 tolerance guidelines and risk limits;
 - (b) procedures to periodically review and revise risk exposure limits to address changes in market conditions;
 - (c) strategies to minimize credit losses and reduce the level of problem assets;
- and
- (d) procedures to identify, limit, and manage concentrations of credit that are consistent with the Interagency Guidance on Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices, dated December 12, 2006 (SR 07-1).

Lending and Credit Administration

4. Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Division an acceptable written lending and credit administration program that shall, at a minimum, address, consider, and include:

- (a) Establishment of documentation standards for loans;
- (b) underwriting standards that require documented analyses 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 renewing, extending, or modifying existing loans, including, but not limited to, analysis, documentation, and approval requirements;
- (d) standards for extending unsecured loans;
- (e) compliance with the Interagency Guidelines for Real Estate Lending Policies, Appendix C of Regulation H of the Board of Governors of the Federal Reserve System (the "Board of Governors") (12 C.F.R. Part 208, Appendix C);
- (f) enhancements to the internal loan grading system to timely and accurately identify individual problem credits; and
- (g) appropriate controls on construction and land development loans, including, but are not limited to, disbursement of loan proceeds and periodic inspections.

Loan Review

5. Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Division an acceptable written program for the ongoing review and grading 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, at a minimum, address, consider, and include:

- (a) The scope and frequency of loan review;
- (b) standards and criteria for assessing the credit quality of loans, including procedures to re-evaluate loans in the event of material changes in the borrower's performance or the value of the collateral;
- (c) application of loan grading standards and criteria to the loan portfolio;
- (d) controls to ensure staff's adherence to the revised loan review and grading standards; and
- (e) written reports to the board of directors, at least quarterly, that identify the status of those loans that are nonperforming or adversely graded and the prospects for full collection or strengthening of the quality of any such loans.

Appraisal and Appraisal Review Program

6. Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Division 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 (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) written standards for when reappraisals and reevaluations must be conducted; and

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

Accounting Practices

7. (a) Within 30 days of this Agreement, the Bank shall engage an independent accounting firm, acceptable to the Reserve Bank and the Division, to review the Bank's accounting for nonaccruals, repossessed assets, and other real estate owned ("OREO").

(b) Within 60 days of completion of the review described in paragraph 7(a), the Bank shall submit to the Reserve Bank and the Division acceptable revised policies and procedures for accounting for nonaccruals, repossessed assets, and OREO.

Asset Improvement

8. 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 the examination of the Bank conducted by the Reserve Bank that commenced on April 14, 2009 and November 2, 2009 (the "Reports of Examination") (other than credits that were criticized in the April 14, 2009 Report and then passed in the November 2, 2009 Report), 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)).

9. (a) Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Division 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 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 Reports of Examination (other than credits that were criticized in the April 14, 2009 Report and then passed in the November 2, 2009 Report). 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 any additional loan or other asset in excess of \$250,000, including OREO, 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 Division an acceptable written plan to improve the Bank's position on such loan 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 Division 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. The board of directors shall review the progress reports before submission to the Reserve Bank and the Division and shall document the review in the minutes of the board of directors' meetings.

Allowance for Loan and Lease Losses

10. (a) 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 Division.

(b) Within 60 days of this Agreement, the Bank shall review and revise its allowance for loan and lease losses ("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 Division. 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 collectibility.

(c) Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Division 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 Division, 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

11. Within 60 days of this Agreement, Bankshares and the Bank shall submit to the Reserve Bank and the Division an acceptable joint written plan to maintain sufficient capital at the Bank. The plan shall, at a minimum, address, consider, and include:

(a) The Bank's current and future capital requirements, 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;

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

(d) the requirements of section 225.4(a) of Regulation Y of the Board of Governors (12 C.F.R. § 225.4(a)) that Bankshares serve as a source of strength to the Bank.

12. Bankshares and the Bank shall notify the Reserve Bank and the Division, 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, Bankshares and the Bank shall submit an acceptable written plan that details the steps Bankshares and the Bank will take to increase the Bank's capital ratios to or above the approved capital plan's minimums.

Business Plan and Budget

13. (a) Within 60 days of this Agreement, the Bank shall submit to the Reserve Bank and the Division a written business plan to improve the Bank's earnings and overall condition, and a budget for 2010. The written plan and budget shall include, but not be limited to:

(i) Identification of the major areas where, and means by which, the board of directors will seek to improve the Bank's operating performance;

(ii) a realistic and comprehensive budget for calendar year 2010, including income statement and balance sheet projections; and

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

(b) A business plan and budget for each calendar year subsequent to 2010 shall be submitted to the Reserve Bank and the Division at least 30 days prior to the beginning of that calendar year.

Funds Management

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

Dividends

15. (a) Bankshares and 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 (the "Director"), and, as to the Bank, the Division.

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

(c) All requests for prior approval shall be received at least 30 days prior to the proposed payment or dividend declaration date. All requests shall contain, at a minimum, current and projected information, as appropriate, on Bankshares's capital, earnings, and cash flow; the Bank's capital, asset quality, earnings and ALLL needs; and identification of the sources of funds for the proposed payment or dividend. Bankshares and the Bank, as appropriate, must also demonstrate that the requested declaration or payment of dividends is 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).

Debt and Stock Redemption

16. (a) Bankshares shall not, directly or indirectly, incur, increase, or guarantee 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) Bankshares shall not, directly or indirectly, purchase or redeem any shares of its stock without the prior written approval of the Reserve Bank.

Compliance with Laws and Regulations

17. (a) The Bank shall immediately take all necessary steps to correct all violations of law or regulation cited in the Reports of Examination. In addition, the Bank shall take necessary steps to ensure future compliance with all applicable laws and regulations.

(b) 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, Bankshares 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 (12 C.F.R. §§ 225.71 *et seq.*), and, as to the Bank, provide written notice to the Division.

(c) Bankshares and 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

18. Within 30 days after the end of each calendar quarter following the date of this Agreement, the board of directors of the bank shall submit to the Reserve Bank and the Division 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, Policies, Procedures, and Programs

19. (a) The Bank and, as applicable, Bankshares shall submit written plans, policies, procedures, and programs that are acceptable to the Reserve Bank and the Division within the applicable time periods set forth in paragraphs 3, 4, 5, 6, 7, 9, 10(c), 11, 12, and 14 of this Agreement. An independent accounting firm acceptable to the Reserve Bank and the Division shall be retained by the Bank within the time period set forth in paragraph 7(a) of this Agreement.

(b) Within 10 days of approval by the Reserve Bank and the Division, the Bank and, as applicable, Bankshares shall adopt the approved plans, policies, procedure, and

programs. Upon adoption, the Bank and, as applicable, Bankshares shall promptly implement the approved plans, policies, procedures, and programs, and thereafter fully comply with them.

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

Communications

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

- (a) Ms. Diann G. Townsend
Assistant Vice President
Federal Reserve Bank of Minneapolis
90 Hennepin Avenue
Minneapolis, Minnesota 55401-1804
- (b) Ms. Annie Goodwin
Commissioner
State of Montana
Division of Banking and Financial Institutions
301 South Park, Suite 316
P.O. Box 200546
Helena, Montana 59601
- (c) Mr. Charles D. Shonkwiler
Ravalli County Bankshares, Inc.
Ravalli County Bank
224 West Pinckney Street
Hamilton, Montana 59840-0150

Miscellaneous

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

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

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

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

25. 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 4th day of March, 2010.

RAVALLI COUNTY BANKSHARES, INC.

FEDERAL RESERVE BANK
OF MINNEAPOLIS

By: /s/ Charles Shonkwiler
Charles Shonkwiler
Secretary-Treasurer

By: /s/ James M. Barnes
James M. Barnes
Vice President and
Chief Examination Officer

RAVALLI COUNTY BANK

STATE OF MONTANA
DIVISION OF BANKING AND
FINANCIAL INSTITUTIONS

By: /s/ Charles Shonkwiler
Charles Shonkwiler
President

By: /s/ Annie Goodwin
Annie Goodwin
Commissioner