We will support your regulatory compliance program on an ongoing basis by providing testing services periodically. We believe that regulatory compliance, like other business risks, should be managed on an institution-wide basis, with relative regulatory risk considered in all business decisions.

Compliance Testing Scope

To complete these services, we will review key compliance areas as follows:

Closed End Credit – Real Estate Secured Loan Sample
Truth in Lending Act – Regulation Z
Real Estate Settlement Procedures Act (RESPA)
Flood Disaster Protection Act
Equal Credit Opportunity Act – Regulation B
Home Ownership and Equity Protection Act
Home Mortgage Disclosure Act, if applicable
FACT Act

Closed End Credit – Non-Real Estate Secured Loan Sample
Truth in Lending Act – Regulation Z
Equal Credit Opportunity Act – Regulation B
Fair Credit Practices Act – Regulation AA

Open End Credit Sample (Overdraft Protection, Home Equity Lines of Credit)
Truth in Lending Act – Regulation Z
Flood Disaster Protection Act
FACT Act

Adverse Action Sample
Equal Credit Opportunity Act – Regulation B
Fair Credit Reporting Act/FACT Act
Fair Housing Act
Home Mortgage Disclosure Act, if applicable

Bank Secrecy Act/USA PATRIOT Act Compliance
Program Elements
Complete Independent Test as required annually

Loan Review Approach

We have designed an external loan review delivery system to provide the highest quality and most cost-effective alternative for your Bank. Our approach will consist of the following steps:

1. Discuss with management the desired coverage and loan sample selection.
2. Perform on-site review of selected lending relationships.
3. Review the Bank's internal Criticized Asset Action Plans, noting any deficiencies and making recommendations fo improvement.
4. Meet with management and lending personnel to discuss individual loan files, general portfolio practices, documentation exceptions, action plans, and compliance observations.
5. Issue final report with detail observations, recommendations, ratings, and exceptions.

Loan Review Reporting

We will provide individual detailed worksheets for each loan reviewed that will include a write-up on each credit reviewed including a summary of the notes, collateral, key financial information, a brief narrative of the compliance with Bank loan policies and procedures, and a list of loan policy and documentation exceptions. Additional copies of the loan relationship write-ups will be provided for inclusion in the individual loan files.

Loan reviews will be restricted to documentation contained in the Bank's loan files and interviews with Bank personnel. For the most part, loan files will contain financial information supplied by the borrower. Our procedures will not include tests to determine the following:

- The accuracy of the loan file documentation or the accuracy of the Bank's responses to direct inquiries.
- The completeness or accuracy of reports or lists provided to us by the Bank.

The procedures we perform will not be for the purpose of determining the adequacy of the allowance for loan loss, although the information we provide in our report can be used by management to assist in this process. Bank management has the ultimate responsibility for determining the adequacy of the allowance for loan loss.

Bank Responsibility for Loan Review

The Bank is responsible for the following:

- Concurring with the selection of all loan relationships to be reviewed or selecting all loan relationships to be reviewed.
- The initial and ongoing assignment of ratings on all lending relationships.
- Use of the project reports to evaluate the adequacy of the allowance for loan losses.

I. STATEMENT OF NEED AND DEFINITION

The Board of Directors of Federation Bank believes that sound loans are a desirable and profitable means of employing funds available for investment. The Board recognizes that lending money necessarily includes reasonable business risks; and thus, formulates this Loan Policy to provide guidance and to control the quality of major earning assets. The Bank will maximize the return of shareholder investment without sacrificing quality and reputation.

II. THE PURPOSE

The Bank will extend credit to its delineated trade area and depositors. All loans will comply with all applicable State and Federal laws, regulations, rulings and interpretations thereof. This Bank will not discriminate against any applicant on the basis of age (provided that the applicant has the capacity to enter into a binding contract), race, color, religion, sex, marital status, national origin, handicap, familial status (defined as children under the age of 18 living with a parent or legal custodian, pregnant women and people securing custody of children under 18), receipt of income from public assistance programs, or because of the applicant having in good faith exercised any rights provided in the Consumer Protection Act of 1968.

III. GENERAL OBJECTIVES

The general objective of this policy is to delegate authority and to provide guidelines for management to exercise flexibility in extending credit to customers. These guidelines are structured to maintain asset quality while providing a systematic approval and review process thus enhancing customer relations.

IV. SPECIFIC GOALS

The specific goals of this Loan Policy are:

A. To extend credit at a minimum of 3 1/2% spread over the Bank's average cost of funds.

B. To define underwriting and documentation standards.

C. To sustain a high quality loan portfolio with internal or regulator classified loans of less than 30% of total capital.

D. To focus on the overall liquidity strategies of the Bank.

E. To extend credit which will be in compliance with this policy, with prudent lending practices and laws and regulations under which this Bank is chartered.

F. To keep the Board of Directors fully informed as to the overall quality of the loan portfolio.

G. To aid in the training and development of loan officers.

V. LOAN AUTHORITY

Although ultimate authority for all lending activities is vested in the Board of Directors, the Board hereby delegates the administration of these responsibilities to the President & CEO and/or the Senior Lending Officer and further delegates responsibility for the execution of the loan policy to the Executive Loan Committee, to the Loan Committee and to loan officers by the establishment of lending limits.

A. Board Loan Committee:

This committee will be responsible for reviewing large and problem credits determined by its discretion. This committee has the ultimate authority to make decisions to ensure a large credit continues to meet Loan Policy requirements. This committee also has the ultimate authority to make decisions ensuring all problem credits have the proper direction to increase its quality or form a workout plan that ensures a timely repayment plan with the least amount of loan loss possible. The committee will also be responsible for reviewing the past due and non-accrual loan reports, loans that do not conform with the loan policy, loan participations (purchased and sold), internal "watch list" loans and letters of credit issued by the Bank.

B. Executive Loan Committee

A committee, whose membership includes two members of the Board of Directors Lending Committee, President & CEO, Sr. Loan Officer and other members designated by the Board of Directors who are key to lending decisions in the Bank. This Committee will approve loans that are desirable loans, but need Board approval between Board meetings.

C. Loan Committee:

A committee, whose membership includes all bank lending officers, will review new, renewed, and modified credits that exceed officer lending limits. overdraft reports, current interest rate schedules, and new loan audit reports.

The following real estate loans must receive prior Loan Committee approval:

1. All loans in excess of the loan officer's authorized lending limit as defined below.
2. Loans that do not conform to the bank's policies and procedures.
3. All loans to customers who appear on the bank's internal watch list and/or have loans that are over 60 days past due.
4. Beacon score that is 600 or less.

D. Loan Officer Lending Limits:

Sr. Lending Officer has the list of approved limits for Loan Officers.

LOAN COMPOSITION

A. Consumer - All appropriate disclosures and regulations will be followed. A minimum down payment of 20% or sufficient additional collateral is needed with all titled vehicle loans Below is a listing of maturities for various years of automobiles:

See guidelines from Consumer Loan Rate Sheet.

B. Agricultural Loans

Loans will be secured by real estate, livestock, equipment, machinery, crops in storage growing crops and intangibles. Depending on a customer's net worth, past repayment experience and income, unsecured notes are permissible. The term on livestock and equipment notes, will not exceed five years unless approved by the loan committee. Line of Credit loans will not be for more than 13 months.

C. Commercial

Loans will be secured by real estate, inventory, accounts receivable, equipment, fixtures, machines, vehicles assignment of sales contracts and intangibles. Depending on a customer's net worth, past repayment experience, and income, unsecured notes are permissible. The terms on these loans will not exceed seven years or the maturity allowed by SBA or rural development. Real Estate loans may be longer.

D. Real Estate Loans

The desired composition of the total loan portfolio is projected to be comprised of 65% real estate loans including agriculture, commercial, and residential real estate loans.

E. First Mortgage Loans

Loans will be secured by a first mortgage on the property being purchased or refinanced, all other real estate loans will be secured by a mortgage or deed of trust.

All down payment requirements and loan to value ratios on a 1-4 family **owner occupied** residential real estate will be calculated as follows:

XXV. LOAN REVIEW

The credit administration of Federation Bank's large commercial and agricultural accounts; specifically those representing a significant exposure to the Bank (defined as credit lines exceeding $250,000) and all watch credit lines is accomplished through a systematic loan review process.

This process includes the annual review of individual credit files, individual notes, security documents, and other financial information and senior loan officer analysis and commentary.

All documentation reviews are completed by the Bank's Loan Administrator using the format attached as Appendix "A".

The results of individual credit reviews will be presented to Federation Bank's Board and the Loan Officer at least annually.

Appendix A

Date of Review By

Name of Borrower

Total Debt

Financial Statement Date

Income Tax Return Date P&L Date

Date of Last Inspection

Notice to Buyers

Extensions Rewrites

Cash Flow Projections

Final Title Opinion Lien Search

Articles of Incorporation Resolution Certificate

Guarantor F/S Income Tax

Liens Perfected

Comments and Evaulation

POLICY ADHERENCE

EXCELLENT	1.	Current audited financial statements, documentation correct and current, i.e. lien perfection, inspections, listing of A/Rec. and A/Pay. No policy exception on LTV ratio.
AVERAGE	2.	Current compilation financial statements from excellent records. Last 3 years tax returns. All documentation correct and current. No policy exception on LTV ratio.
WATCH	3.	Current financial statements prepared by individuals from records that are reliable. Does not have the most recent tax return. Documentation is not current; i.e. inspection is past due. All policy exceptions have been waived by appropriate authority.
SUBSTANDARD	4.	Financial statements not current or accuracy is in question. Does not have recent tax return. Has policy exceptions, questionable lien position.
DOUBTFUL	5.	Financial Statements not current or accuracy is in question. Tax returns are not current or are non-existent. Major documentation deficiencies. Has policy exceptions.
LOSS	6.	No financial statements or are outdated so that they have little value or are not reliable. Major documentation problems. Has policy exceptions.

Management Experience

EXCELLENT	1. Proven ability to produce above average income. Manages time, finances and priorities well.
AVERAGE	2. Proven ability to produce the higher range of industry average income. Manages time, finances, and priorities well.
WATCH	3. Proven ability to produce industry average income. Deficiencies in managing time, finances, and priorities.
SUBSTANDARD	4. Income has been low to below industry average income. Deficiencies in managing time, finances, and priorities.
DOUBTFUL	5. Income has been below industry average income. Manages time, finances, and priorities unsatisfactorily.
LOSS	6. Has not produced satisfactory income. Manages time, finances, and priorities unsatisfactorily.

Analysis of Borrower
March 04 Federation Bank

Bank/Borrower Relationship

EXCELLENT	1. Prompt. Uses other banking services —all handled well.
AVERAGE	2. Expedient. Uses other banking services in a satisfactory manner.
WATCH	3. Timely. Uses other banking services--adequately, except may have an occasional overdraft.
SUBSTANDARD	4. Very Slow. Other banking services misused.
DOUBTFUL	5. Response is obtained after personal calls, letters from officers or legal counsel. Other banking services are abused.
LOSS	6. Does not respond. Other banking services are abused.

Quality of Collateral

EXCELLENT	1. Very marketable. Government-secured loan, Maintains value very well. Bank can maintain very good control of collateral. Security (loan value) margin is greater than 25% of loan value
AVERAGE	2. Easily marketable. Maintains value well. Bank can maintain good control of collateral. Security (loan value) is between 10% and 25%.
WATCH	3. Readily marketable. Maintains value. Bank can adequately control collateral. Security (loan value) margin is between 0% and 10%
SUBSTANDARD	4. Collateral may be marketable but with some difficulty due to its nature or condition. Bank may have problems controlling collateral. Security margin (loan value) is between 0% and –15%
DOUBTFUL	5. Collateral may be marketable but with extreme difficulty due to its nature or condition. Bank may have major problems controlling collateral. Security margin (actual value) is positive but security margin (loan value) is less than –15%.
LOSS	6. Unmarketable collateral. Bank may have very major problems in controlling collateral. Security margin (actual value) is negative.

Borrower Condition

EXCELLENT	1. Exceeds all standards, positive growth trend with measurable improvement. Credit assets of the highest quality.
AVERAGE	2. Meets all standards. Credit asset of good quality.
WATCH	3. Standards are met, but some are marginal; some strong areas offset weak areas and there is no area of excessive or undue high risk. Some standards are met while others are not met.
SUBSTANDARD	4. The credit assets are not adequately protected by the sound worth of the borrower or the collateral pledged. There is a well-defined weakness, which jeopardizes the payment of the debt. There is a distinct possibility of loss if the weakness is not corrected. It is not known if the standards are met
DOUBTFUL	5. The credit assets contain a high probability of loss but this loss cannot be immediately determined.
LOSS	6. None of the credit standards are met and/or are not adequate to prevent a loss to the lender. The credit assets are considered uncollectable and the loss is clearly defined.

Standards	**Acceptable**	**Goal**
1. Owner Equity=Net Worth/Assets	40%	>50%
2. Solvency=Total Debts/Total Assets	60%	<50%
3. Leverage=Total Debts/Net Worth	1.5-1.0	>1.0-1.0
4. Liquidity=Current Assets/Current Debts	1.0-1.0	1.5-1.0
5. Intermediate Ratio=Int. Term Assets/Int. Term Debts	1.0-1.0	1.5-1.0
6. Working Capital=Current Assets-Current Debts	Positive	>120%
7. Debt Service Coverage*=NP+Dep+Interest on term Debt-Living Expenses (unless corporate) divided by Term Debt Payment	1.15	1.25

**FSA & RD guaranteed loans require minimum debt service charge of 1.10*

Definitions

1. *Owner Equity*-Measures the ownership percent of the owner and obligation percent to creditor.

2. *Solvency*-Measures the ability to meet long-term debts and the ability to pay all debts if all assets are sold.

3. *Leverage*-Measures the relationship of total debts to net worth.

4. *Liquidity*-Measures the ability to pay the current debts with current assets-both assets and debts must be analyzed.

5. *Intermediate Ratio*-Measures the relationship of IT assets and IT debts.

6. *Working Capital*-Measures the amount available to carry on operations. Must be analyzed and put into proper perspective.

7. *Debt Service Coverage*-measures the firm's ability to cover term debt payment.

Consumer Debt

- Real Estate, Home Equity and Mobile Home Loans kept in our portfolio:

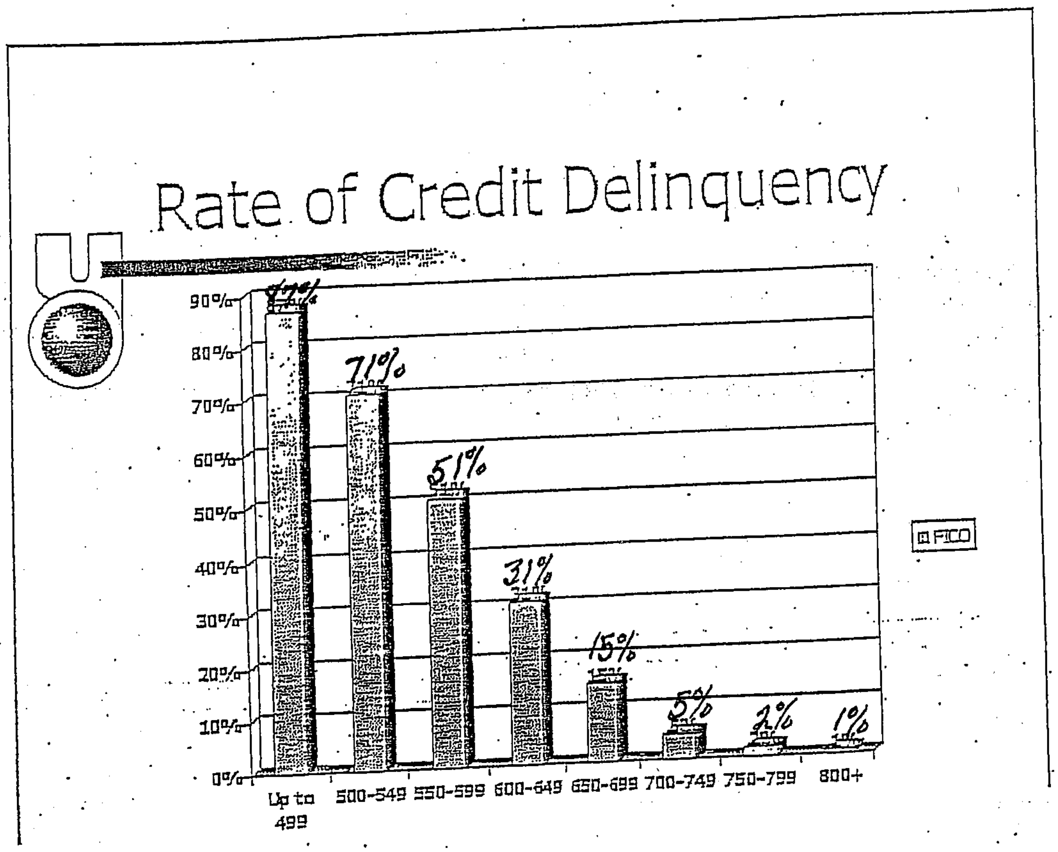
  Maximum "MOTI" ration should not exceed 36% and the maximum "PITI" ratio should not exceed 29%.

  Ratios for Real Estate Loans to be sold to the "secondary market" are set by the purchasing companies. The "MOTI" is currently 36% and the "PITI" ratio is currently 29%

  Rural Development (formerly FmHA) has a higher ratio for "MOTI" of 41%. The "PITI" ratio is 29%

- Other consumer debt such as loans for: vehicles, campers, motorcycles, unsecured debt, etc.

  The "MOTI" ratio should not exceed 36%. It is recommended that you be aware of the "PITI" ratio of these loans. It could be that other expenditures (i.e. taxes and/or insurance) could cause cash flow problems for the borrower. The recommended ratio for "PITI" should not exceed 29%.



This chart was a handout during the compliance and loan quality seminar we held in the Bank on September 18, 2003.

It is very interesting in that it shows what happens when you sacrifice loan quality or you do not pay attention to credit scores.

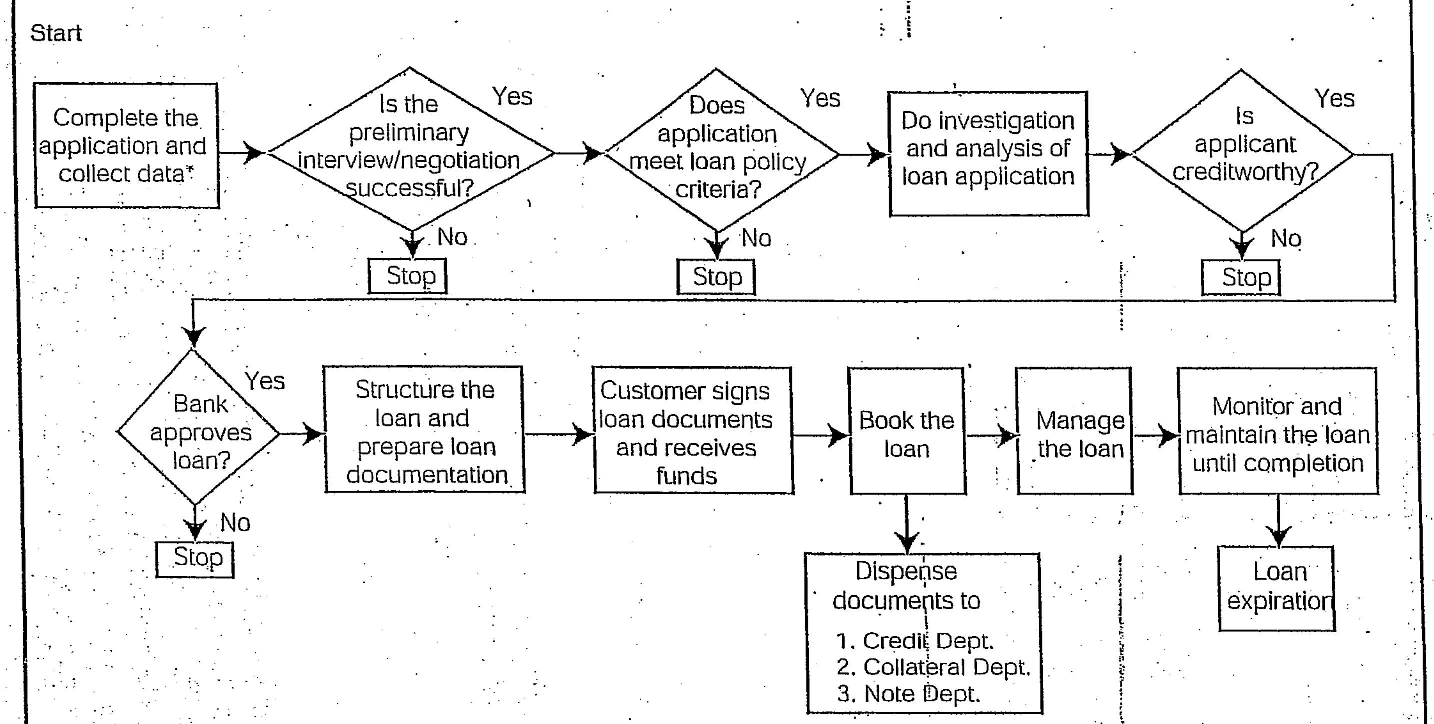
The figures across the bottom are the credit scores as issued by the credit bureau. These scores rate a customer's payment record, number of times there has been a credit inquiry and the long term history of the customer.

The figures that are vertical represent the projected percent of loans that will go to collection.

So, lets say a customer has a credit rating in the 500-549 area it would indicate that 71% of these customers would end up as a collection. On the other end of the scale if a customer has a credit score in the 700-749 area it would indicate a 5% chance that these customers would end up as a collection. This is a valid reason for us not to make loans to anyone under 600 credit score and only then if they have a good history with the Bank. We should really only be looking at customers in the 650+ area.

This is something for the Board to pay close attention to when reviewing loans for approval.

Exhibit 6.1: The Lending Process



*This step will be completed first if it is a consumer loan.

Federation Bank – Loan Committee Presentation

Date:

Name of Borrower:

Individual ( )	Joint ( )	Partnership ( )	LLC ( )	Corporation C ( )	Corporation S ( )	Non Profit ( )

Loan Type:

Agriculture ( )	Commercial ( )	Consumer ( )

Credit History:

Excellent ( )	Good ( )	Poor ( )	Bad ( )	Beacon:

Description of Operation:

Present Loans:

Type:LOC,OL,FP,REM,BRIDGE

Type:	Date of Note:	Original Balance	Present Balance	Rate	Payments	Frequency & Maturity	Current/ Past Due	Collateral	$ Value
1.									
2.									
3.									
4.									
5.									
6.									

Total Balance:$

New Request:

Type: LOC,OL,FP,REM,BRIDGE

Type:	New/Renew	Amount	Rate	Payments	Frequency & Maturity	Collateral	$ Value
1.							
2.							
3.							
4.							

Total New Loans:$

Guildance Line:

Total Commitment (Including New Request):

Cash Flow DSC: ____________________ **Tax Returns DSC:** ____________

FS Date: ________

CA:$: ________ **CL:$** ____________ **Ratio:** ____________

Total Assets$** ____________ **NW:$ ____________ **Owners Equity:%** ____________

Change in NW:$ ____________ ____ **%** **From adjusted value:** ____________ **Earned:** ____________ **Loss:** ______

EVALUATION

Policy Adherence:____________________

Bank/ Borrower Relationship:___________

Quality of Collateral:_________________

Borrower Condition:___________________

Management Experience:______________

Overall:_____________________________

COMMENTS: