



PUBLIC DISCLOSURE

JULY 21, 2014

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**MONTROSE BANK
RSSD# 522959**

**200 NORTH TOWNSEND AVENUE
MONTROSE, COLORADO 81401**

**Federal Reserve Bank of Kansas City
1 Memorial Drive
Kansas City, Missouri 64198**

NOTE: This document is an evaluation of this institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operation of the institution. This evaluation is not, nor should it be construed as, an assessment of the financial condition of this institution. The rating assigned to this institution does not represent an analysis, conclusion or opinion of the federal financial supervisory agency concerning the safety and soundness of this financial institution.

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INSTITUTION'S CRA RATING: *This institution is rated **Satisfactory**.*

Montrose Bank (the bank) has a satisfactory record of helping to meet the credit needs of its delineated assessment area (AA), including low- and moderate-income (LMI) families, as well as small businesses in a manner consistent with its resources, operating philosophy, and credit needs of the communities in which it operates.

The bank's net loan-to-deposit (NLTD) ratio indicated a reasonable effort to extend credit in its competitive market, considering the credit needs of the AA, the bank's financial condition, and the ratios of other similarly-situated financial institutions. A majority of the bank's loans were extended to borrowers within its AA. In addition, the bank's distribution of loans to individuals of different income levels and to businesses of different revenue sizes was reasonable. The bank's lending also reflected a reasonable dispersion of loans throughout its AA based on the income level of census tracts.

SCOPE OF EXAMINATION

The bank's Community Reinvestment Act (CRA) performance was evaluated using the Federal Financial Institutions Examination Council Interagency Small Bank Procedures. Four of the five criteria used to evaluate small bank CRA performance were relevant to this review and are as follows:

- NLTD Ratio
- Lending Inside the AA
- Distribution of Loans by Income Level of Geography
- Lending to Borrowers of Different Income Levels and Businesses of Different Revenue Sizes

The bank's responsiveness to complaints under the CRA, the fifth core criterion used to assess small bank performance, was not evaluated because the bank has not received any CRA-related complaints.

The bank's CRA examination included an evaluation of the bank's performance, with appropriate consideration given to demographic information. Conclusions regarding the four performance criteria were based on data compiled from the bank's major product lines: commercial and residential real estate loans. The major product lines were determined through discussions with bank management, a review of the March 31, 2014, Report of Condition and Income (Call Report), and a review of the number of loan originations since the bank's prior CRA examination conducted by the Federal Reserve Bank of Kansas City the week of July 12, 2010. The bank received a satisfactory rating at that review.

The CRA examination analyzed a statistical sample of 44 residential real estate loans from a universe of 56, as well as a statistical sample of 45 commercial loans from a universe of 57 originated between July 1, 2013 and December 31, 2013.

To augment the evaluation, interviews were conducted with members of the community to obtain perspectives of local economic conditions and to assess the bank's responsiveness to the credit needs of its AA communities. The community contacts included representatives from two local economic development corporations as well as a local real estate research company.

DESCRIPTION OF INSTITUTION

The bank is a full-service institution headquartered in the nonmetropolitan city of Montrose, Colorado. Montrose is located in southwest Colorado, approximately 50 miles south of Grand Junction, Colorado. The bank is wholly-owned by First Mountain Company (FMC), a one-bank holding company. Chairman Dennis W. White and Sherry White are the controlling shareholders of FMC and President Garth Gibson and Cynthia Gibson are the principal shareholders of FMC.

In addition to its main office located in north Montrose, the bank has five branches, including an additional location in south Montrose, and individual locations in Cedaredge, Delta, Hotchkiss, and Paonia. All six of the bank's locations, including its headquarters, are full-service offices, which include automated teller machines. The bank offers traditional credit and deposit products to meet the needs of its AA. According to the June 30, 2013 Federal Deposit Insurance Corporation (FDIC) Deposit Market Share Report, 11 financial institutions are located within the bank's AA, and the bank is ranked second in deposit market share with 18.2 percent of market deposits and total deposits of \$111.8 million. Table 1 illustrates the composition of the bank's loan portfolio by product type as of the March 31, 2014 Call Report. The bank reported total assets of \$234.8 million, with gross loans of \$84.9 million.

TABLE 1		
MONTROSEBANK'S LOAN PORTFOLIO		
Loan Type	Amount \$(000)	Percent of Total
Commercial	36,922	43.5
Residential Real Estate	31,996	37.7
Agricultural	11,569	13.6
Consumer	3,545	4.2
Other	902	1.0
Gross Loans	84,934	100.0

The analysis of the bank's CRA performance considered the bank's financial capacity, local economic conditions, AA demographics, and the bank's competitive operating environment. No legal or financial impediments exist that would prevent the bank from fulfilling its responsibility under the CRA. The bank received a satisfactory rating at its previous CRA examination conducted by the Federal Reserve Bank of Kansas City on July 12, 2010.

DESCRIPTION OF THE BANK'S ASSESSMENT AREA¹

The bank has designated the contiguous counties of Montrose, Delta, and Ouray located in rural southwest Colorado as its AA. The majority of Montrose County consists of national forest, park, or Bureau of Land Management land. Montrose County includes the city of Montrose and the communities of Naturita, Nucla, and Olathe. Delta County contains the city of Delta and the towns of Cedaredge, Hotchkiss, Orchard City, and Paonia. Ouray County is situated in the San Juan Mountains and includes the municipalities of Ouray and Ridgway.

The AA consists of 18 census tracts, six are moderate-income, 11 are middle-income, and one is upper-income. Three of the bank's offices are located in the moderate-income tracts in Hotchkiss, Cedaredge, and Montrose; two offices are located in the middle-income tracts in Paonia and Delta; and one office is located in an upper-income tract in south Montrose. The bank does not have a facility located in Ouray County.

Labor and Employment Characteristics

Montrose County's principal industrial sectors are manufacturing, healthcare and retail trade. These industries account for approximately 48 percent the area's employment. Montrose County School District, Montrose Memorial Hospital, and Russell Stover Candies are the three largest employers in the county. Other notable employers in the area include Montrose County, Volunteers of America, Wal-Mart Supercenter, City Market, and the City of Montrose according to Colorado Department of Labor data as of February 16, 2014.

The principal industrial sectors in Delta County are construction, retail trade, mining, quarrying, oil and gas extraction, and agriculture. The largest employers in Delta County are Bowie Resources and West Elk/Arch Mines (coal mining), City and County government organizations, and healthcare facilities. Ouray County's largest employers fall into government, education, and tourism sectors.

Population Trends and Economic Characteristics

The bank's AA population, according to 2010 Census data, is economically and demographically similar, with approximately 76,664 residents located in Montrose, Delta, and Ouray Counties. The AA's population is concentrated in Montrose and Delta Counties which contains 94.2 percent of the overall AA population. The population declined from April 1, 2010 to July 1, 2013, in Montrose and Delta Counties by 1.4 percent and 1.5 percent, respectively, while it increased in Ouray County by 2.7 percent. In the state of Colorado, the population is estimated to have grown by 4.6 percent during the same period. The decrease in population may be attributed to weak economic conditions and lack of job growth in the AA.

Census data in 2012 reflects an elevated level of residents age 65-and-over in the AA at 19.4

¹ Sources of economic and demographic data include the 2013 Dun & Bradstreet (D&B), Commerce Department's Bureau of Economic Analysis, the U.S. Census Bureau, and FDIC RECON data.

percent (Montrose County), 21.7 percent (Delta County), and 21.8 percent (Ouray County), which is significantly higher than that of the state of Colorado at 11.8 percent. Community contacts confirmed that the AA has historically contained a large retirement population.

According to the Bureau of Labor Statistics for May of 2014, the unemployment rate in the AA is slowly declining but remains above the state and national averages. Montrose, Delta, and Ouray Counties had unemployment rates of 7.2 percent, 6.4 percent and 4.6 percent, respectively, while the state and national unemployment rates were 5.5 percent and 6.3 percent, respectively, for the same time frame.

Housing Conditions

As of 2010, the median housing values in the Montrose and Delta Counties were \$193,900 and \$201,700, respectively, which was lower than the state of Colorado at \$236,600 and the figure for statewide rural areas, at \$211,122. For Ouray County, the median housing value was \$405,800, which was significantly higher than the state of Colorado and statewide rural areas. The median housing stock age for the AA was 30 years, which is slightly higher than the state of Colorado and statewide rural areas housing stock age of 29 years.

The AA housing affordability ratio², at 20.9 percent for Montrose County and 21.7 percent for Delta County, was slightly lower when compared to the state of Colorado ratio of 23.9 percent and statewide rural ratio of 23.0 percent. However, the housing affordability ratio for Ouray County was significantly lower at 14.4 percent, when compared to the state of Colorado and the statewide rural percentages. A higher ratio generally indicates greater affordability. A community contact stated homes in Ouray mainly consist of secondary residences or vacation homes and that Ouray is home to a large population of early retirees. A community contact stated that 25 percent to 30 percent of people who work in Ouray County reside in Montrose or Delta County where housing is more affordable.

Income Characteristics

According to the 2010 Census, the median family income (MFI) for Montrose and Delta Counties was \$52,640 and \$48,395, respectively, which is significantly lower than the state of Colorado's MFI of \$70,046, but comparable to the figure for statewide rural areas of \$57,817. For Ouray County the MFI was \$65,804, which is slightly lower than the state of Colorado, but above the statewide rural MFI.

In general, Montrose and Delta Counties have a less affluent population than Ouray County, the state of Colorado, and other statewide rural areas. In Montrose and Delta Counties, approximately 34.4 percent and 29.4 percent, respectively, of families were considered upper-income. In Ouray County, 43.3 percent of families were considered upper-income while 40.5 percent of families in the state of Colorado and in statewide rural areas were considered upper-income.

² The affordability ratio is calculated by dividing the area MFI by the median housing value, and a higher ratio generally indicates greater affordability

Table 2 summarizes the demographic and economic characteristics of the bank's AA based on 2010 American Community Survey (ACS) and 2013 D&B data.

TABLE 2 MONTROSE BANK AA DEMOGRAPHICS								
Income Categories	Tract Distribution		Families by Tract Income		Families < Poverty Level as % of Families by Tract		Families by Family Income	
	#	%	#	%	#	%	#	%
Low-income	0	0.0	0	0.0	0	0.0	4,588	21.5
Moderate-income	6	33.3	7,722	36.1	898	11.6	4,665	21.8
Middle-income	11	61.1	12,844	60.1	922	7.2	5,103	23.9
Upper-income	1	5.6	819	3.8	16	2.0	7,029	32.9
Total AA	18	100.0	21,385	100.0	1,836	8.6	21,385	100.0
	Housing Units by Tract	Housing Type by Tract						
		Owner-occupied			Rental		Vacant	
		#	% by tract	% by unit	#	% by unit	#	% by unit
Moderate-income	12,850	8,161	35.7	63.5	3,296	25.6	1,393	10.8
Middle-income	20,712	13,773	60.2	66.5	4,431	21.4	2,508	12.1
Upper-income	1,106	948	4.1	85.7	128	11.6	30	2.7
Total AA	34,668	22,882	100.0	66.0	7,855	22.7	3,931	11.3
	Total Businesses by Tract		Businesses by Tract & Revenue Size					
			Less Than or = \$1 Million		Over \$1 Million		Revenue Not Reported	
			#	%	#	%	#	%
Moderate-income	2,127	37.3	1,984	37.1	81	39.9	62	40.3
Middle-income	3,239	56.8	3,046	57.0	108	53.2	85	55.2
Upper-income	337	5.9	316	5.9	14	6.9	7	4.5
Total AA	5,703	100.0	5,346	100.0	203	100.0	154	100.0
Percentage of Total Businesses:				93.7		3.6		2.7

Based on 2010 Census tract boundaries, 2010 ACS data, and 2013 D&B data.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

The bank's CRA performance was considered satisfactory based on an assessment of its 16-quarter average NLTD ratio, distribution of lending within its AA, level of lending within its AA to geographies of different income levels, as well as its level of lending within its AA to LMI borrowers and to businesses of different revenue sizes. Data utilized for the analysis included the bank's lending performance data, demographic information, and information obtained from members of the community.

Net Loan-to-Deposit Ratio

The bank's NLTD ratio is reasonable given its size, financial condition, competitive operating environment, and the credit needs of the areas it serves. The bank's 16-quarter average NLTD ratio at 56.4 percent, was less than Colorado's statewide ratio at 65.4 percent, Colorado statewide rural ratio at 64.0 percent, U.S. peer ratio at 70.4 percent, and one similarly-situated bank in Delta County at 72.9 percent. However, the bank's NLTD ratio was considerably higher than one bank in its AA with a NLTD ratio of 38.9 percent. In addition, the bank's ratio compared favorably to two similarly-situated banks in a nearby county at 43.2 percent and 54.8 percent.

Community contact interviews supported discussions with bank management referencing a decrease in loan demand in recent years due to a sluggish economy and unemployment resulting from closures of local manufacturing and mining companies. The stagnant and aging population of the bank's AA also may have contributed to an overall lack of loan demand since the prior examination. In addition, the bank sells a majority of its residential real estate loans to secondary market investors, and this lending activity was not reflected in the bank's NLTD ratio. In 2013, the bank originated and sold \$21MM in secondary market residential real estate loans. Further, according to community contacts and bank management, several large regional and national banks provide considerable competition for local lending activity. Community contacts also stated that the credit needs of its area residents and businesses are being met.

Assessment Area Concentration

This performance criterion evaluates the concentration of loans originated by the bank within its AA. This analysis focused on the number of originations rather than the dollar volume, as this is a better representation of the number of borrowers served. Table 3 shows the distribution of loans originated within the bank's AA. The bank originated 90.9 percent of the sampled residential real estate loans and 95.6 percent of the sampled commercial loans to borrowers within its AA. Overall, the bank originated 93.3 percent of the sampled loans within its designated AA which reflects a reasonable effort to serve the credit needs of its AA. The remaining analysis is based solely on the loans originated within the bank's AA.

Bank Loans	Inside				Outside			
	#	\$(000)	#%	\$%	#	\$(000)	#%	\$%
Residential Loans	40	7,470	90.9	90.9	4	749	9.1	9.1
Business Loans	43	7,784	95.6	98.5	2	119	4.4	1.5
Total Loans	83	15,254	93.3	94.6	6	868	6.7	5.4

Distribution by Income Level of Geographies

This performance criterion evaluates the bank's distribution of loans among geographies of various income levels, with emphasis placed on lending in LMI geographies. The bank's residential real estate loans were compared to the percentage of owner-occupied housing units located in each geographic income category, while the bank's business loans were compared to the percentage of businesses located in each geographic income category. The bank's distribution of loans reflects a reasonable dispersion throughout LMI tracts within the AA. Table 4 illustrates the bank's lending distribution by income level of geographies.

TABLE 4 DISTRIBUTION BY INCOME LEVELS OF GEOGRAPHIES MONTROSEBANK'S AA					
Census Tract Income Level	Residential Loans				% of Owner Occupied Units¹
	#	\$(000)	#%	\$%	
Moderate	16	3,624	40.0	48.5	35.7
Middle	19	3,033	47.5	40.6	60.2
Upper	5	814	12.5	10.9	4.1
Census Tract Income Level	Business Loans				% of Businesses²
	#	\$(000)	#%	\$%	
Moderate	22	4,648	51.2	59.7	37.3
Middle	17	2,655	39.5	34.1	56.8
Upper	4	480	9.3	6.2	5.9

¹ Based on 2010 ACS data.
² Based on 2013 D&B data.
 (Note: Total percentages shown may vary by 0.1 percent due to automated rounding differences.)

Residential Real Estate Lending

The bank's distribution of residential real estate loans to geographies of different income levels is considered reasonable. The bank's level of residential real estate lending in the moderate-income tracts was 40.0 percent, which compared favorably to the percentage of owner-occupied units in the moderate-income geographies at 35.7 percent.

Small Business Lending

The bank's distribution of loans to businesses located in LMI geographies is considered excellent. The bank's level of commercial lending to the moderate-income tracts was 51.2 percent, which was significantly higher than the percentage of businesses located in moderate-income tracts at 37.3 percent.

Distribution by Borrower Income and Revenue Size of Businesses

This performance criterion evaluates the bank's distribution of lending to borrowers of different income levels, with emphasis placed on lending to LMI individuals, as well as, the bank's level of lending to businesses of different revenue sizes, primarily small businesses which are

defined as those businesses with gross annual revenues of \$1MM or less. The residential real estate loans were compared to the percentage of families located in the AA by income level, and the commercial loans were compared to the percentage of small businesses located in the AA. The bank's overall distribution of loans to borrowers of different income levels and to businesses of different revenue sizes is considered reasonable.

TABLE 5
DISTRIBUTION BY INCOME LEVEL OF BORROWER AND
REVENUE SIZE OF BUSINESSES
MONTROSEBANK'S AA

Borrower Income Level	Residential Loans				% of Families ¹
	#	\$(000)	#%	\$%	
Low	5	696	12.5	9.3	21.5
Moderate	6	912	15.0	12.2	21.8
Middle	7	873	17.5	11.7	23.9
Upper	22	4,990	55.0	66.8	32.9
Business Revenue	Business Loans				% of Businesses by Revenue ²
	#	\$(000)	#%	\$%	
\$1MM or Less	38	7,576	88.4	97.3	93.7
Over \$1MM	3	153	7.0	2.0	3.6
Income Not Known	2	54	4.7	0.7	2.7

¹ Based on 2010 ACS data.
² Based on 2013 D&B data.
 (Note: Total percentages shown may vary by 0.1 percent due to automated rounding differences.)

Residential Real Estate Lending

The bank's lending to low-income borrowers is considered reasonable at 12.5 percent, compared to the demographic of 21.5 percent. Lending to moderate-income borrowers is also considered reasonable at 15.0 percent, compared to the demographic of 21.8 percent. While the bank's level of lending to both low-income borrowers and moderate-income borrowers was below demographic figures, performance was considered reasonable given various contextual factors. As mentioned earlier, housing affordability within the bank's AA is lower than state and statewide rural figures; the local economy is still recovering from the recent recession; and loan demand in the area has decreased significantly since the prior examination. In addition, bank management stated that national banks and credit unions with locations in Montrose have captured much of the local residential real estate loan demand with the ability to offer lower rates and more diverse mortgage products. Lastly, community contacts indicated that the AA lacks affordable housing for LMI residents, specifically properties of \$150,000 or less.

Small Business Lending

The bank's level of lending to small businesses is considered reasonable. While the bank's lending to small businesses at 88.4 percent was slightly lower than the demographic figure of small businesses in the AA at 93.7 percent, this performance was reasonable given the overall lack of loan demand in the area and strong competition within the bank's market.

FAIR LENDING OR OTHER ILLEGAL CREDIT PRACTICES REVIEW

An evaluation of the bank's fair lending activities was conducted during the examination to determine compliance with the substantive provisions of the antidiscrimination laws and regulations, including the Equal Credit Opportunity Act and the Fair Housing Act. No evidence of discrimination was identified, and the bank has not engaged in any illegal credit practices inconsistent with helping to meet the community credit needs.