



PUBLIC DISCLOSURE

OCTOBER 4, 2010

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**CITIZENS STATE BANK OF CORTEZ
RSSD# 782650**

**77 WEST MAIN STREET
CORTEZ, COLORADO 81321-313**

**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**.*

Citizens State Bank of Cortez (the bank) has a satisfactory record of helping to meet the credit needs of its assessment area (AA), including low- and moderate-income (LMI) families and neighborhoods, in a manner consistent with its resources, operating philosophy, and the credit needs of its communities.

The bank's net loan-to-deposit (NLTD) ratio indicated a reasonable effort to extend credit in a competitive lending market. In addition, a majority of the bank's lending activity occurred inside its AA. The bank's distribution of loans among borrowers of different income levels and to businesses of different revenue sizes reflected a reasonable penetration based on area demographics. Furthermore, the bank's geographic distribution of loans reflected a reasonable dispersion throughout its AA.

SCOPE OF EXAMINATION

The bank's Community Reinvestment Act (CRA) performance was assessed using the small bank examination procedures. Four of the five criteria used in evaluating small bank lending performance were relevant to this review and are as follows:

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

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

The examination evaluated the bank's performance in the criteria articulated above in the context of demographic information of the areas in which the bank operates. Conclusions regarding the four performance criteria were based on data compiled from the bank's major product lines. The major product lines were determined through discussions with bank management, a review of the Report of Condition and Income (Call Report), and a review of the number of loan originations since the bank's last CRA examination in September 2006. Loan products evaluated were commercial, consumer motor vehicle, and residential real estate loan originations. The review included statistical samples of 27 commercial loans from a universe of 59 loans and 31 consumer motor vehicle loans from a universe of 79, which were originated between July 15, 2009 and July 14, 2010. The residential real estate loan review consisted of a sample size of 32 loans from a universe of 89 loans originated between September 18, 2006 and July 16, 2010.

To augment the evaluation, interviews were conducted with members of the local community to ascertain specific credit needs, opportunities, and local market conditions within the AA.

DESCRIPTION OF INSTITUTION

The bank operates from the main office and a branch location in Cortez, Colorado, with onsite automated teller machines (ATMs) at each office. The bank is wholly-owned by Community Bankshares, Inc. (CBI), a two bank holding company located in Greenwood Village, Colorado. According to the June 30, 2010 Federal Deposit Insurance Corporation Market Share Report, the bank has approximately \$70 million in deposits with a deposit market share of 15.45 percent, ranking it fourth out of eight banks in Montezuma County, Colorado. The bank has the ability to meet the credit needs of its AA based on its asset size, financial condition, and credit products offered. As reported in its Call Report dated June 30, 2010, total assets were \$83,754M, of which loans represented \$57,780M. As illustrated in Table 1, commercial, residential real estate, and agricultural loans represent the majority of the bank's lending by dollar volume.

TABLE 1 BANK'S LOAN PORTFOLIO		
Loan Type	Amount (\$000)	Percent of Total
Commercial	25,763	44.6
Residential Real Estate	17,007	29.5
Agricultural	11,989	20.7
Consumer	3,021	5.2
Total Gross Loans	57,780	100.0

The bank has no financial or legal impediments that prevent it from fulfilling its responsibilities under the CRA. The bank received a satisfactory rating at the previous CRA evaluation conducted by the Federal Reserve Bank of Kansas City (Reserve Bank) as of September 5, 2006.

DESCRIPTION OF THE BANK'S ASSESSMENT AREA

The bank has designated its AA as all of Montezuma County, Colorado, which is located in the far southwestern corner of the state. This is the "four corners" region where the boundaries of four states (Colorado, New Mexico, Utah, and Arizona) meet. The AA is not in a Metropolitan Statistical Area (MSA). The area is primarily a rural and mountainous region with the economy divided between tourism, government services, wholesale/retail trade, and agriculture. Much of the county is irrigated cropland, and it produces fruit and beans and provides pastureland for large numbers of cattle and sheep. Major employers in the AA include Ute Mountain Executive

(television/cable services), Ute Mountain Indian Tribe (tribal government and casino), Mesa Verde National Park (rangers), Southwest Memorial Hospital (medical services), and Wal-Mart (retail).

The AA consists of eight census tracts: one low-, one moderate-, and five middle-income. Additionally, there is one census tract which is uninhabited and for which no income data has been reported. Both the unknown- and low-income census tracts are part of the Ute Mountain Indian Reservation, which comprises the southern third of the county. Another third of the county is managed by various federal agencies, including the National Park and Forest Services and the Bureau of Land Management. The remainder is private and state land. There are no upper-income tracts in the AA.

The bank's offices are located in the AA's only moderate-income tract in the town of Cortez. Cortez is the largest community in the county and serves as the county seat. In terms of transportation, Cortez is served by US Highway 160 and the regional airport in Durango. Cortez lies approximately 60 miles west of Durango and 380 miles southwest of Denver. Other communities in the county include Dolores, Mancos, and Towaoc. Towaoc is the capital of the Ute Mountain Tribe.

The AA population has increased almost 6.5 percent from 23,830 enumerated in the 2000 Census to an estimated 25,368 in 2009. Cortez increased 8.2 percent to an estimated 2009 population of 8,632 from 7,977 in 2000.

Based on 2000 Census data, the economics of the area are somewhat less favorable than other nonmetropolitan areas in Colorado. The AA had a lower median family income, a higher concentration of LMI families, and a higher family poverty level.

Selected economic data is shown below:

	Median Family Income ¹	Low & Moderate Income Families (percent) ¹	Families below Poverty level (percent) ¹	2000 Unemployment (percent)	2009 Unemployment (percent) ³	2000 Housing Affordability ^{1,2}
Assessment Area	\$37,747	46.6	13.1	6.9	7.5	29
Colorado Nonmetropolitan Areas	\$44,319	37.7	8.7	4.5	7.6	32
Colorado-State	\$55,883	37.1	6.2	4.3	7.9	29

¹ Based on 2000 Census data (U.S. Census Bureau).

² The housing affordability ratio is measured by dividing the median household income by the median housing value. A higher affordability ratio indicates that the housing stock is more affordable.

³ Based on 2009 American Factfinder (U.S. Census Bureau).

The interviews with members of the community indicated that the county is a very competitive banking market with 15 financial institutions in the area. Community members also indicated a majority of the area's income and employment opportunities are through the tourism industry, which offers lower paying jobs. Many individuals work two or more part-time jobs that are seasonal and do not offer health benefits. The median age of area housing stock is similar to other state nonmetropolitan areas, yet the housing has higher values and is considered less

affordable. This too can be attributed to the tourism focus, in this case the purchase of second homes by out of area persons, which places upward pressure on house values.

Other characteristics of the AA, based on 2000 Census data, are summarized in Table 2.

TABLE 2 BANK'S ASSESSMENT AREA DEMOGRAPHICS								
Income Categories	Tract Distribution		Families by Tract Income		Families < Poverty Level as % of Families by Tract		Families by Family Income	
	#	%	#	%	#	%	#	%
Low-income	1	12.5	371	5.7	129	34.8	1,571	24.0
Moderate-income	1	12.5	909	13.9	181	19.9	1,480	22.6
Middle-income	5	62.5	5,266	80.4	549	10.4	1,480	22.6
Upper-income	0	0.0	0	0.0	0	0.0	2,015	30.8
Unknown-income	1	12.5	0	0.0	0	0.0	0	0.0
Total Assessment Area	8	100.0	6,546	100.0	859	13.1	6,546	100.0
	Housing Units by Tract	Housing Type by Tract						
		Owner-occupied			Rental		Vacant	
		#	% by tract	% by unit	#	% by unit	#	% by unit
Low-income	521	281	4.1	53.9	182	34.9	58	11.1
Moderate-income	1,604	736	10.7	45.9	711	44.3	157	9.8
Middle-income	8,372	5,863	85.2	70.0	1,428	17.1	1,081	12.9
Upper-income	0	0	0.0	0.0	0	0.0	0	0.0
Unknown-income	0	0	0.0	0.0	0	0.0	0	0.0
Total Assessment Area	10,497	6,880	100.0	65.5	2,321	22.1	1,296	12.3
	Total Businesses by Tract	Businesses by Tract & Revenue Size						
		Less Than or = \$1 Million		Over \$1 Million		Revenue Not Reported		
		#	%	#	%	#	%	#
Low-income	25	1.5	20	1.3	2	2.9	3	5.9
Moderate-income	167	9.8	158	10.0	4	5.7	5	9.8
Middle-income	1,513	88.7	1,406	88.8	64	91.4	43	84.3
Upper-income	0	0.0	0	0.0	0	0.0	0	0.0
Unknown-income	0	0.0	0	0.0	0	0.0	0	0.0
Total Assessment Area	1,705	100.0	1,584	100.0	70	100.0	51	100.0
	Percentage of Total Businesses:			92.9		4.1		3.0

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Net Loan-to-Deposit Ratio

The bank's average NLTD ratio is considered reasonable based on the institution's size, financial condition, AA credit needs, and NLTD ratios of competing institutions and national and state peer groups. During the 17-quarter period since the bank's previous CRA

evaluation, the bank's average NLTD was 79.7 percent. Over the most recent eight quarters, the bank's NLTD ratio averaged 83.7 percent. This figure was higher than the eight-quarter averages of all four peer banks that operate near the bank's AA, whose average NLTD ratios range from 46.7 percent to 76.3 percent. Also, the bank's NLTD ratio was higher than the national peer group at 70.5 percent and the state peer group average of 71.1 percent.

Summary of Lending Performance

TABLE 3 SUMMARY OF LENDING PERFORMANCE								
Lending within the Assessment Area								
	Inside AA				Outside AA			
	#	%	\$(000)	%	#	%	\$(000)	%
Residential Real Estate	28	87.5	2,281	81.4	4	12.5	521	18.6
Small Business	20	74.1	2,345	71.8	7	25.9	923	28.2
Consumer Motor Vehicle	28	90.3	280	92.2	3	9.7	24	7.8
TOTAL	76	84.4	4,906	77.0	14	15.6	1,467	23.0
Distribution by Income Level of Geographies								
	% of Bank Loans				% of Owner-Occupied Units			
	Low	Moderate	Middle	Upper	Low	Moderate	Middle	Upper
Residential Real Estate	0.0	28.6	71.4	0.0	4.1	10.7	85.2	0.0
	% of Bank Loans				% of Small Businesses			
	Low	Moderate	Middle	Upper	Low	Moderate	Middle	Upper
Small Business	0.0	30.0	70.0	0.0	1.5	9.8	88.7	0.0
	% of Bank Loans				% of Households			
	Low	Moderate	Middle	Upper	Low	Moderate	Middle	Upper
Consumer Motor Vehicle	3.6	35.7	60.7	0.0	5.0	16.6	78.4	0.0
Distribution by Borrower Income Level and Revenue Size of Business								
	% of Bank Loans				% of Families			
	Low	Moderate	Middle	Upper	Low	Moderate	Middle	Upper
Residential Real Estate	3.6	10.7	14.3	71.4	24.0	22.6	22.6	30.8
	% of Bank Loans				% of Small Businesses			
	100.0				92.9			
	% of Bank Loans				% of Households			
	Low	Moderate	Middle	Upper	Low	Moderate	Middle	Upper
Consumer Motor Vehicle	50.0	17.9	21.4	0.0	26.7	20.2	20.6	32.5

Lending in the Bank's Assessment Area

This core performance criterion evaluates the concentration of loans originated by the bank within its AA as summarized in Table 3. A majority of the loans, 84.4 percent by number and 77.0 percent by dollar volume, were originated within the bank's AA. The bank's performance in this lending test is considered reasonable.

Distribution of Loans by Income Level of Geographies

This performance criterion evaluates the bank's distribution of loans among geographies of various income levels, with emphasis on lending in the LMI tracts. The distribution of consumer, residential real estate, and commercial loans among geographies of various income levels is considered to be reasonable compared to the percentage of households, families, and businesses in each of the geographies.

Consumer Loans - Motor Vehicle:

The bank's level of consumer motor vehicle lending was compared to the percentage of households in each income tract. Approximately 39.3 percent of the bank's motor vehicle loans went to households located in the LMI tracts, which exceeded the area's total households in the LMI tracts of 21.6 percent. The bank's geographic distribution of consumer motor vehicle loans is considered reasonable.

Residential Real Estate Loans:

The bank's level of residential real estate lending was compared to the percentage of owner-occupied housing units located in each geographic income category. As shown in Table 3, residential real estate lending reflected no penetration in the low-income tract but 28.6 percent of the sampled residential real estate loans originated by the bank were made in the moderate-income tract. The bank's moderate-income tract lending exceeds the total percentage of owner-occupied units in the LMI tracts of 14.8 percent or 4.1 percent and 10.7 percent, respectively. The bank's geographic distribution of residential real estate loans is considered reasonable.

Small Business Loans:

The bank's geographic distribution of small business loans reflects a reasonable penetration throughout the AA. The bank's lending patterns appear to be consistent with the AA credit demand and the lending strategy of the bank. According to 2009 Dun & Bradstreet data, 1.5 percent and 9.8 percent of the small businesses in the AA were located in LMI tracts, respectively. The sample revealed no lending activity by the bank in the low-income tract; however, due to the extremely low percentage of businesses reported in the respective tract, the bank's ability to provide commercial credit to the low-income geographies is inherently limited. The bank originated 30.0 percent of its small business loans in the moderate-income tract, which exceeded the total LMI demographic figure of 11.3 percent.

Lending to Borrowers of Different Income Levels and to Businesses of Different Revenue Sizes

This performance criterion evaluates the bank's lending to borrowers of different income levels, primarily LMI individuals, and the bank's lending to businesses of different revenue sizes, particularly those with gross annual revenues of \$1 million or less. The analysis of lending to LMI individuals and to small businesses focus on the number of loans originated, rather than dollar volume, as it is a better indicator of the number of individuals and businesses benefiting from these products. The results of the loan distribution are summarized in Table 3.

Consumer Loans - Motor Vehicle:

The bank's level of lending to borrowers of different income levels was considered reasonable. The total percentage of consumer loans to LMI borrowers was 67.9 percent, which exceeded the percentage of households in the AA classified as LMI of 46.9 percent.

Residential Real Estate Loans:

The bank's lending distribution to LMI borrowers is considered reasonable as compared to the percentage of LMI families in the area and in consideration of economic and demographic factors. The bank originated fewer residential real estate loans to LMI borrowers than suggested by area demographics. The bank originated 14.3 percent of its residential real estate loans to LMI borrowers, while 46.6 percent of families in the AA are considered LMI. Community members stated the bank's AA is in need of affordable housing. Approximately 53.7 percent of occupied housing in the AA is valued at \$100,000 or more, resulting in relatively low affordability. Currently, 22.1 percent of the housing available in the AA are rental units and 33.6 percent of the renters in the AA have rent costs that exceed 30.0 percent of their income. Furthermore, all housing in the sole low-income tract is considered government housing with little or no individual ownership. These reasons, together with the area economics and high number of financial institutions, tend to reduce the overall opportunity for the bank to lend to LMI borrowers for housing related purposes.

Small Business Loans:

The bank's level of lending to small businesses was considered reasonable. The percentage of loans to small businesses was higher than the percentage of small businesses in the bank's AA. The analysis revealed that 100.0 percent of the loans originated were to small businesses compared to the number of small businesses in the bank's AA at 92.9 percent.

FAIR LENDING OR OTHER ILLEGAL CREDIT PRACTICES REVIEW

The bank is in compliance with the substantive provisions of the antidiscrimination laws and regulations. A review of bank policies and procedures, credit applications, loans and denials, and staff interviews revealed no prohibited practices designed to discourage loan applicants. Furthermore, the bank had not engaged in other illegal credit practices inconsistent with helping to meet the credit needs of its communities.

GLOSSARY OF COMMON CRA TERMS

(For additional information, please see the Definitions section of Regulation BB at 12 CFR 228.12.)

Assessment Area – The geographic area(s) delineated by the bank and used in evaluating the bank’s record of helping to meet the credit needs of its community. The assessment area must include the geographies where the main office, branches, and deposit-taking automated tellers machines are located. The assessment area must consist only of whole geographies, may not reflect illegal discrimination, and may not arbitrarily exclude low- or moderate-income geographies.

Census Tracts – Census tracts are small, relatively permanent geographic entities within counties delineated by a committee of local data users. Census tracts are designed to be homogenous with respect to population characteristics, economic status, and living conditions to allow for statistical comparisons and average about 4,000 inhabitants.

Community Development – Includes affordable housing (including multifamily rental housing) for low- and moderate-income individuals; community services targeted to low- and moderate-income individuals; activities that promote economic development by financing businesses or farms that have gross annual revenues of \$1 million or less; or activities that revitalize or stabilize low- or moderate-income geographies, designated distressed or underserved nonmetropolitan middle-income areas or designated disaster areas.

Community Development Loan – A loan that has community development as its primary purpose and (except in the case of a wholesale or limited-purpose bank):

1. Has not been reported or collected by the bank or an affiliate as a home mortgage, small business, small farm, or consumer loan, unless it is a multifamily dwelling loan, and
2. Benefits the bank’s assessment area(s) or a broader statewide or regional area that includes the bank’s assessment area(s).

Community Development Service – A service that has as its primary purpose community development, is related to the provision of financial services, has not been considered in the evaluation of the bank’s retail banking services, benefits the banks assessment area(s) or a broader statewide or regional area that includes the bank’s assessment area, and has not been claimed by other affiliated institutions.

Consumer Loans – Loans to individuals for household, family, and other personal expenditures. These loans do not include real estate-secured loans.

Dun & Bradstreet Data – Data collected by Dun & Bradstreet regarding types of businesses and their respective gross annual revenues. The data can be sorted by geographies.

Geography – A census tract delineated by the U.S. Bureau of the Census in the most recent decennial census.

Income Level – Both geographies and individuals can be described in terms of their income levels. In MSAs, the level is based on the MSA median family income (**MFI**). In nonMSA areas, the level is based on the statewide, nonMSA median family income.

Low-Income – Less than 50 percent of the area median family income

Moderate-Income – At least 50 percent and less than 80 percent of the area median family income

Middle-Income – At least 80 percent and less than 120 percent of the area median family income

Upper-Income – At least 120 percent or more of the area median family income

LMI – Collectively, low- and moderate-income families or tracts.

Metropolitan Statistical Area (MSA) – The general concept of an MSA is that of a core area containing a large population nucleus, together with adjacent communities having a high degree of economic and social integration with that core. Generally, a single city with at least 50,000 inhabitants or an urbanized area with a total population of at least 100,000 would meet the definition of an MSA.

Qualified Investment – A lawful investment, deposit, membership share, or grant that has as its primary purpose community development.

Small Business – A business with gross annual revenues of \$1 million or less.

Small Farm – A farm with gross annual revenues of \$1 million or less.

Small Loan(s) to Business(es) – A loan included in “loans to small businesses” as defined in the Consolidated Report of Condition and Income (“Call Report”). These loans have original amounts of \$1 million or less and typically are either secured by nonfarm or nonresidential real estate or are classified as commercial and industrial loans.

Small Loan(s) to Farm(s) – A loan included in “loans to small farms” as defined in the instructions for preparation of the Call Report. These loans have original amounts of \$500 thousand or less and are either secured by farmland, or are classified as loans to finance agricultural production and other loans to farmers.

