

PUBLIC DISCLOSURE

December 8, 2003

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**NorthStar Bank
RSSD #2194426**

**5602 15th Avenue NW
Seattle, Washington 98107**

**Federal Reserve Bank of San Francisco
101 Market Street
San Francisco, California 94105**

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.

TABLE OF CONTENTS

INSTITUTION.....	1
PERFORMANCE CONTEXT	
Description of Institution.....	2
Description of Assessment Area.....	3
CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA	
Scope of Examination	5
Loan-to-Deposit Ratio	5
Lending in Assessment Area	6
Lending by Business Revenue and Borrower Income	6
Geographic Distribution of Loans	7
Response to Complaints.....	9
Compliance with Fair Lending Laws and Regulations	9
GLOSSARY OF TERMS	10

INSTITUTION

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

The major factors supporting the satisfactory rating include:

- A significant majority of small business and home mortgage loans were originated within the assessment area.
- The distribution of small business loans reflects a good penetration among businesses of different sizes and among census tracts of different income levels.
- Home mortgage loan distributions to borrowers of different income levels and in census tracts of different income levels are adequate.

PERFORMANCE CONTEXT

Description of Institution

NorthStar Bank is a \$111 million full service community bank headquartered in the Seattle neighborhood of Ballard. The bank was founded in 1994 as Fremont First National Bank and after adding a branch in 1997 began doing business as NorthStar Bank. Effective June 30, 2003, NorthStar Bank converted from a national chartered financial institution to a state chartered member of the Federal Reserve System.

The bank offers a range of deposit and lending products through its main office in Ballard and a branch office in the nearby Seattle neighborhood of Fremont. The institution's focus is serving the credit needs of commercial businesses and providing residential loans to customers within the city limits of Seattle. Consumer loans are provided on an accommodation basis to the bank's business loan customers. Its market niche for residential loans is the Seattle floating home market. This unique type of dwelling is by definition, located on the water along the shoreline of inland bodies of water. Suitable locations for floating homes are limited and tend to be concentrated in middle- and upper-income census tracts. NorthStar Bank takes pride in noting on its web site that it is the leading provider of financing for floating homes in Seattle's floating home community. Traditional home loan services are provided via third-party mortgage brokerage services.

NorthStar Bank's strategic focus is reflected in its loan portfolio mix as a significant percentage has a business purpose or is secured by residential real estate. The table below details the bank's loan portfolio as of September 30, 2003.

Loan Type	Dollar Amount (000s)	Percent of Total Loans
Commercial/Industrial and Non-Farm Non-Residential Real Estate	\$52,044	54.0%
Secured by 1-4 Family Residential Real Estate	\$26,803	27.8%
Construction	\$11,083	11.5%
Consumer	\$2,716	2.8%
Multi-Family Housing	\$ 2,662	2.7%
Credit Cards	\$954	1.0%
Other (Lease Financing)	\$145	0.2%
Total	\$96,407	100.0%

There are no legal or financial impediments that would inhibit the bank's ability to meet the credit needs of its community consistent with its business strategy, size, resources, and the local economic climate. NorthStar Bank's CRA performance was rated satisfactory at its previous examination conducted as of August 27, 1998, by the Office of the Comptroller of the Currency.

Description of Assessment Area

NorthStar Bank's designated assessment area consists of the entire city of Seattle, Washington and has not changed since its previous CRA performance evaluation.

Based on the 1990 census data, the bank's assessment area has a population of approximately 517,000. The following table illustrates the 1990 census data that was used to help develop the performance context. Both of the bank's offices are located in moderate-income census tracts. Tracts designated "NA" reflect income data which was not available.

1990 Census Tract Income Level	Census Tracts		Population by Census Tract		Families by Census Tract		Households by Census Tract	
	Number	Percent	Number	Percent	Number	Percent	Number	Percent
Low	9	6.7%	30,733	6.0	4,755	4.2%	10,042	4.2%
Moderate	29	21.6%	132,786	25.7	25,690	22.6%	60,618	25.6%
Middle	65	48.5%	272,212	52.7	63,857	56.1%	127,740	53.9%
Upper	20	14.9%	79,647	15.4	19,587	17.2%	38,531	16.3%
NA	11	8.2%	1,005	0.2	0	0.0%	0	0.0%
Total	134	100.0%	516,383	100.0	113,889	100.0%	236,931	100.0%

The bank's assessment area is a competitive market for financial services. Deposits are concentrated in two national banks and one savings bank that collectively hold 75 percent of deposits in the Seattle market. With approximately \$89 million in deposits (less than half of one percent) NorthStar Bank ranks twentieth out of thirty-nine institutions in the area with respect to deposit market share.¹

Seattle is home to a number of major industries and service organizations. It is a major center for aerospace products and manufacturing. Also central to Seattle's economy is advanced technology such as computer software, electronics, medical equipment and environmental engineering. Two of its largest employers are Boeing Aircraft and Microsoft Corporation.²

The regional economy has been negatively impacted by the recent recession. Seattle's unemployment rate grew to 6.6 percent at year end 2002, up from 5.2 percent at year end 2001.³ The employment picture was heavily influenced by layoffs at Boeing Aircraft which is Seattle's dominant employer.⁴ Since the September 11, 2001, terrorist attack, Boeing has targeted 31,850 jobs for elimination. Through November of 2002, 25,640 workers have left Boeing's payroll,

¹ Federal Deposit Insurance Corporation, Market Share and Banking Holding Company, Summary of Deposits market Share Report, June 30, 2003, (accessed January 28, 2004); available from <http://www2.fdic.gov/sod/>.

² Seattle Washington Resource Guide: Seattle; (accessed February 6, 2004) available from <http://www.pe.net/~rksnow/wacountyseattle.htm>.

³ *Précis® METRO: Oakland* (West Chester, Pennsylvania: Economy.com, April 2003).

⁴ *Ibid.*

15,650 of them in the Seattle area. Additionally, the high-technology industry felt the continued effects of reductions in corporate spending. This condition affected local companies like Microsoft, one of the largest companies in the United States, and other similar-type companies with a regional and state presence. Washington state's unemployment rate hit a high of 7.6 percent in January, 2002, reflecting continued layoffs in the both the aerospace and high-technology sectors. As the U.S. economy recovers from what's been called a mild recession, the Pacific Northwest continues to struggle, with rates well in excess of the national unemployment rate of 5.6 percent.⁵

Despite these economic downturns, Seattle remains a growing city. Net population migration into the area remains positive with population increases in both 2001 and 2002.⁶ Demand factors and falling interest rates caused housing prices to increase, making it difficult for some lower-income and first-time home buyers to afford the requisite down-payments.⁷ According to the Washington Center for Real Estate Research, for the period ending December 31, 2002, the median price for a single family home in King County (which includes Seattle) equaled \$277,000, which is an increase of approximately 11 percent from early 2001.

There is a significant percentage of small businesses in the area. According to 2002 Dun & Bradstreet data, approximately 20,000 or 83 percent of the 24,000 non-farm businesses located in Seattle have gross annual revenues of less than \$1 million. The following table illustrates the concentration of businesses per tract income level.

Census Tract Income Level	Census Tracts		2002 Dun & Bradstreet			
	Number	Percent	Number Small Businesses	Percent Small Businesses	Number Total Businesses	Percent Total Businesses
Low	9	6.7%	1,220	6.1%	1,561	6.4%
Moderate	29	21.6%	5,035	25.0%	6,284	25.9%
Middle	65	48.5%	9,252	46.0%	10,805	44.5%
Upper	20	14.9%	4,594	22.9%	5,655	23.3%
NA	11	8.2%	-	-	-	-
Total	134	100.0%	20,101	100.0%	24,305	100.0%

Demographic and economic information, including interviews with community representatives, indicated that there are many opportunities for financial institutions to meet local area credit needs. Working capital loans and letters of credit are needed to assist local small businesses. Financial institutions can also participate in SBA lending programs that target the credit needs of these companies. In addition, programs that provide down-payment assistance for first-time homebuyers also fulfill an important need.

⁵ *Seattle Times*, Wednesday, October 16, 2002; (accessed February 6, 2004) available from <http://archives.seattletimes.nwsourc.com>.

⁶ *Précis® METRO: Oakland* (West Chester, Pennsylvania: Economy.com, April 2003).

⁷ *Washington State's Housing Market: A Supply/Demand Assessment, Third Quarter 2003*, Washington Center for Real Estate Research/Washington State University; available from <http://cbe.wsu.edu/~wrcer>.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Scope of Examination

The bank's CRA performance was evaluated using the five performance standards for small banks:

- Lending volume in comparison to deposits (Loan-to-Deposit Ratio);
- Lending inside and outside the bank's assessment area (Lending in Assessment Area);
- Distribution of lending to businesses of different revenue sizes and borrowers of different income levels (Lending by Business Revenue and Borrower Income); and
- Dispersion of lending throughout the assessment area (Geographic Distribution of Loans).

Responsiveness to consumer complaints was not evaluated as the bank received no CRA-related complaints.

The CRA performance was based on small business and Home Mortgage Disclosure Act ("HMDA") reported home purchase and home refinance loans originated between January 1, 2001, and December 31, 2002. Consistent with the bank's commercial loan focus, small business loans carried greater weight in the evaluation. A total of 142 small business loans, 34 home purchase, and 28 home refinance loans were originated during the review period and these loans were used in the evaluation *Lending in Assessment Area*. A statistical sample of loans extended inside the assessment area was used for evaluating *Lending by Business Revenue and Borrower Income* and *Geographic Distribution of Loans*. The statistical sample included 61 small business, 32 home purchase, and 28 home refinance loans.

Loan-to-Deposit Ratio

The bank's loan-to-deposit ratio is reasonable and meets standards for satisfactory performance. The eight-quarter average loan-to-deposit ratio of 95.3 percent exceeds the state's loan-to-deposit average of 85.0 percent.

Lending in Assessment Area

The concentration of loans extended inside the assessment area meets standards for satisfactory performance. As depicted in the table below, a majority of each loan type was extended in the assessment area.

Loan Type	Percent Number Inside Assessment Area	Percent Dollar Amount Inside Assessment Area
Small Business	74%	73%
Home Purchase	94%	90%
Home Refinance	100%	100%

Lending by Business Revenue and Borrower Income

Lending by business revenue and borrower income meets standards for satisfactory performance.

Small Business Lending

Lending to businesses of different revenue sizes is good. A majority, 62 percent, of the small business loans were extended to businesses with gross annual revenues of \$1 million or less. Comparatively, 83 percent of all businesses within the assessment area are small businesses. This performance surpasses that of the aggregate market, which extended only 32 percent to these businesses.

Home Mortgage Loans

Considering the bank's business strategy and the uniqueness of floating home loans, lending levels reflect adequate responsiveness to assessment area credit needs. Due to higher credit risk, these properties typically require higher down payments than their non-floating counterparts. In addition to being somewhat expensive to purchase and maintain, many require monthly slip rental fees in addition to the mortgage payment. Accordingly, home purchase and refinance loans were concentrated in middle- and upper-income borrowers. While the distribution of loans to low- and moderate-income families exhibited less favorable comparisons, they are reasonable given market conditions and these families' relative ability to finance a floating home.

The following table details the distribution of NorthStar Bank's home purchase and home refinance loans by borrower income level.

Borrower Income Level	Families	Home Purchase Loans	Home Refinance Loans
Low	21.7%	9.4%	0.0%
Moderate	20.1%	15.6%	14.3%
Middle	24.4%	25.0%	17.9%
Upper	33.8%	50.0%	67.9%

Geographic Distribution of Loans

The geographic distribution of loans meets standards for satisfactory performance.

Small Business Lending

The geographic distribution of small business loans throughout the assessment area is good. The following table illustrates the bank's distribution of lending against aggregate small business lending and percentage of these companies in the assessment area.

Census Tract Income Level	Small Businesses	Bank Small Business Lending	Aggregate Small Business Lending
Low	6.4%	1.6%	6.0%
Moderate	25.3%	36.1%	27.4%
Middle	44.3%	41.0%	43.7%
Upper	24.0%	21.3%	23.0%

Bank performance in moderate-income census tracts exceeds aggregate performance and the percentage of businesses located within moderate-income census tracts. Both bank offices are located in moderate-income census tracts which helps complement bank marketing efforts in these areas. The low distribution of the bank's small business loans in low-income census tracts is attributed to the relative distance between the bank's branch locations and the low-income census tracts in the assessment area.

Home Mortgage Loans

The geographic distribution patterns are reasonable considering the bank's business strategy targeting Seattle's floating home market. The following table shows the distribution of the bank's home purchase and home refinance loans within its assessment area level. The low level of lending in low- and moderate-income census tracts is due to the fact that the inland waterways where floating homes are located are predominately middle- and upper-income census tracts.

Census Tract Income Level	Owner Occupied Units	Home Purchase Loans	Home Refinance Loans
Low	1.8%	0.0%	0.0%
Moderate	18.1%	6.3%	3.6%
Middle	60.1%	37.5%	14.3%
Upper	20.0%	56.3%	82.1%

Response to Complaints

NorthStar Bank received no complaints relating to its CRA performance since the previous examination. Accordingly, this component was not used to determine the overall performance rating.

Compliance with Fair Lending Laws and Regulations

No violations of the substantive provisions of the anti-discrimination laws and regulations were identified at this examination. Additionally, there was no evidence of prohibitive lending practices.

GLOSSARY OF TERMS

Aggregate lending: The number of loans originated and purchased by all lenders subject to reporting requirements as a percentage of the aggregate number of loans originated and purchased by all lenders in the MSA/assessment area.

Block numbering area (“BNA”): Statistical subdivisions of a county for grouping and numbering blocks in non-metropolitan counties where local census statistical area committees have not established census tracts. BNAs do not cross county lines.

Census tract: Small subdivisions of metropolitan and other densely populated counties. Census tract boundaries do not cross county lines; however, they may cross the boundaries of metropolitan statistical areas. They usually have between 2,500 and 8,000 persons, and their physical size varies widely depending upon population density. Census tracts are designed to be homogeneous with respect to population characteristics, economic status, and living conditions to allow for statistical comparisons.

Community development: Affordable housing for low- or moderate-income individuals; community services targeted to low- or moderate-income individuals, activities that promote economic development by financing businesses or farms that meet the size eligibility standards of the Small Business Administration’s Development Company or Small Business Investment Company programs (13 CFR 121.301) or have gross annual revenues of \$1 million or less; or, activities that revitalize or stabilize low- or moderate-income geographies,

Consumer loan: A loan to one or more individuals for household, family, or other personal expenditures. A consumer loan does not include a home mortgage, small business, or small farm loan. This definition includes the following categories of loans: motor vehicle, credit card, home equity, other secured loan, and other unsecured loan.

Family: Includes a householder and one or more other persons living in the same household who are related to the householder by birth, marriage, or adoption. The number of family households always equals the number of families; however, a family household may also include non-relatives living with the family. Families are classified by type as either a married couple family or other family, which is further classified into “male householder” (a family with a male householder and no wife present) or “female householder” (a family with a female householder and no husband present).

Full review: Performance under the lending, investment, and service tests is analyzed considering performance context, quantitative factors (e.g., geographic distribution, borrower distribution, total number and dollar amount of investments, branch distribution) and qualitative factors (e.g., innovation, complexity).

Geography: A census tract or a block numbering area delineated by the U.S. Bureau of the Census in the most recent decennial census.

Home Mortgage Disclosure Act (“HMDA”): The statute that requires certain mortgage lenders that do business or have banking offices in a metropolitan statistical area to file annual summary reports of their mortgage lending activity. The reports include such data as the race, gender, and the income of applications, the amount of loan requested, and the disposition of the application (e.g., approved, denied, and withdrawn).

Home mortgage loans: Include home purchase and home improvement loans as defined in the HMDA regulation. This definition also includes multifamily (five or more families) dwelling loans, loans for the purchase of manufactured homes and refinancings of home improvement and home purchase loans.

Household: Includes all persons occupying a housing unit. Persons not living in households are classified as living in group quarters. In 100 percent tabulations, the count of households always equals the count of occupied housing units.

Low-income: Individual income that is less than 50 percent of the area median income, or a median family income that is less than 50 percent in the case of geography.

Limited review: Performance under the lending, investment, and service tests is analyzed using only quantitative factors (e.g., geographic distribution, borrower distribution, total number and dollar amount of investments, branch distribution).

Market share: The number of loans originated and purchased by the institution as a percentage of the aggregate number of loans originated and purchased by all lenders in the MSA/assessment area.

Metropolitan area: Any primary metropolitan statistical area (“PMSA”), metropolitan statistical area (“MSA”), or consolidated metropolitan area (“CMSA”), as defined by the Office of Management and Budget, with a population of 250 thousand or more, and any other area designated as such by the appropriate federal financial supervisory agency.

Moderate-income: Individual income that is at least 50 percent and less than 80 percent of the area median income, or a median family income that is at least 50 percent and less than 80 percent in the case of geography.

Middle-income: Individual income that is at least 80 percent and less than 120 percent of the area median income, or a median family income that is at least 80 percent and less than 120 percent in the case of geography.

Multifamily: Refers to a residential structure that contains five or more units.

Optional loans: Includes any unreported category of loans for which the institution collects and maintains data for consideration during a CRA examination. Also includes consumer loans and other loan data an institution may provide concerning its lending performance.

Owner-occupied units: Includes units occupied by the owner or co-owner, even if the unit has not been fully paid for or is mortgaged.

Qualified investment: A qualified investment is defined as any lawful investment, deposit, membership share, or grant that has as its primary purpose community development.

Small loans to business: 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 are either secured by nonfarm nonresidential properties or are classified as commercial and industrial loans.

Small loans to farms: A loan included in “loans to small farms” as defined in the instructions for preparation of the Consolidated Report of Condition and Income (Call Report). These loans have original amounts of \$500 thousand or less and are either secured by farmland, including farm residential and other improvements, or are classified as loans to finance agricultural production and other loans to farmers.

Owner-occupied units: Includes units occupied by the owner or co-owner, even if the unit has not been fully paid for or is mortgaged.

Qualified investment: A qualified investment is defined as any lawful investment, deposit, membership share, or grant that has as its primary purpose community development.

Upper-income: Individual income that is more than 120 percent of the area median income, or a median family income that is more than 120 percent in the case of geography.