

## **PUBLIC DISCLOSURE**

November 17, 2003

### **COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION**

First State Bank  
RSSD #867650

309 S. Old Betsy Road  
Keene, Texas 76059

Federal Reserve Bank of Dallas

2200 North Pearl Street  
Dallas, Texas 75201

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.

The performance of First State Bank in originating loans to meet the credit needs of all segments of its community is rated Satisfactory for the period covered by this evaluation. The factors supporting this rating include:

- A majority of the residential real estate and small business loans were originated inside the bank's assessment area, including 87% of the number and 83% of the dollar volume of loans reviewed;
- An excellent penetration of loans among individuals of different income levels and businesses of different sizes, as demonstrated by 59% of the residential loans made to low- and moderate-income borrowers, as well as 98% of the loans to small businesses;
- A reasonable dispersion of loans throughout the assessment area, and;
- A more than reasonable loan-to-deposit ratio of 85% as of June 30, 2003, with a quarterly average of 77% since the previous CRA evaluation.

## DESCRIPTION OF INSTITUTION

First State Bank, Keene, Texas (FSB) is a full-service, retail bank operating three banking offices in the Forth Worth-Arlington, Texas Metropolitan Statistical Area (MSA) in north central Texas. The main bank facility is located in the Johnson County town of Keene, approximately 30 miles south of Fort Worth, and branch offices which are located in Cleburne and Burleson. The bank also operates a motor bank in Joshua and a loan production office in Burleson. FSB offers commercial, agricultural, construction, home mortgage, home improvement, automobile, and unsecured consumer loans. A full line of deposit services is offered, and the bank operates automated teller machines (ATMs) at the Keene, Burleson, and Joshua locations, as well as two off-premise ATMs in Cleburne and one in Burleson.

FSB is a subsidiary of Nichols Bancshares, Dover, Delaware, which is owned by Keene Bancorp (Keene). Keene, formerly a one bank holding company, was merged into Pinnacle Bancorp, Inc., Central City, Nebraska, in September 2002. Affiliates include Skybank LLC, Harlan, Iowa; Bank of Colorado, Fort Collins, Colorado; First National Bank, Abilene, Kansas; Pinnacle Bank, Papillion, Nebraska; Pinnacle Bank Wyoming, Torrington, Wyoming; and Western Bank, Gallup, New Mexico.

As of June 30, 2003, FSB reported total assets of \$135.3 million, total deposits of \$112.8 million, gross loans of \$97.1 million, and a loan-to-deposit ratio of 84.8%. The following table provides further detail on the bank's loan portfolio mix.

LOAN PORTFOLIO MIX JUNE 30, 2003	DOLLAR VOLUME (000'S)	PERCENT OF LOAN PORTFOLIO
<u>Real Estate</u>		
Construction/Land Development	4,497	4.63%
Agriculture	1,464	1.51%
1-4 Family – Revolving	653	0.67%
1-4 Family	20,224	20.83%
Multi-family	967	1.00%
Commercial	21,787	22.44%
Total Real Estate	49,592	51.09%
Consumer	24,067	24.79%
Commercial/Industrial	22,806	23.49%
Agricultural	232	0.24%
All Other	376	0.39%
<b>Gross Loans</b>	<b>97,073</b>	<b>100.00%</b>

As illustrated by the loan mix, FSB is primarily a commercial and consumer lender, with almost 46% of its portfolio concentrated in commercial real estate, commercial and industrial loans and 25% in consumer related loans. Since the previous CRA evaluation in 1999, the bank's total assets have more than doubled and the loan portfolio has increased almost 200%. The bank

received a satisfactory rating at its last CRA assessment conducted by the Federal Deposit Insurance Corporation as of March 16, 1999. No legal or financial factors exist that would hinder the bank's ability to meet the credit needs of its assessment area.

## **DESCRIPTION OF THE ASSESSMENT AREA**

FSB's assessment area (AA) consists of Johnson County, one of the four counties that comprise the Fort Worth-Arlington, Texas MSA. The 2001 estimated population for Johnson County was 132,247. Johnson County municipalities include the county seat of Cleburne, as well as Alvarado, Burleson, Joshua, and Keene.

As of June 30, 2003, there were 15 insured institutions operating 31 banking offices in Johnson County. Wells Fargo Bank Texas, N.A. held 21.7% market share of the county's \$851 million in insured deposits, followed by First Financial Bank, N.A., Cleburne with 21.3% and Community Bank, Granbury with 13.6%. FSB ranked fourth, with 13.3% market share of the county's deposits.

Demographic and economic information also impact the bank's performance context and are discussed below. Information was obtained from publicly available sources including the U.S. Department of Commerce's Bureau of the Census, 1990 and 2000; the U.S. Department of Labor; the U.S. Department of Housing and Urban Development (HUD); Dun & Bradstreet; and the Texas Workforce Commission.

The following chart details selected characteristics of the assessment area:

<b>FIRST STATE BANK, KEENE, TEXAS</b>				
<b>Assessment Area Characteristics:</b>				
<b>Tract Summary<sup>1</sup></b>				
	<b>1990</b>		<b>2000</b>	
Total Number of Tracts	15		23	
Number/Percent of Low-Income Tracts	0	0%	0	0%
Number/Percent of Moderate-Income Tracts	2	13%	6	26%
Number/Percent of Middle-Income Tracts	12	80%	16	70%
Number/Percent of Upper-Income Tracts	1	7%	1	4%
<b>Income Summary<sup>2</sup></b>				
Total Families	26,782		34,633	
Percent Low-Income Families	22.3%		19.2%	
Percent Moderate-Income Families	19.6%		21.4%	
Percent Middle-Income Families	27.1%		25.3%	
Percent Upper-Income Families	31.0%		34.0%	
Percent Below Poverty Level	8.8%		6.9%	
<b>Unemployment Summary<sup>3</sup></b>				
	<b>2001</b>		<b>2002</b>	
Labor Force	64,823		66,282	
Percent Unemployment (Assessment Area)	4.1%		6.1%	
Percent Unemployment (State)	4.8%		6.3%	
<b>Miscellaneous Information<sup>4</sup></b>				
Total Population, 2001 Estimate	132,247			
Total Housing Units – 1990/2000	37,029	46,269		
Percentage Owner-Occupied Units to Total Units	68.8%		74.4%	
Percentage Rental Units to Total Units	21.5%		19.9%	
Percentage Vacant Units to Total Units	9.6%		5.7%	
Total Business Establishments	815			

**Geographic Characteristics** - The bank's assessment area contained 23 census tracts according to the 2000 census, none of which are considered low-income. Of the 23 census tracts, 26% are moderate-income, 70% middle-income, and 4% upper-income census tracts. In 1990, Johnson County contained 15 census tracts, with 13% considered moderate-income, 80% middle-income, and 7% upper-income.

<sup>1</sup> Source: U.S. Census Bureau, 1990 and 2000

<sup>2</sup> Source: U.S. Dept. of Housing and Urban Development, 2000; U.S. Census Bureau, 1990 and 2000

<sup>3</sup> Source: Texas Workforce Commission, 2001 & 2002 Annual Averages

<sup>4</sup> Source: U.S. Census Bureau, 1990 and 2000; Dun & Bradstreet, 2002

***Income Characteristics*** - According to the 1990 census, there were 26,782 families in the assessment area. Twenty-two percent of the 1990 families were low-income, 20% moderate-income, 27% middle-income, and 31% were upper-income families. The 2000 census reflected a 29% increase in total families in the AA to 34,633. The distribution by family income level reflected a lower level of low-income families and an increase in upper-income families. The poverty level declined from almost 9% in 1990 to just under 7% in 2000.

***Housing Characteristics*** - Total housing units in the AA increased almost 25% from 37,029 in 1990 to 46,269 in 2000. In 1990, sixty-nine percent of housing units were owner-occupied, 21% were rental properties, and 10% were vacant. Sixty-eight percent of AA housing units were single-family, 5% were multifamily dwellings with five or more units, 6% were 2-4 family units, and 21% were mobile homes. The distribution of the owner-occupied housing units by census tract income level was 5% moderate-income, 90% middle-income, and 5% upper-income.

Owner-occupancy rose to 74% as of the 2000 census. Sixty-five percent of AA housing units are single-family, 6% are 2-4 family units, 3% are multifamily dwellings with five or more units, and 26% are mobile homes. The distribution of the owner-occupied housing units by census tract income level is 17% moderate-income, 78% middle-income, and 5% upper-income. The median value of owner-occupied housing units was \$61,374 in 1990 and \$83,935 in 2000.

***Labor, Employment and Economic Characteristics*** – The Johnson County labor force totals over 66,000, and the area’s annual average unemployment rate rose from 4.1% in 2001 to 6.1% in 2002. Many residents commute to work in the Fort Worth-Arlington area. The local economy is supported by agribusiness, the railroad and manufacturing and distribution. Major employers include Wal-Mart, Harris Methodist Walls Regional Hospital, Gunderson Southwest, Johns Manville, Rangaire and Rubbermaid.

## CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

### Loan-To-Deposit Ratio

FSB's net loan-to-deposit (LTD) ratio is considered more than reasonable, given the bank's size and financial condition, the credit needs of the assessment area, and the competitive local banking environment. As of June 30, 2003, FSB's LTD ratio was 84.9%, and the quarterly average for the 18 quarters since the previous evaluation was 76.8%.

To better understand the bank's performance in relation to its assessment area, a comparison of similarly situated banks was performed. These banks were chosen for analysis based on their proximity and similar size and structure. As noted, FSB's LTD ratios are higher than the similarly situated banks in the AA.

BANK	COUNTY	TOTAL ASSETS 6/30/2003*	LTD RATIO 6/30/2003	QUARTERLY AVG. LTD RATIO
<b>First State Bank Keene, Texas</b>	<b>Johnson</b>	<b>\$135,329</b>	<b>84.85%</b>	<b>76.75%</b>
First State Bank Grandview, Texas	Johnson	\$52,166	75.24%	67.29%
First Financial Bank Cleburne, Texas	Johnson	\$202,888	56.75%	57.81%

\*In thousands

### Lending in Assessment Area

The institution's performance demonstrates a good response to the credit needs of its AA, as the majority of the loans sampled were to borrowers residing or operating inside the AA. The institution's loan performance was evaluated based upon the residential real estate loans (home mortgage, refinance, and home improvement loans) reported on the bank's Home Mortgage Disclosure Act Loan Application Registers (HMDA LARs) for the years 2001 and 2002. FSB originated a total of 420 HMDA-reportable loans for \$12.4 million during the two-year period. A sample of 58 small business loans totaling \$2.5 million extended in 2003 was also reviewed.

This analysis revealed that a majority of loans are originated within the bank's designated assessment area, demonstrating good responsiveness to the credit needs of the community. As indicated in the following chart, 88% of the HMDA loans and 83% of the sampled small business loans were made to borrowers living or operating in Johnson County.



ANALYSIS OF LENDING IN THE ASSESSMENT AREA								
Loan Type	Inside Assessment Area				Outside Assessment Area			
	#	%	\$000's	% of \$	#	%	\$000's	% of \$
2001-2002 HMDA	369	87.9	10,700	86.1	51	12.1	1,721	13.9
2003 Small Business	48	82.8	884	59.6	10	17.2	598	40.4
<b>TOTAL</b>	<b>417</b>	<b>87.2</b>	<b>11,584</b>	<b>83.3</b>	<b>61</b>	<b>12.8</b>	<b>2,319</b>	<b>16.7</b>

The remaining analysis was conducted using only those loans originated within the assessment area. The following table provides further detail on the geographic and borrower distribution of the bank's HMDA loans.

FIRST STATE BANK, KEENE, TEXAS 2001 - 2002 HMDA LENDING								
Income Categories	HMDA By Tract Income				By Borrower Income			
	#	%	\$	%	#	%	\$	%
Low	0	0.0%	0	0.0%	29	21.0%	606	10.6%
Moderate	25	18.1%	658	11.5%	43	31.2%	1,540	27.0%
Middle	109	79.0%	4,894	85.8%	25	18.1%	985	17.3%
Upper	4	2.9%	154	2.7%	39	28.3%	2,285	40.0%
NA	0	0.0%	0	0.0%	2	1.4%	290	5.1%
<b>Total</b>	<b>138</b>	<b>100.0%</b>	<b>5,706</b>	<b>100.0%</b>	<b>138</b>	<b>100.0%</b>	<b>5,706</b>	<b>100.0%</b>
	Refinance							
	#	%	\$	%	#	%	\$	%
Low	0	0.0%	0	0.0%	11	18.3%	187	6.8%
Moderate	6	10.0%	278	10.1%	16	26.7%	584	21.1%
Middle	51	85.0%	2,259	81.7%	10	16.7%	384	13.9%
Upper	3	5.0%	227	8.2%	21	35.0%	1,472	53.3%
NA	0	0.0%	0	0.0%	2	3.3%	137	5.0%
<b>Total</b>	<b>60</b>	<b>100.0%</b>	<b>2,764</b>	<b>100.0%</b>	<b>60</b>	<b>100.0%</b>	<b>2,764</b>	<b>100.0%</b>
	Home Improvement							
	#	%	\$	%	#	%	\$	%
Low	0	0.0%	0	0.0%	76	44.7%	369	23.2%
Moderate	35	20.6%	127	8.0%	41	24.1%	351	22.1%
Middle	121	71.2%	1,203	75.7%	25	14.7%	366	23.0%
Upper	14	8.2%	260	16.4%	25	14.7%	479	30.1%
NA	0	0.0%	0	0.0%	3	1.8%	25	1.6%
<b>Total</b>	<b>170</b>	<b>100.0%</b>	<b>1,590</b>	<b>100.0%</b>	<b>170</b>	<b>100.0%</b>	<b>1,590</b>	<b>100.0%</b>
	Total HMDA*							
	#	%	\$	%	#	%	\$	%
Low	0	0.0%	0	0.0%	116	31.4%	1,162	10.9%
Moderate	66	17.9%	1,063	9.9%	100	27.1%	2,475	23.1%
Middle	282	76.4%	8,996	84.1%	60	16.3%	1,735	16.2%
Upper	21	5.7%	641	6.0%	85	23.0%	4,236	39.6%
NA	0	0.0%	0	0.0%	8	2.2%	1,092	10.2%
<b>Total</b>	<b>369</b>	<b>100.0%</b>	<b>10,700</b>	<b>100.0%</b>	<b>369</b>	<b>100.0%</b>	<b>10,700</b>	<b>100.0%</b>

\*Total includes one \$640 multifamily loan in a middle-income census tract.

### **Lending to Borrowers of Different Incomes and to Businesses of Different Sizes**

The distribution of lending based on income and revenue levels of the borrowers reflects an excellent penetration among individuals of different income levels and businesses of different sizes. The income level of the borrowers was compared to the HUD-adjusted median family income (MFI) for the Fort Worth-Arlington, Texas MSA. The following table depicts the income level ranges from 2001 through 2003:

<b>Income Level</b>	<b>2001 Fort Worth-Arlington MSA</b>	<b>2002 Fort Worth-Arlington MSA</b>	<b>2003 Fort Worth-Arlington MSA</b>
Median Income	\$60,100	\$61,300	\$60,300
Low-income	\$0 < \$30,050	\$0 < \$30,650	\$0 < \$30,150
Moderate-income	\$30,050 < \$48,080	\$30,650 < \$49,040	\$30,150 < \$48,240
Middle-income	\$48,080 < \$72,120	\$49,040 < \$73,560	\$48,240 < \$72,360
Upper-income	\$72,120 and up	\$73,560 and up	\$72,360 and up

As noted on the table on page 7, FSB originated 31% of its HMDA loans to low-income borrowers, and 27% to those with moderate-incomes. By comparison, low-income families comprise only 19% of total families and 21% of AA families are moderate-income. This performance demonstrates exceptional responsiveness to the credit needs of low-income individuals in its assessment area, especially in the home improvement loan category. Almost 45% of the bank's home improvement loans were extended to low-income borrowers, and 24% to moderate-income individuals.

The following two tables reflect the distribution of the small business loans in the assessment area by gross annual revenues and loan amount:

<b>DISTRIBUTION OF SMALL BUSINESS LOANS BY GROSS ANNUAL REVENUES</b>		
<b>Gross Annual Revenues</b>	<b>Number of Loans</b>	<b>Percent of Loans</b>
Less than \$100,000	14	29.2%
\$100,001 - \$250,000	8	16.7%
\$250,001 - \$500,000	10	20.8%
\$500,001 - \$1,000,000	9	18.7%
Over \$1,000,000	1	2.1%
Information Unavailable	6	12.5%
<b>TOTAL</b>	<b>48</b>	<b>100.0%</b>

Under the Community Reinvestment Act, a small business is defined as one that generates gross annual revenues of less than \$1 million. FSB Keene is more than satisfactorily meeting the credit needs of the community's small businesses. According to Dun & Bradstreet, 88% of the 815 businesses in the AA reported annual revenues of \$1 million or less. Approximately 98% of FSB

Keene’s small business loans sampled were made to businesses with gross annual revenues under \$1 million. Also, approximately 46% of the sampled loans were to businesses with gross annual revenue of less than \$500 thousand. Further, 29% were for amounts under \$100 thousand. Contacts often indicate that the local financial institutions are more than willing to help meet the credit needs of small businesses in the community. This demonstrates the bank’s commitment to small business.

**Geographic Distribution of Loans**

The bank’s geographic distribution of loans reflects a reasonable dispersion throughout the assessment area and demonstrates FSB’s willingness to meet the credit needs of the community. A review of the distribution of the bank’s HMDA and commercial loans in its AA among low-, moderate-, middle-, and upper-income geographies was performed. The bank’s lending distribution was compared to performance context factors including the distribution of the AA population, families, housing units, and businesses by geographic income level. These factors are summarized in the chart below.

<b>JOHNSON COUNTY PERFORMANCE CONTEXT</b>				
<b>Geographic Income Level</b>	<b>Percent of Total</b>			
	<b>Population</b>	<b>Families</b>	<b>Owner-Occupied Housing Units</b>	<b>Businesses</b>
Moderate-Income	20.5%	19.0%	17.3%	51.9%
Middle-Income	75.2%	76.2%	77.6%	48.1%
Upper-Income	4.3%	4.8%	5.2%	0.0%
Total (2000)	126,811	34,633	34,420	815

The geographic distribution of FSB’s HMDA loans closely approximates the distribution of families and owner-occupied housing units throughout the AA. As noted in the table on page 7, 18% of the bank’s HMDA loans were made in moderate-income tracts, while 76% went to middle-income tracts, and 6% to upper-income census tracts. The bank’s HMDA loans were well-dispersed throughout the area.

The following chart details the geographic distribution of the sampled small business loans.

<b>DISTRIBUTION OF SMALL BUSINESS LENDING BY GEOGRAPHIC INCOME LEVEL</b>				
	<b>Moderate</b>	<b>Middle</b>	<b>Upper</b>	<b>Total</b>
Number of Loans	8	39	1	48
% of Number	16.7%	81.3%	2.0%	100%
Dollar Volume	109,649	756,465	17,545	883,659
% of Dollar Volume	12.4%	85.6%	2.0%	100%
Businesses	51.9%	48.1%	0.0%	815

The geographic distribution of small business loans sampled reflects a reasonable dispersion throughout the AA. The percentage of loans made in the middle-income census tracts appears high when compared to the 48 percent of AA businesses that reside in those middle-income tracts. However, Johnson County is comprised primarily of rural, middle-income tracts and FSB Keene only operates one branch within a moderate-income tract. Additionally, growth and expansion from the Fort Worth MSA is moving south along the I-35 corridor which is comprised primarily of middle-income tracts in which the institution operates a branch.

### **Response to Complaints**

The bank has not received any CRA-related complaints since the previous evaluation.

### **Compliance With Anti-Discrimination Laws (ECOA, FHA OR HMDA)**

No violations of the substantive provisions of the anti-discrimination laws and regulations were identified during the concurrent Consumer Affairs Examination.

## GLOSSARY

**Census tract:** A small, relatively permanent statistical subdivision of a county or statistically equivalent entity, delineated for data presentation purposes by a local group of census data users or the geographic staff of a regional census center in accordance with U.S. Census Bureau guidelines. Designed to be relatively homogeneous units with respect to population characteristics, economic status, and living conditions **at the time they are established**, census tracts generally contain between 1,000 and 8,000 people, with an optimum size of 4,000 people. Census tract boundaries are delineated with the intention of being stable over many decades, so they generally follow relatively permanent visible features. However, they may follow governmental unit boundaries and other invisible features in some instances; the boundary of a state or county (or statistically equivalent entity) is always a census tract boundary.

**Consumer loan(s):** A loan(s) 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: motor vehicle loans, credit card loans, home equity loans, other secured consumer loans, and other unsecured consumer loans.

**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).

**Geography:** A census tract delineated by the United States 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 applicants, the amount of loan requested, and the disposition of the application (e.g., approved, denied, and withdrawn).

**Home mortgage loans:** Includes 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 refinancing 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 a geography.

**Metropolitan Statistical Area (MSA):** A core area, as defined by the United States Office of Management and Budget, with at least one urbanized area of 50,000 or more population, plus adjacent territory that has a high degree of social and economic integration with the core as measured by commuting ties. MSAs are defined in terms of whole counties.

**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 a 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 a geography

**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.

**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 a geography.