



# INTERMEDIATE SMALL BANK

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Comptroller of the Currency  
Administrator of National Banks

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Washington, DC 20219

## PUBLIC DISCLOSURE

November 9, 2009

### COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

The First National Bank of Bemidji  
Charter Number: 5582

1600 Paul Bunyan Drive NW  
Bemidji, Minnesota 56619

Office of the Comptroller of the Currency  
Minneapolis Field Office  
222 South 9<sup>th</sup> Street, Suite 800  
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**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.

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

**The Lending Test is rated: Outstanding.**

**The Community Development Test is rated: Outstanding.**

The major factors that support these ratings include:

- Home and consumer lending penetration to borrowers with low and moderate incomes is excellent, and exceeds the demographics.
- Commercial lending penetration to small businesses is excellent, and exceeds the demographics.
- Home, business and consumer lending within the assessment area (AA) is strong, with a substantial majority of originations inside the AA.
- Responsiveness to community development needs is excellent.
- Performance in other rating elements is satisfactory.

## **Scope of Examination**

The First National Bank of Bemidji's (FNB) CRA examination is based upon a review of the bank's primary loan products. Primary loan products include home mortgage loans, commercial loans, and consumer loans, consistent with the bank's business strategy. The evaluation period included originations in 2007, 2008, and January through October 2009. The evaluation period for community development loans, qualified investments, and community development services was the same.

The lending test consisted of a random sample of 30 home, 30 commercial, and 30 consumer loans. From these loans we determined the bank's performance with regards to lending within the AA and we then excluded loans outside of the AA for our assessment of FNB's performance regarding geographic distribution and lending to borrowers of different income/revenue levels. We also selected an additional sample of 30 commercial loans, to expand our assessment of the geographic distribution of this loan type.

The following table details the breakdown of loan origination amounts over the evaluation period by loan type and highlights FNB's primary loan products.

<b>FNB Loan Originations in 2007, 2008, and 2009</b>		
<i>Loan Type</i>	<i>% of Volume by \$</i>	<i>% of Volume by #</i>
Home Mortgage Loans	39%	22%
Commercial Loans	35%	15%
Consumer Loans	24%	61%
Agricultural Loans	2%	2%

*Source: Data sort of FNB's November 6, 2009 Loan Trial Balance*

Primary community credit needs, as identified through a variety of sources, include loans for housing, small businesses, job creation, and retail lending throughout the bank's AA. To help establish the performance context for FNB, we met with a local government representative and reviewed internal reports of three other local contacts made by examiners throughout the evaluation period. Local perspectives were also gained via reviews of the AA's county, city, and Tribal governments' websites, Department of Labor unemployment data, and information provided by the Indian Affairs Council.

## **Description of Institution**

FNB is a \$514 million institution located in Bemidji, Minnesota. The bank is wholly owned by First Bemidji Holding Company (FBHC), a one-bank holding company also located in Bemidji, Minnesota. FBHC's assets consist primarily of FNB. The bank does not have any operating subsidiaries and affiliate activities do not affect this evaluation. The bank is located in a non-metropolitan statistical area in northern Minnesota, between Grand Forks, North Dakota and Duluth, Minnesota. A portion of the bank's AA includes areas of the Red Lake and Leech Lake Indian Reservations.

FNB has three office locations, all in Bemidji, Minnesota. The main office and one branch are located in the same middle-income census tract (CT) and the additional branch in another moderate-income CT. FNB relocated and consolidated its former main office and one branch location into its new main office in February 2008. The former main office and consolidated branch were then closed. FNB also operates ten automated teller machines (ATMs) in Bemidji. Six of these ATMs are limited to cash dispensing services only.

FNB is a full-service bank offering a variety of loan and deposit products and services. The bank's loan mix, as a percent of average gross loans and leases, is comprised of 47% commercial, 41% home mortgage, and 12% consumer loans, as reported in the September 30, 2009 Call Report. This Report also detailed that net loans represented 55% of total assets.

FNB's CRA performance was rated "Outstanding" during the last CRA examination dated January 8, 2007. There are no legal, financial, or other factors impeding FNB's ability to help meet the credit needs of the community. However, as described in the next section, the unique status of the Red Lake Indian Reservation poses substantial challenges to mortgage lending on reservation lands.

## Description of Assessment Area

FNB's sole assessment area (AA) consists of eleven adjacent CTs. The AA includes all of Beltrami County, the northwestern portion of Cass County, and the northernmost section of Hubbard County, all in Minnesota. One CT is designated as low-income, four are moderate-income, and the remaining six are middle-income. The AA does not include any upper-income CT. The AA's population was reported at 46,650 persons in the 2000 U.S Census data. The largest city in the AA, Bemidji, recently reported a population of just over 13,000. Other cities in the AA include Cass Lake, Red Lake, and Blackduck. These cities are surrounded by woodlands, lakes, rural homesteads, lake homes, and Indian reservation lands. The AA complies with the CRA regulation and does not arbitrarily exclude any low- or moderate-income CTs.

The low-income CT consists primarily of that part of the Red Lake Indian Reservation immediately surrounding the Upper and Lower Red Lakes in Beltrami County. Tribal government has full sovereignty over the reservation, subject only to the Federal government, and the Tribe has the right to limit who can visit, operate businesses or live on the reservation. All land within the reservation is owned by the Tribe and financial institutions are unable to obtain mortgages on this land. The reservation is referred to as a "closed" reservation, due to this unique status, and is only one of two such reservations within the United States. Currently, the reservation's unemployment rate is very high at 60% as reported by a member of the Tribal Council. This rate is far above the 7.5% average of the tri-county area, 7.3% statewide, and 10.2% for the nation, as reported by the Department of Labor on September 30, 2009. In addition, two of the moderate-income tracts include a portion of the Leech Lake Indian Reservation in Beltrami and Cass Counties. This reservation is referred to as an "open" reservation. This Tribe continues to work with the Bureau of Indian Affairs to operate programs under self-governance procedures and delineate its sovereignty. Based upon the 2000 Census data, these two CTs reported a 31% unemployment rate.

The AA economy is not robust and has pockets of high unemployment, as described above. The economic conditions of the AA have experienced a decline during the evaluation period, but less so than reported from the larger state and national economies. Major employers include area public school systems, Beltrami County and other city municipalities, the Red Lake Band of Chippewa and related entities, the Leech Lake Band of Chippewa and related entities, Bemidji State University, and North County Health Services. The AA's updated median family income is \$58,500 and the updated median housing value is \$72,956. The poverty level of the AA was reported at 17% of households in the 2000 Census data, compared to the national average of 12%.

FNB experiences strong competition from other financial institutions in and around the AA. As reported in the Federal Deposit Insurance Corporation's June 30, 2009 Deposit Market Share Report, competition includes 16 federal or state chartered banks and 2 savings associations in Beltrami, Cass and Hubbard counties. These institutions range in size from very small community banks to large banks with offices nationwide. FNB ranks first of all these banks in terms of local deposit market share with 26%; the next closest competitor reported a market share of 15%. Other local competitors include several credit unions, mortgage companies, and investment companies.

## Conclusions with Respect to Performance Tests

### LENDING TEST

FNB's performance under the lending test is excellent. The bank exceeds the demographics in lending to borrowers of low and moderate incomes and to small businesses. FNB's loan origination percentage within the AA is strong. The bank's geographic distribution of loan originations is adequate and its loan-to-deposit ratio reasonable.

#### Loan-to-Deposit Ratio

FNB's loan-to-deposit (LTD) ratio is reasonable. At 74%, the bank's average LTD ratio over the last eleven quarters reflects an adequate lending volume. This level is not out of line with several other similarly situated banks. FNB's LTD ratio also reflects an increase in lending volume from the 65% reported in its last Public Evaluation, dated January 8, 2007. We compared FNB's LTD ratio to six other financial institutions within Beltrami, Cass and Hubbard counties. As of September 30, 2009, these banks ranged in asset size of \$274 million down to \$84 million. FNB reported total assets of \$514 million. The banks reported average loan-to-deposit ratios ranging from 77% to 98%, as detailed below.

<b>Loan-to-Deposit Ratios</b>		
Average of Quarterly LTDs March 31, 2007 – September 30, 2009		
<b>Bank Name</b>	<b>Average LTD</b>	<b>Asset Size (000) 9/30/09</b>
Security State Bank USA	98%	\$ 99,415
Citizens National Bank of Park Rapids	92%	\$191,021
Woodland Bank	86%	\$103,381
The First National Bank of Walker	85%	\$274,217
State Bank of Park Rapids	79%	\$104,523
Pine River State Bank	77%	\$ 84,137
The First National Bank of Bemidji	74%	\$514,009

*Source: Call Report data, March 31, 2007 through September 30, 2009.*

## Lending in Assessment Area

FNB's lending within the AA is strong. By number or dollar comparisons, our loan sample detailed that FNB originated a substantial majority of its loans within the AA. In total, 81% of loan originations came from within the AA, by number, and 82%, by dollar. As listed in the table below, 90% of the home loan originations were within the AA, followed by commercial loans at 80% and consumer loans at 73%.

Lending in the Assessment Area								
	Number of Loan Originations				Dollars of Loan Originations			
	Inside		Outside		Inside		Outside	
	#	%	#	%	\$(000)	%	\$(000)	%
Home Loans	27	90%	3	10%	1,418	87%	205	13%
Commercial Loans	24	80%	6	20%	1,622	81%	392	19%
Consumer Loans	22	73%	8	27%	153	60%	104	40%
<b>Totals</b>	<b>73</b>	<b>81%</b>	<b>17</b>	<b>19%</b>	<b>3,194</b>	<b>82%</b>	<b>701</b>	<b>18%</b>

Source: Examiner loan sample and 2000 U.S. Census data.

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

FNB's home lending distribution to borrowers of different incomes is excellent. The bank exceeds the demographics in lending to borrowers of low and moderate incomes. The table below details the findings of our loan sample regarding this loan type.

Borrower Distribution of Home Loans								
Borrower Income Level	Low		Moderate		Middle		Upper	
	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans
	26%	26%	19%	26%	23%	11%	32%	37%

Source: Examiner loan sample and 2000 U.S. Census data.

FNB's commercial lending distribution to borrowers of different revenue levels is excellent. The bank exceeds the demographics in lending to small businesses. The table below details the findings of our loan sample regarding this loan type.

Borrower Distribution of Loans to Businesses/Farms				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/Unknown	Total
% of AA Businesses	77%	4%	19%	100%
% of Bank Loans in AA by #	88%	12%	0%	100%
% of Bank Loans in AA by \$	88%	12%	0%	100%

Source: Examiner loan sample; Dunn and Bradstreet data.

FNB’s consumer lending distribution to borrowers of different incomes is excellent. The bank far exceeds the demographics in lending to borrowers of low and moderate incomes. The table below details the findings of our loan sample regarding this loan type.

<b>Borrower Distribution of Consumer Loans</b>								
Borrower Income Level	Low		Moderate		Middle		Upper	
	% of AA Households	% of Number of Loans	% of AA Households	% of Number of Loans	% of AA Households	% of Number of Loans	% of AA Households	% of Number of Loans
	27%	32%	18%	40%	20%	14%	35%	14%

Source: Examiner loan sample and 2000 U.S. Census data.

### Geographic Distribution of Loans

FNB’s geographic distribution of loan originations is adequate and reasonable. The bank’s geographic distribution performance for home and commercial loans is adequate. The geographic distribution for consumer loans is excellent. Sampled loans verified that FNB originated loans in all CTs of the AA and we did not identify any unexplained or conspicuous gaps in lending.

Our analysis for home loan geographic distribution focused upon FNB’s penetration into the four moderate-income tracts of the AA. We concluded that an analysis of home lending into the low-income CT was not meaningful, as home loans are mortgage dependent. The low-income CT is located on the Red Lake Indian Reservation which, as discussed earlier, is a closed reservation and the bank is unable to obtain mortgages on real property within this CT. This also limits the bank’s capacity for commercial real estate lending within this CT.

FNB’s geographic distribution of home loans is adequate. Our sample of home loans detailed that the volume of lending to moderate-income CTs is somewhat lower than the demographics, as detailed in the table below.

<b>Geographic Distribution of Home Loans</b>								
Census Tract Income Level	Low		Moderate		Middle		Upper	
	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans
	7%	0%	22%	15%	71%	85%	0%	0%

Source: Examiner loan sample and 2000 U.S. Census data.

FNB’s geographic distribution of loans to businesses is adequate. The sample of commercial loans detailed that lending to the low-income CT is equal to the demographics while lending in the moderate-income CTs is lower than the demographics.

The findings of our sample of loans to business originated within the AA are highlighted in the table below.

<b>Geographic Distribution of Loans to Businesses</b>								
Census Tract Income Level	Low		Moderate		Middle		Upper	
	% of AA Businesses /Farms	% of Number of Loans	% of AA Businesses/ Farms	% of Number of Loans	% of AA Businesses /Farms	% of Number of Loans	% of AA Businesses /Farms	% of Number of Loans
	4%	4%	27%	16%	69%	80%	0%	0%

Source: Examiner loan sample and 2000 U.S. Census data.

FNB’s geographic distribution of consumer loans is excellent. The sample of consumer loans detailed that FNB far exceeds the demographics in lending to the low-income geography and was very near to the demographics in lending to moderate-income geographies. FNB’s consumer loan geographic distribution performance is highlighted in the table below.

<b>Geographic Distribution of Consumer Loans</b>								
Census Tract Income Level	Low		Moderate		Middle		Upper	
	% of AA Households	% of Number of Loans	% of AA Households	% of Number of Loans	% of AA Households	% of Number of Loans	% of AA Households	% of Number of Loans
	8%	18%	25%	23%	67%	59%	0%	0%

Source: Examiner loan sample and 2000 U.S. Census data.

**Responses to Complaints**

There were no CRA complaints during the evaluation period.

**COMMUNITY DEVELOPMENT TEST**

Performance under the Community Development Test is rated “Outstanding”. FNB’s responsiveness to community development (CD) needs is excellent. Related efforts include originating CD loans, providing CD services, and making qualified investments. As noted earlier, our assessment of FNB’s CD activities included all of 2007, 2008 and January through October 2009.



## Number and Amount of Community Development Loans

FNB's performance in extending CD loans is excellent. The bank originated 25 qualifying loans and another 12 qualifying letters of credit within its AA during the evaluation period. Qualifying loan originations totaled \$8.8 million and the letters of credit totaled another \$46 thousand. This level of activity represents a significant commitment of the bank's capital. A few examples of qualifying loans and letters of credit are detailed immediately hereafter.

- A loan to help cover the ongoing operating needs of a local Chippewa Tribe.
- A loan to a non-profit to purchase lots to build affordable housing.
- Two loans to a non-profit to acquire land and a warehouse to run its operations and better meet its mission of providing affordable housing.
- Various loans to entities providing training and other community services to individuals with low and moderate incomes.
- Several loans to Tribal business entities that promote economic development in the AA's low-income CT.
- Numerous letters of credit to revitalize and support the economy of the AA's low-income CT.

## Number and Amount of Qualified Investments

The bank's level of qualified CD investments demonstrates excellent responsiveness to the needs of the AA and designated distressed or underserved nonmetropolitan middle-income geographies in Minnesota. Due to the lack of other opportunities, investments within the AA are limited to donation and grant activity. Other qualifying investments benefit geographies in broader regional and statewide areas.

The table below summarizes FNB's CD investment activity during the evaluation period, as well as, the remaining balances of bonds purchased prior to this period.

Type	Number	Dollar Amount (000's)
Donations/Grants	54	\$ 84
Investment Purchases, Current Evaluation Period	15	\$3,600
Balance of Investments, Purchased Prior to the Current Period	19	\$4,385
Total	88	\$8,069

## **Extent to Which the Bank Provides Community Development Services**

FNB's level of CD services is excellent. These services provide training, information, referral, and collaboration efforts, along with key leadership, technical support, and financial expertise. Organizations benefiting from these efforts include those focused upon small business and economic development, affordable housing, and meeting the needs of persons with low and moderate incomes.

Compiled data for the evaluation period reports that 64 employees of FNB donated their time and efforts to 20 such local organizations. Specific examples of organizations benefiting from these efforts include The Joint Economic Development Commission, First National Foundation Board, Downtown Development Authority Board, Bemidji Downtown Revitalization Committee, Habitat for Humanity, Bemidji Area Race Relations Council, Chamber of Commerce, Small Business Development Center Advisory Board, Northwest Technical College Foundation Board, and the Bemidji Development Corporation Board. FNB staff also provides first-time home buyer seminars each year via its *Home Stretch* program and are key to an ongoing high school financial education curricula and school savings program.

FNB has three locations and ten ATMs. One of the ATMs is located in a moderate-income CT. These ATMs allow transactions for electronic benefit transfers (EBT) and the State of Minnesota's unemployment compensation.

## **Fair Lending or Other Illegal Credit Practices Review**

We found no evidence of discriminatory or other illegal credit practices inconsistent with helping to meet community credit needs.