



SMALL BANK

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

PUBLIC DISCLOSURE

July 7, 2008

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

First National Bank, Cortez
Charter Number 14833

140 West Main Street
Cortez, Colorado 81321

Office of the Comptroller of the Currency

ARIZONA & NEW MEXICO
9633 South 48th Street, Suite 265
Phoenix, Arizona 85044

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 Satisfactory.

First National Bank, Cortez's (FNBC) lending performance reflects a satisfactory response to community credit needs. This is based on the following factors.

- The bank's loan to deposit (LTD) ratio has increased since the new bank management team took over mid-2007.
- A substantial majority of the loans were made inside the bank's assessment area (AA).
- Lending activities represent an excellent penetration of borrowers with different incomes and businesses of different sizes.
- Geographic distribution represents a reasonable dispersion throughout CTs of different income levels in the bank's AA.

SCOPE OF EXAMINATION

The examination of FNBC consisted of a full-scope review of the bank's single AA. The lending test covered January 2006 through May 2008, referred to in this report as the evaluation period. We identified commercial and residential real estate loans as the bank's primary products based on the number and dollar amount of loans originated in the evaluation period. There were no affiliate loans to review.

Loan Originations for Evaluation Period	% of Dollar Amount of Loans	% of Number of Loans
Commercial Loan Originations as a % of Total Originations	51%	20%
Residential RE Loan Originations as a % of Total Originations	39%	19%

Source: Loan originations for the evaluation period.

We sampled 20 loans from each of the bank's primary loan products. The data from the original commercial and residential real estate loan samples was used to calculate the inside/outside AA ratio. To perform other lending tests, we eliminated loans outside the AA from the original sample and added enough additional loans to provide a sample of 20 commercial and 20 residential real estate loans inside the AA. The sample is representative of the bank's business strategy since the last examination.

DESCRIPTION OF INSTITUTION

FNBC is a community bank headquartered in Cortez, Colorado, which is a non-metropolitan area in the southwestern part of the state. As of March 31, 2008, FNBC had \$73.6 million in assets, total loans of \$26.1 million, and total deposits of \$59.7 million. FNBC operates a main office in Cortez and one branch located in Mancos, Colorado, in addition to owning and operating two full-service ATMs. However, subsequent to the evaluation period, the bank closed the Mancos branch and ATM as of July 11, 2008. The bank is publicly owned with no affiliates. The bank offers a wide range of deposit and loan services to individuals and small businesses. The bank's primary lending focus is commercial loans to small businesses and residential real estate.

During the first half of 2007, FNBC experienced substantial turnover in senior management and the board. A majority of the bank's senior management and three of the bank's five board members were replaced. These changes have been positive for the bank and the new board is actively involved and supportive of management. Together they have developed a written strategic plan to focus on the future needs of the bank. The most important item identified was the need to restructure the balance sheet. The prior board and management team did not actively seek loan growth and were content with increasing the investment portfolio. As a result, the bank has a very low LTD ratio compared to its peers. During the past year, the new management team has made a concerted effort to increase loans originated and the LTD ratio trend reflects their efforts.

The bank was rated Satisfactory at the June 30, 2003 CRA examination. There are no financial or legal impediments that hinder the bank's ability to help meet the credit needs of the AA.

Additional details about the bank may be found in its Public File, maintained at the main office of the bank.

DESCRIPTION OF ASSESSMENT AREA

FNBC has designated one CT for Dolores County and seven CTs in Montezuma County as its AA, which includes the city of Cortez and towns of Mancos, Dolores, Dove Creek, and Rico. The entire area is a non-metropolitan statistical area. Dolores County has also been designated as an underserved middle-income non-metropolitan tract since June 1, 2005. The underserved designation relates to population size, density, and dispersion, and applies to remote rural areas.

FNBC's AA has one low-, one moderate-, six middle-, and no upper-income CTs. The low-income CT is made up of the Ute Mountain Ute Indian Reservation. The moderate-income CT incorporates a portion of the business and retail area of Cortez. The AA meets the legal requirements of the regulation and does not arbitrarily exclude low- or moderate-income (LMI) geographies.

The economy of the AA is equally divided between tourism, the provision of government services, and agriculture. Primary employers are lodging and food service industries, federal/county/city/tribal governments, and wholesale/retail trade. The AA encompasses a diversified employment base and over the past three years unemployment has fallen from six

percent to four percent. Local economic conditions are stable and have not been adversely affected by recent adverse commercial real estate and mortgage market trends.

Demographic Information for the FNBC AA					
	#	% Low	% Moderate	% Middle	% Upper
Geographies (Census Tracts)	8	13	13	74	N/A
Population by Geography	25,674	1,513	3,566	20,595	N/A
Owner-Occupied Housing by Geography	7,477	4	10	86	N/A
Businesses by Geography	2,858	2	12	86	N/A
Farms by Geography	150	1	6	93	N/A
Family Distribution by Income Level	7,084	25	23	23	29
Household Distribution by Income Level	9,995	28	21	21	30
Census Median Family Income (MFI)		\$44,319	Median Housing Value		\$104,892
Housing and Urban Development (HUD) - Adjusted MFI: 2007		\$52,400	Families Below the Poverty Level		16%
HUD - Adjusted MFI: 2006		\$51,500	Unemployment Rate		3%
HUD - Adjusted MFI: 2005		\$51,900			

Source: 2000 U.S. Census Data

Competition for financial services is strong. The June 30, 2007 FDIC Deposit Market Share Report shows seven financial institutions, with a total of 12 branches, competed for over \$417 million of insured deposits. The nature of the competition includes three state-wide financial institutions comprising over 37 percent of the deposit market share and three local financial institutions comprising over 49 percent of the deposit market share. Since the FDIC report date, one out-of-state bank has opened up a new branch in the AA, adding to the direct competition. FNBC is the third smallest with a 14 percent share in the marketplace and does not operate outside the area. The three state-wide financial institutions have a significant presence and access to other loans and deposits outside the local market.

There are three similarly situated banks to FNBC in the marketplace. The similarities are identified in terms of size, geographic presence, and line of business. Two are larger local banks with two branches and operate only inside the AA. One of these banks was recently acquired by one of the state-wide financial institutions described above and has broadened their deposit and lending base as a result. Another bank is approximately the same size as FNBC but has only a main office with no branches and operates only inside the AA. These institutions were used to evaluate the bank's LTD ratio.

During our evaluation of FNBC, we contacted a local community organization to help determine the credit and financial needs and opportunities in the AA. The contact reported economic conditions in the area were stable and local financial institutions are supportive in meeting identified credit needs. The contact identified the primary credit need as financing for individual rural lot construction; including road, sewer and water, and residential construction. Community service needs include small business grant writing and business plan creation assistance. The contact stated that the major long-term issue facing the area is the retention of a qualified workforce and the need to create sustainable companies and jobs.

Maps and additional information about the bank’s AA may be found in the bank’s Public File, maintained at the main office of the bank.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Loan-to-Deposit Ratio

FNBC’s average LTD ratio is less than reasonable given the bank’s size, financial condition, and credit needs of the AA. As of March 31, 2008, the bank’s quarterly average LTD ratio for the last 21 quarters was 34 percent, with a low of 27 percent and a high of 44 percent.

The bank’s net LTD ratio compares unfavorably, ranking last among the three other similarly situated banks located in FNBC’s AA. The results are summarized below.

Bank	Average Quarterly Loan-to-Deposit Ratio (3/2003 - 3/2008)
First National Bank, Cortez	34%
Bank A	62%
Bank B	63%
Bank C	74%

Source: Uniform Bank Performance Report.

FNBC’s low LTD can be directly attributed to the prior board and management team who did not actively seek to meet the credit needs of the AA and reinvested community deposits into the bank’s investment portfolio instead. However, the new management team has made a concerted effort to increase loans originated and the current LTD ratio reflects their efforts.

Bank	Average Quarterly Loan-to-Deposit Ratio (6/2007 - 3/2008)
First National Bank, Cortez	42%
Bank A	62%
Bank B	69%
Bank C	83%

Source: Uniform Bank Performance Report.

Lending in Assessment Area

We calculated the percentage of both number and dollar amount of our original sample of 20 commercial and 20 residential real estate loans made inside the bank’s AA. With a combined 85 percent of the number and 84 percent of dollars of loans, FNBC’s inside/outside ratio reflects a substantial majority of the primary loan products originated are within its AA. The bank has also made commercial and residential real estate loans in Dolores County, designated as an underserved middle-income non-metropolitan tract. This exceeds the standard for satisfactory performance.

Lending in Dolores County and Montezuma County, Colorado										
Loan Type	Number of Loans					Dollars of Loans (000s)				
	Inside		Outside		Total	Inside		Outside		Total
	#	%	#	%		\$	%	\$	%	
Commercial	17	85	3	15	20	1,742	88	235	12	1,977
Residential RE	17	85	3	15	20	1,937	80	476	20	2,413
Totals	34	85	6	15	40	3,678	84	712	16	4,390

Source: Loan originations for the evaluation period.

We replaced three loans each for commercial and residential real estate loans made outside the bank’s AA to arrive at a new sample of 20 loans for both primary loan products. With these new samples, we analyzed the following tests for Borrower and Geographic Distribution.

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

The borrower distribution of commercial and residential real estate loans originated in the AA reflects excellent penetration among individuals and businesses. We relied more heavily on the borrower distribution of business loans as these loans represent the majority of the bank’s loan portfolio.

Commercial Loans

FNBC exceeds the standard for loans to businesses with revenues of \$1 million or less. The table below shows the bank has excellent penetration of its AA compared to the demographic of only 59 percent of area businesses with revenues of \$1 million or less.

Borrower Distribution of Loans to Businesses in Dolores County and Montezuma County, Colorado				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/ Unknown	% Total
% of AA Businesses	59	4	37	100
% of Bank Loans in AA by #	70	15	15	100
% of Bank Loans in AA by \$	88	8	4	100

Source: Loan sample; Dunn & Bradstreet data.

Residential Real Estate Loans

The distribution of residential real estate loans to LMI borrowers reflects reasonable penetration among borrowers of different income levels. The number of loans for low-income borrowers is significantly lower than the ratio and does not meet the standard. However, this is due to 16 percent of families in the AA living below the poverty level. As a result, it is harder for these families to qualify for residential real estate loans especially when the Median Housing Value is \$104,892 for the AA. Performance for loans to moderate-income borrowers meets the standard. Considering the limited opportunity for the bank to lend to low-income borrowers, the bank’s distribution is reasonable.

Borrower Distribution of Residential Real Estate Loans in Dolores County and Montezuma County, Colorado
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Borrower Income Level	Low		Moderate		Middle		Upper	
Loan Type	% 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
Residential RE	25	5	23	15	23	35	29	45

Source: Loan sample and U.S. Census data.

Geographic Distribution of Loans

The geographic distribution of FNBC’s commercial and residential real estate loans within the AA is reflects reasonable dispersion.

Commercial Loans

When combined, the geographic distribution of commercial loans to businesses in the AA is reasonable. The table and explanations below support this conclusion.

FNBC has not originated any commercial loans in the low-income CT of the AA and does not meet the standard, reflecting poor dispersion. However, businesses in the low-income CT represent only two percent of all businesses located in the AA. As discussed in the *Description of Assessment Area* section of this evaluation, the low-income CT incorporates the Ute Mountain Ute Indian Reservation. Lending opportunities are limited as this area is sparsely populated with both people and commerce. According to management, difficulties associated with placing liens on collateral located on Indian Reservation land further limits the bank’s lending opportunities.

The distribution of loans to the moderate-income CT reflects reasonable dispersion. The sample of commercial loans originated in the middle-income CTs also includes five percent made to businesses in Dolores County, designated as an underserved middle-income non-metropolitan tract.

Geographic Distribution of Loans to Businesses in Montezuma County and Dolores County, Colorado								
Census Tract Income Level	Low		Moderate		Middle		Upper	
Loan Type	% of AA Businesses	% of Number of Loans	% of AA Businesses	% of Number of Loans	% of AA Businesses	% of Number of Loans	% of AA Businesses	% of Number of Loans
Commercial	2	0	12	5	86	95	N/A	N/A

Source: Loan sample and U.S. Census data.

Residential Real Estate Loans

Overall, the geographic distribution of residential real estate loans is reasonable. The table and explanations below support this conclusion.

FNBC has not originated any residential real estate loans in the low-income CT of the AA and does not meet the standard, reflecting poor dispersion. As discussed above, the low-income CT incorporates the Ute Mountain Ute Indian Reservation. Lending opportunities are limited as this

area is sparsely populated and only four percent of the available housing is owner occupied, which limits the number of homes eligible for residential mortgages. According to management, difficulties associated with taking real estate as collateral on Indian Reservation land further limits the bank’s lending opportunities.

The geographic distribution of loans to the moderate-income CT meets the demographic, and reflects excellent dispersion. The sample of residential real estate loans originated in the middle-income CTs also includes five percent made to individuals in Dolores County, designated as an underserved middle-income non-metropolitan tract.

Geographic Distribution of Residential Real Estate Loans in Montezuma County and Dolores County, Colorado								
Census Tract Income Level	Low		Moderate		Middle		Upper	
Loan type	% 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
Residential RE	4	0	10	10	86	90	N/A	N/A

Source: Loan sample and U.S. Census data.

Responses to Complaints

No complaints have been received by the bank or OCC relating to the bank’s CRA performance during this evaluation period.

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.