



SMALL BANK

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

PUBLIC DISCLOSURE

January 24, 2012

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

Kilgore National Bank
Charter Number 24051

410 North Kilgore Street
Kilgore, TX 75662-0000

Office of the Comptroller of the Currency

Longview Field Office
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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 Satisfactory.

Kilgore National Bank has a satisfactory record of meeting community credit needs. This rating is based on the following:

- The bank's loan to deposit ratio is reasonable based on the bank's performance context and lending opportunities.
- A majority of the bank's loans are extended to borrowers within the assessment area.
- The distribution of loans to borrowers of different incomes and businesses of different sizes is reasonable.
- The geographic distribution of loans reflects a reasonable dispersion throughout the bank's assessment area.

SCOPE OF EXAMINATION

This Performance Evaluation (PE) is an assessment of Kilgore National Bank's ability to meet the credit needs of the communities in which it operates. The bank was evaluated under the small bank performance criteria. Conclusions regarding the bank's lending performance are based on residential mortgages reported under the Home Mortgage Disclosure Act (HMDA) and business loans originated from January 1, 2009 to December 31, 2011. A sample of consumer loans originating in the Cherokee County assessment area was also reviewed.

DESCRIPTION OF INSTITUTION

Kilgore National Bank (KNB) is an \$84 million bank located in Kilgore, Texas. KNB serves parts of the adjacent counties of Gregg, Rusk, Smith and Cherokee through four banking locations. The bank is wholly owned by Kilgore National Financial Corporation and has no holding company affiliations. Products offered include traditional, non-complex residential loans, consumer loans and business loans. There are no financial or legal obstacles affecting the bank's ability to meet community credit needs. The bank was rated satisfactory during the prior Community Reinvestment Act (CRA) Examination dated September 4, 2007. The following chart reflects the distribution of the bank's loan portfolio:

Loan Category	\$ (000)	%
Residential Real Estate Loans	\$24,157	50.81%
Commercial Real Estate Loans	\$12,126	25.50%
Commercial Loans	\$6,734	14.16%
Consumer Loans	\$3,710	7.80%
Agricultural Loans	\$822	1.73%
Total	\$47,549	100.00%

DESCRIPTION OF ASSESSMENT AREAS

The Board has designated ten census tracts in Gregg and Rusk counties as the assessment area served by the Kilgore and Liberty City branch offices. The Board has also designated 28 census tracts in Smith County and seven census tracts in Cherokee County as the assessment areas for the Tyler and Troup branch locations. These assessment areas meet the requirements of the Community Reinvestment Act and do not arbitrarily exclude low and moderate-income geographies. Our review included an assessment of the bank's lending in all assessment areas.

Gregg/Rusk County Assessment Area

KNB's main office is located in Kilgore, Texas in Gregg County with an additional branch located in Liberty City. Census tracts in Gregg and Rusk Counties surrounding these locations are included in the bank's assessment areas and are a part of the Longview MSA. This area has no designated low income tracts, one moderate income tract, eight middle income tracts, and one upper income tract. Based on 2000 census data, the assessment area has a total population of 50,757 and the local economy is considered stable. Competition in the area is strong with branches of larger national and state banks operating within the bank's assessment area. The distribution of families by income level, regardless of census tract location, consists of the following: 18.58% are low income, 17.41% are moderate income, 22.86% are middle income, and 41.15% are upper income. Major employers in the area include Eastman Chemical Company, LeTourneau Technologies, Kilgore Independent School District, and General Dynamics. Contact with a local business organization revealed the primary community credit needs for the assessment area are residential mortgages. The contact also noted the lack of available affordable housing in the area. The following table reflects the demographics for the assessment area (AA):

DEMOGRAPHIC AND ECONOMIC CHARACTERISTICS OF THE GREGG/RUSK COUNTIES AA	
<i>Population</i>	
Number of Families	13,961
Number of Households	18,842
<i>Geographies</i>	
Number of Census Tracts/BNA	10
% Low-Income Census Tracts/BNA	0.00%
% Moderate-Income Census Tracts/BNA	10.00%
% Middle-Income Census Tracts/BNA	80.00%
% Upper-Income Census Tracts/BNA	10.00%
<i>Median Family Income (MFI)</i>	
2000 MFI for AA	\$42,782
2010 HUD-Adjusted MFI	\$54,500
<i>Economic Indicators</i>	
Unemployment Rate (Dec. 2011)	5.9%
2010 Median Housing Value	\$63,271
% of Households Below Poverty Level	13.89%

Source: 2000 Census Data

Smith County Assessment Area

The Board has designated 28 census tracts in Smith County as its assessment area for the branches located in Tyler and Troup, Texas. Two tracts are considered low income, six are moderate income, and eleven are middle income tracts with nine tracts considered upper income tracts. These tracts make up the lower portion of Smith County and are a part of the Tyler MSA. Competition is strong with several branches of larger national and state banks operating within the bank's assessment area. Based on 2000 census data, the distribution of families by income level, regardless of census tract location, consists of the following: 18.75% are low income, 16.76% are moderate income, 20.39% are middle income, and 44.10% are upper income. Major employers in the area include East Texas Medical Center, Trinity Mother Frances, Tyler Independent School District, and Brookshire Grocery Company. Contact with a local business organization in Tyler revealed the primary community credit need for the assessment area is residential mortgages. The contact also noted the need for affordable housing in the area. The following table reflects the demographics for the AA:

DEMOGRAPHIC AND ECONOMIC CHARACTERISTICS OF THE SMITH COUNTY AA	
<i>Population</i>	
Number of Families	35,733
Number of Households	50,736
<i>Geographies</i>	
Number of Census Tracts/BNA	28
% Low-Income Census Tracts/BNA	7.14%
% Moderate-Income Census Tracts/BNA	21.43%
% Middle-Income Census Tracts/BNA	39.29%
% Upper-Income Census Tracts/BNA	32.14%
<i>Median Family Income (MFI)</i>	
2000 MFI for AA	\$49,118
2010 HUD-Adjusted MFI	\$56,200
<i>Economic Indicators</i>	
Unemployment Rate (Dec. 2011)	7.3%
2010 Median Housing Value	\$86,592
% of Households Below Poverty Level	12.38%

Source: 2000 Census Data

Cherokee County Assessment Area

The bank has designated seven census tracts in Cherokee County as a part of the assessment area for the branches located in Tyler and Troup, Texas. There are no low or upper income tracts in the area with three tracts designated as moderate and four as middle. However, the middle income tracts have been designated as distressed by the FFIEC. We considered this information in our review of the Cherokee County assessment area. The tracts included in the bank’s assessment area consists of the upper portion of Cherokee County and are contiguous with the bank’s Smith County assessment area; however, they are not a part of the Tyler MSA and are considered a non-metropolitan area. Cherokee and Smith Counties divide the Troup community where the bank has a branch location. Although the Troup office is in located in Smith County with no banking offices in Cherokee County, this area is included as a separate assessment area due to the close proximity of the branch to the county line. The bank’s primary competition consists of branches of larger national and state banks, all of which operate within the bank’s assessment area. Based on 2000 census data, the distribution of families by income level, regardless of census tract location, consists of the following: 20.38% are low income, 20.02% are moderate income, 21.75% are middle income, and 37.85% are upper income. Major employers in the area include the Jacksonville Independent School District, Stream Global Services, Wal-Mart, and Cardinal Healthcare. Contact with a local business organization revealed the primary community credit need for the assessment area is residential mortgages. The following table reflects the demographics for the AA:

DEMOGRAPHIC AND ECONOMIC CHARACTERISTICS OF THE CHEROKEE COUNTY AA	
<i>Population</i>	
Number of Families	7,977
Number of Households	10,812
<i>Geographies</i>	
Number of Census Tracts/BNA	7
% Low-Income Census Tracts/BNA	0.00%
% Moderate-Income Census Tracts/BNA	42.86%
% Middle-Income Census Tracts/BNA	57.14%
% Upper-Income Census Tracts/BNA	0.00%
<i>Median Family Income (MFI)</i>	
2000 MFI for AA	\$35,064
2010 HUD-Adjusted MFI	\$46,500
<i>Economic Indicators</i>	
Unemployment Rate (Dec.2011)	8.1%
2010 Median Housing Value	\$53,881
% of Households Below Poverty Level	17.75%

Source: 2000 Census Data

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

KNB's performance under the lending test is satisfactory. KNB has demonstrated satisfactory performance in meeting the credit needs of the community. All performance criteria of the lending test are documented below:

Loan-to-Deposit Ratio

The loan-to-deposit ratio of KNB is reasonable given the bank's size, financial condition and assessment area credit needs. KNB's loan-to-deposit ratio is comparable to other banks headquartered within the bank's assessment area. The bank's quarterly loan-to-deposit ratio has averaged 61.60% since the prior CRA examination. The average quarterly loan-to-deposit ratio of banks within the assessment area, regardless of size, for the same time period is 64.10%.

Institution	Assets (000s) (as of 9/30/11)	Average LTD Ratio
Kilgore National Bank	83,649	61.60%
Citizens Bank, Kilgore	325,628	71.89%
Gladewater National Bank	32,046	67.24%
First State Bank, Overton	43,760	34.47%
American State Bank, Arp	207,830	66.79%
Citizens State Bank, Tyler	258,410	80.13%

Lending in Assessment Area

A majority of the KNB's lending activity was originated within the designated AAs. Our sample included all HMDA reportable residential real estate loans, 20 business loans and 20 consumer loans. By number of loans made, 82.19% of loans were made to borrowers inside the AA. By dollar volume, 73.81% of the loans made by the bank were to customers inside the AA. Please see the following chart for further information on lending in the assessment area by product type.

Table 1 - Lending in AA										
Loan Type	Number of Loans					Dollars of Loans				
	Inside		Outside		Total	Inside		Outside		Total
	#	%	#	%		\$	%	\$	%	
Home Purchase	92	78.63	25	21.37	117	10,221	75.07	3,395	24.93	13,616
Home Improvement	62	87.32	9	12.68	71	930	84.70	168	15.30	1,098
Refinance	51	79.69	13	20.31	64	5,660	71.40	2,267	28.60	7,927
Business Loans	16	80.00	4	20.00	20	1752	68.72	798	31.28	2,550
Consumer Loans	19	95.00	1	5.00	20	120	97.96	3	2.04	123
Total Loans	240	82.19	52	17.81	292	18683	73.81	6631	26.19	25,314

Source: Data reported under HMDA, loan sample.

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

The overall distribution of loans to borrowers of different incomes and businesses of different sizes is reasonable throughout all assessment areas.

Gregg/Rusk County Assessment Area

The distribution of loans within the AA represents a reasonable penetration among borrowers of different income levels and businesses of different sizes. The 2000 US Census information reflects that the median cost of housing is \$63 thousand whereas a low income person earns less than \$27 thousand a year based on the HUD updated 2010 median family income information. Demographic data indicates that 18.26% of the population qualifies as low income; additionally

almost 14% of the population lives below the poverty line. Further, 26% of the housing market is comprised of rental units and 91% of the housing available is occupied. This further reduces the availability of affordable housing to low income borrowers. We considered these mitigating factors in our lending analysis to low income borrowers.

Residential Real Estate Mortgages:

The distribution of residential real estate loans represents a reasonable penetration among borrowers of different income levels. While lending to low income borrowers is less than the percentage of low income borrowers in the AA, the distribution of loans to moderate income level borrowers exceeds that of the demographic data. The lower level of lending to low income borrowers is reflective of the factors discussed above. Please see the following chart for further information.

Table 2 - Borrower Distribution of Residential Real Estate Loans in Gregg & Rusk Co AA								
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
Home Purchase	18.58	2.56	17.41	23.08	22.86	20.51	41.15	48.72
Home Improvement	18.58	20.41	17.41	22.45	22.86	28.57	41.15	28.57
Refinance	18.58	5.00	17.41	20.00	22.86	15.00	41.15	50.00%

Source: Data reported under HMDA; U.S. Census data. Income NA for 5.13% of home purchase and 10.00% of refinancing loans.

Business Loans:

The distribution of business loans reflects reasonable penetration among businesses of different sizes. Sixty-five percent of the bank’s loans to businesses during the loan sampling period were made to small business customers. Please see the following chart for further information.

Table 2A - Borrower Distribution of Loans to Businesses in Gregg & Rusk Co AA				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/ Unknown	Total
% of AA Businesses	68.93	2.85	28.22	100%
% of Bank Loans in AA by #	65.00	30.00	5.00	100%
% of Bank Loans in AA by \$	47.83	46.19	5.98	100%

Source: Loan sample; Dun and Bradstreet data.

Smith County Assessment Area

The distribution of loans within the Smith County AA to borrowers of different income levels is reasonable. Per 2000 US Census information, the median cost of housing in the AA is \$87 thousand. HUD updated 2010 family median income information shows that low income borrowers earn less than \$28 thousand a year and moderate income borrowers earn less than \$45 thousand a year. Also, demographic data indicates that almost 13% of the population lives below the poverty line and that unemployment for December 2011 was 7.3%. Additionally 34% of the housing market is comprised of rental units with 92% of all housing occupied. These combined factors reduce the availability of affordable housing to low and moderate income borrowers. We considered these mitigating factors in our lending analysis to low and moderate income borrowers.

Residential Real Estate Mortgages:

The distribution of residential real estate loans represents a reasonable penetration among borrowers of different income levels. While lending overall is less than the demographic data in total, home purchase loans to low income borrowers is near the demographic data. Additionally, home improvement loans to moderate income borrowers exceed the demographic data. This overall low level of lending is reflective of the factors discussed above. Please see the following chart for further information.

Table 2 - Borrower Distribution of Residential Real Estate Loans in Smith Co AA								
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
Home Purchase	18.75	14.29	16.76	5.71	20.39	28.57	44.10	48.57
Home Improvement	18.75	0.00	16.76	20.00	20.39	20.00	44.10	60.00
Refinance	18.75	4.35	16.76	4.35	20.39	8.70	44.10	47.82

Source: Data reported under HMDA; U.S. Census data. Income NA for 2.86% of home purchase and 34.78% of refinancing loans.

Business Loans:

The distribution of business loans reflects excellent penetration among businesses of different sizes. Ninety percent of the bank’s loans to businesses during the loan sampling period were made to small business customers. Please see the following chart for further information.

Table 2A - Borrower Distribution of Loans to Businesses in Smith Co AA				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/ Unknown	Total
% of AA Businesses	68.89	2.53	28.58	100%
% of Bank Loans in AA by #	90.00	10.00	n/a	100%
% of Bank Loans in AA by \$	91.18	8.82	n/a	100%

Source: Loan sample; Dun and Bradstreet data.

Cherokee County Assessment Area

The Cherokee County AA is serviced primarily by the bank’s location in Troup, Texas. This location produces a very limited number of residential or commercial loans with the primary product type being consumer lending. Therefore, commercial and residential loans were not considered during our review of the Cherokee County AA.

Consumer Loans:

The distribution of consumer loans represents a reasonable penetration among borrowers of different income levels. While consumer lending to low income borrowers is less than the percentage of low income borrowers in the AA, the distribution of loans to moderate income borrowers exceeds the demographic data. The lower level of lending to low income borrowers is reflective of high unemployment and low income levels. Unemployment as of December 2011 totaled 8.1% and 2000 Census data shows that a low income borrower makes less than \$15.5 thousand annually. Additionally, the FFIEC has designated Cherokee County as distressed based on the high levels of poverty in the county. We considered these mitigating factors in our review of lending to low income borrowers. Please see the following chart for further information.

Table 2B - Borrower Distribution of Consumer Loans in Cherokee Co AA								
Borrower Income Level	Low		Moderate		Middle		Upper	
	% of AA Households	% of Number of Loans						
Consumer Loans	23.94	8.33	17.85	20.83	17.83	20.83	40.38	50.00

Source: Loan sample; U.S. Census data

Geographic Distribution of Loans

The overall geographic distribution of loans reflects a reasonable dispersion throughout the bank’s assessment areas.

Gregg/Rusk County Assessment Area

The geographic distribution of loans reflects a reasonable distribution throughout the AA. There are no low income census tracts in the AA and only one (1) moderate income census tract in the AA.

Residential Real Estate Loans:

The geographic distribution of residential real estate loans reflects reasonable dispersion throughout the AA for moderate income census tracts. Please see the following charts for further information.

Table 3 - Geographic Distribution of Residential Real Estate Loans in Gregg & Rusk Co AA								
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
Home Purchase	0.00	0.00	6.16	5.13	83.72	71.79	10.12	23.08
Home Improvement	0.00	0.00	6.16	16.33	83.72	75.51	10.12	8.16
Refinance	0.00	0.00	6.16	5.00	83.72	75.00	10.12	20.00

Source: Data reported under HMDA; U.S. Census data.

Business Loans:

The geographic distribution of business loans reflects excellent dispersion throughout the AA. Please see the following chart for further information.

Table 3A - Geographic Distribution of Loans to Businesses in Gregg & Rusk Co AA								
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
Businesses	0.00	0.00	17.33	30.00	72.71	45.00	9.96	25.00

Source: Loan sample; Dun and Bradstreet data.

Smith County Assessment Area

The geographic distribution of loans is poor throughout the AA. The Smith County AA contains 28 census tracts. There are two (2) low income census tracts and six (6) moderate census tracts in the AA. The bank’s branches in the AA are located in south Tyler and in Troup, TX. These locations are in the southeastern and southwestern portions of the AA, respectively. The branch

in south Tyler was opened on December 31, 2009 and has had only two years of operating presence in the Tyler market. The branch in Troup, TX is on the county line between Smith and Cherokee Counties and primarily serves Cherokee County.

All of the low and moderate income census tracts in the Smith County AA are located in the northern portion of the AA. Both of the low income tracts and five of the six moderate income tracts are north of Loop 323 in Tyler, TX. Loop 323 is a major thoroughfare in the AA circling the central part of Tyler, TX which includes the downtown areas. The Tyler branch is located approximately 7 miles south of these areas, while the Troup branch is almost 15 miles south of these areas. Large thoroughfares (including Loop 323) separate these areas and prevent easy access from the low or moderate income tracts to the branch locations nearer the outer limits of the assessment area.

As discussed in the description of the AA, the level of competition in the Smith County AA is intense from both large nationwide and regional banks, as well as larger local banks. The significant competition in the AA, the newness of the Tyler branch, and the geographical barriers to the low and moderate income tracts were considered mitigating factors in our review of the geographic distribution of loans in the Smith County AA.

Residential Real Estate Loans:

The geographic distribution of residential real estate loans reflects poor dispersion throughout the AA for borrowers located in both the low and moderate income census tracts. However, the dispersion of low and moderate income tracts within the AA is low. Low income tracts represent less than 3% of the AA and moderate income tracts represent 12% of the AA. The limited opportunities to lend in the low and moderate tracts were considered with the information presented above as mitigating factors during our review. Please see the following charts for further information.

Table 3 - Geographic Distribution of Residential Real Estate Loans in Smith Co AA								
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
Home Purchase	2.79	0.00	12.03	0.00	51.56	82.86	33.62	17.14
Home Improvement	2.79	0.00	12.03	0.00	51.56	80.00	33.62	20.00
Refinance	2.79	0.00	12.03	0.00	51.56	73.91	33.62	26.09

Source: Data reported under HMDA; U.S. Census data.

Business Loans:

The geographic distribution of business loans reflects poor dispersion throughout the AA. While there is a limited opportunity to lend to businesses in low income tracts, lending to moderate income tracts was less than the demographic data. The lower level of lending to the low and moderate income tracts is reflective of the factors discussed above. Please see the following chart for further information.

Table 3A - Geographic Distribution of Loans to Businesses in Smith Co AA								
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
Businesses	3.59	0.00	18.29	5.00	40.33	25.00	37.79	75.00

Source: Loan sample; Dun and Bradstreet data.

Cherokee County Assessment Area:

The geographical test was not performed for the loan sample in Cherokee County. The geographic analysis of loans in the Cherokee County AA would not be meaningful, as the region has been designated as distressed by the FFIEC. There are seven (7) census tracts included in the Cherokee County AA: four (4) middle income and three (3) moderate income tracts. The distressed designation eliminates the need to evaluate the distribution of geographies in the Cherokee County AA.

Responses to Complaints

There have been no complaints received regarding the Community Reinvestment Act since the prior examination.

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.