



PUBLIC DISCLOSURE

March 10, 2015

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

Preferred Bank
Charter Number 708069

11757 Katy Fwy Ste 100
Houston, TX 77079-1708

Office of the Comptroller of the Currency

1301 McKinney Street
Suite 1410
Houston, TX 77010-3031

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 COMMUNITY REINVESTMENT ACT RATING:
This institution is rated Satisfactory**

Preferred Bank has a “**Satisfactory**” record of meeting community credit needs in its assessment area (AA). The following factors support this rating:

- Preferred Bank has maintained a reasonable loan-to-deposit (LTD) ratio based on the average LTD of similarly situated banks.
- A majority of the bank’s lending was inside the AA by number and dollar amount.
- Distribution of residential mortgage loans reflects reasonable penetration of borrowers of different income levels and reasonable penetration to businesses with revenues less than \$1 million.
- The overall geographic distribution of loans reflects reasonable dispersion in low and moderate-income (LMI) census tracts in the bank’s AA.

SCOPE OF EXAMINATION

Preferred Bank (Preferred) was evaluated under the small bank examination procedures, which includes the lending test. The lending test evaluates the bank’s record of meeting the credit needs of its AAs through its lending activities. The evaluation period is from August 9, 2010 through March 10, 2015.

The bank’s primary lending products are business financing, consisting primarily of loans to small- and medium-size businesses; and residential mortgage loans consisting of 1-4 family residential loans. The lending test covers the period from January 1, 2013 through December 31, 2014 for business loans and 1-4 family residential owner-occupied loans originated by the bank.

For business loans, we used the entire small business loan portfolio in our analysis. For 2013 there were 83 business loans with a dollar amount of \$41.2 million and in 2014 there were 84 totaling \$33.2 million.

For residential mortgage loans, we used all of the originated home purchase loans reported on the Home Mortgage Disclosure Act (HMDA) Loan Application Register (LAR), which consisted of 48 loans in number and \$16.4 million by dollar amount. The number of originated home purchase residential mortgage loans totaled 21 for 2013 and 27 for 2014 and the dollar amounts totaled \$6.6 million and \$9.8 million, respectively.

As a “Small Bank” for Community Reinvestment Act (CRA) purposes, the bank is not required to collect census tract (CT) or revenue information on business loans. However, management does collect this information.

Through testing, we found the data to be reliable; therefore, we used the bank's full report of 167 business loans originated or renewed in 2013 and 2014 in conducting our analysis of business loans.

DESCRIPTION OF INSTITUTION

Preferred is a full-service community bank headquartered at 11757 Katy Freeway, Suite 100, in Houston, Texas. Preferred is a wholly owned subsidiary of Preferred Bancshares, Inc., a one-bank holding company. The bank operates its home office and four branches within the state of Texas.

Preferred offers lobby services Monday through Friday, 9:00 am – 4:00 pm with the exception of the main office hours of 9:00 am – 5:00 pm. All locations offer drive through hours of 8:00 am - 6:00 pm, night deposit drops, and automated teller machines (ATM). ATMs have 24-hour access with the exception of the home office hours of Monday – Friday 6:00 am – 7:00 pm and Saturday 8:00 am- 12:00 pm. The bank also offers free ATM services through the Allpoint Network. Additionally, safe deposit boxes are located at the main office and The Woodlands branch locations.

The bank offers a wide range of commercial and consumer loan and deposit products and other banking services including remote deposit capture, online banking, debit cards, wire transfer, and merchant services.

As of December 31, 2014, total assets were \$219 million and the tier one leverage capital ratio was 15.75 percent. The bank's primary loan products are business loans and residential real estate. By dollar amount, business financing represented 34.33 percent and residential real estate financing represented 25.58 percent of total loans. More weight was given to business lending as a result. The bank has offered mortgage loans since inception with 30 and 15 year terms. In 2013, the mortgage loan changed to a 66 month fixed rate loan with a 30 year amortization and a minimum credit score of 620.

Preferred was rated "Satisfactory" at its last CRA performance evaluation dated August 9, 2010.

DESCRIPTION OF ASSESSMENT AREA(S)

Preferred has one AA in Texas, that consists of three contiguous counties located in the Houston-The Woodlands-Sugar Land Metropolitan Statistical Area (MSA), formerly known as the Houston-Baytown-Sugar Land MSA. The AA consists of all CTs in Harris County, Montgomery County, and Fort Bend County. All counties and CTs in the AA are contiguous.

During the review period, there were CT changes between 2013 and 2014. According to 2010 U.S. census data, the population of the AA is approximately 4.1 million. The AA contains 921 census tracts (CT). In 2014, the AA consists of 122 low-income CTs (13%), 268 moderate-income CTs (29%), 231 middle-income CTs (25%), 296 upper-income CTs (32%), and 4 CTs with no income designation (1%). In 2013, there were 126 low-income CTs (13%), 269 moderate-income CTs (29%), 230 middle-income CTs (25%), 292 upper-income CTs (32%), and 4 CTs with no income designation (1%). According to Housing and Urban Development data, the adjusted MSA median family income for 2013 and 2014 was \$66,200 and \$68,400 respectively.

Harris County

Harris County is the headquarters of Preferred. In 2014, of the 786 CTs in Harris County, 121 are low-income (15%), 251 are moderate-income (32%), 183 are middle-income (23%), 228 are upper-income (29%), and 3 have no designation (1%). According to the U. S. Census, as of 2010, the population was 2.1 million. Harris County is the most populous county in Texas and the third most populous in the nation. Additionally, according to the Texas Workforce Commission, the unemployment rate as of 2014 was 4.9 percent.

Banking competition in the Houston MSA is intense. According to the June 30, 2014 FDIC Market Share Report, there were approximately 82 financial institutions operating 1,024 branches in the bank's AA. The top three competitors are JP Morgan Chase Bank, National Association (NA), Wells Fargo Bank, NA, and Bank of America, NA. Preferred operates three branches in Harris County and has 0.07 percent of the market share.

Montgomery County

Montgomery County is located north of Houston and has 59 CTs, of which 1 is designated as a low-income CT (2%), 9 are moderate-income CTs (15%), 21 are middle-income CTs (36%), and 28 are upper-income CTs (47%). The county includes the communities of Conroe, Montgomery, Magnolia, The Woodlands, and Shenandoah. The county seat is Conroe. According to the U.S. Census, as of 2010, the population was approximately 456 thousand and according to the Texas Workforce Commission, unemployment was 4.4 percent as of 2014.

Banking competition in Montgomery County is intense. According to the June 30, 2014 FDIC Market Share Report, there were approximately 31 financial institutions operating 143 branches in the bank's AA. The top three competitors are Wells Fargo Bank, NA, Woodforest Financial Group, and JP Morgan Chase, NA. Preferred operates two branches in Montgomery County and has 0.03 percent of the market share.

Fort Bend County

The county is comprised of 76 CTs and has no low-income CTs, 8 moderate-income CTs (10%), 27 middle-income CTs (36%), 40 upper-income CTs (53%) and 1 CT (2%) without a designation. The county seat is Richmond.

According to the U.S. Census, as of 2010, the population was 585 thousand and according to the Texas Workforce Commission, unemployment was 4.5 percent as of 2014.

Banking competition in Montgomery County is intense. According to the June 30, 2014 FDIC Market Share Report, there were approximately 40 financial institutions operating 138 branches in the bank's AA. The top three competitors are Wells Fargo Bank, NA, and JP Morgan Chase, NA, and Bank of America, NA. Preferred does not maintain any branches in Fort Bend County.

Community Contact

There are many community and economic development organizations throughout the Houston AA. During the review period, we spoke with a representative of a nonprofit organization that is located in Harris County. The organization is involved with minority owned small business development and directly serves small businesses owned by ethnic minorities, but also serves as a referral agency to other small business owners. The contact indicated there is a need for working capital and construction lines of credit (LOC) and asset backed LOCs and loans.

In response to the community credit needs, Preferred offers LOCs for construction projects and working capital.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

LENDING TEST

Preferred Bank's performance under the lending test is satisfactory.

Loan-to-Deposit Ratio

The bank meets the standard for satisfactory performance. The LTD ratio is below peer average but is reasonable given the bank's performance context. Preferred is the depository institution for several title companies with aggregate deposits ranging from \$20 million to \$40 million on a monthly basis. Therefore, it has a significant volume of deposits that are not available for lending.

The bank's LTD ratio averaged 55.80 percent in the 20 quarters since the prior CRA evaluation. The average LTD ratio for a peer group of banks headquartered in Harris County with assets between \$144 million and \$250 million was 63.89 percent, ranging from a low of 53.16 percent to a high of 74.62 percent. Excluding title company deposits, Preferred's LTD ratio averaged 67.35 percent since the prior CRA evaluation.

Lending in Assessment Area

A substantial majority of the bank’s lending is inside the AA by number and dollar amount of loans originated. Of the total number of business and residential mortgage loans originated in the evaluation period, 90 percent were within the AA. By dollar amount, 89 percent of loans were within the AA. The following table details the bank’s lending inside and outside the AA by number and dollar amount:

Table 1 - Lending in AA										
Loan Type	Number of Loans					Dollars of Loans (in thousands)				
	Inside		Outside		Total	Inside		Outside		Total
	#	%	#	%		\$	%	\$	%	
Residential	48	89	6	11	54	16,457	91	1,670	9	18,127
Business	152	91	15	9	167	65,754	88	8,606	12	74,360
Totals	200	90	21	10	221	82,211	89	10,276	11	92,487

Source: HMDA LARs; Data collected by bank.

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

Distribution of loans to businesses reflects reasonable penetration to businesses with revenues less than \$1 million and residential mortgage loans reflects reasonable penetration to borrowers of different income levels. More weight was given to business loans as business loans represented a higher volume by dollar amount.

Business Loans

Lending to businesses with different revenue levels reflects reasonable penetration. The distribution of 2013 loans to small businesses with gross annual revenues of \$1 million or less reflects penetration by number of loans that is near to the level of such businesses operating in the AA based on the 2010 Census information. The bank’s performance is shown in the following table:

Table 2C - Borrower Distribution of 2013 Loans to Businesses in AA				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/ Unknown	Total
% of AA Businesses	71.64	3.88	24.48	100.00%
% of Bank Loans in AA by #	60.24	37.35	2.41	100.00%
% of Bank Loans in AA by \$	63.89	35.50	0.61	100.00%

Source: Dun and Bradstreet data; loan sample.

The bank’s distribution of 2014 loans to small businesses reflects penetration by number of loans that is somewhat lower than the level of such businesses operating in the AA based on the 2010 Census information. The bank’s performance is shown in the table on the following page.

Table 2D - Borrower Distribution of 2014 Loans to Businesses in AA				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/ Unknown	Total
% of AA Businesses	71.43	4.45	24.12	100.00%
% of Bank Loans in AA by #	49.32	49.32	1.36	100.00%
% of Bank Loans in AA by \$	42.10	57.74	0.16	100.00%

Source: Dun and Bradstreet data; loan sample.

Residential Loans

The bank’s overall distribution of loans to borrowers of low- and moderate-income (LMI) is reasonable. The percentage of home purchase loans to low-income borrowers exceeds that of other lenders in the AA and is near to that of other lenders in the AA for moderate-income borrowers. The following table reflects borrower distributions.

Table 2A - Borrower Distribution of 2013 Residential Real Estate Loans in AA								
Borrower Income Level	Low		Moderate		Middle		Upper	
	% of Loans by AA Lenders	% of Number of Loans	% of Loans by AA Lenders	% of Number of Loans	% of Loans by AA Lenders	% of Number of Loans	% of Loans by AA Lenders	% of Number of Loans
Home Purchase	1.81	4.76	11.45	9.52	26.98	14.29	59.76	71.43

Source: 2013 HMDA LAR; 2013 Peer Mortgage Data.

The bank’s performance for 2014 residential loans reflects penetration of low- and moderate-income families significantly below that of other lenders in the AA. There were no residential loans to borrowers in the low and moderate income census tracks; however, the peer dispersion was low. As previously mentioned, the bank has traditionally offered 30 and 15-year mortgage loans. In 2013, the bank’s mortgage lending program changed to a loan product comprised of 66 month fixed rate loans that are amortized over 30 years, with a minimum credit score of 620. The bank’s performance is shown in the following table.

Table 2B - Borrower Distribution of 2014 Residential Real Estate Loans in AA								
Borrower Income Level	Low		Moderate		Middle		Upper	
	% of Loans by AA Lenders	% of Number of Loans	% of Loans by AA Lenders	% of Number of Loans	% of Loans by AA Lenders	% of Number of Loans	% of Loans by AA Lenders	% of Number of Loans
Home Purchase	1.81	0.00	11.45	0.00	26.98	29.63	59.76	70.37

Source: 2014 HMDA LAR; 2013 Peer Mortgage data.

Geographic Distribution of Loans

The overall geographic distribution of loans reflects outstanding dispersion for business loans in the bank’s AA and poor dispersion in LMI CTs for residential mortgage loans. More weight was given to business loans, as these constitute a larger volume of loans.

Business Loans

The bank’s geographic distribution of small business loans in low-income CTs and moderate-income CTs exceeds the AA census characteristics in 2013 and significantly exceeds the AA census characteristics in 2014.

For small business loans originated in 2013, the bank’s dispersion in low-income CTs was 11.48 percent compared to the 2010 AA census characteristics of 8.80 percent. The dispersion in moderate-income CTs was 23.85 percent compared to the 2010 AA census characteristics of 20.48 percent. The bank’s performance is shown in the following table.

Table 3C - Geographic Distribution of 2013 Loans to Businesses in 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
Commercial	8.80	11.48	20.48	23.85	24.47	24.45	46.19	40.22

Source: Dun and Bradstreet data; data collected by bank.

Note: Income information was not available for 0.06% of AA CTs.

The bank’s distribution of 2014 loans to small businesses with gross annual revenues of \$1 million or less reflects penetration by number of loans that significantly exceeds the level of such businesses operating in the AA based on the 2010 census information. The bank’s performance is shown in the following table.

Table 3D - Geographic Distribution of 2014 Loans to Businesses in Houston 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
Commercial	8.63	10.43	19.91	36.05	24.19	17.04	47.21	36.48

Source: Dun and Bradstreet data; data collected by bank.

Note: Income information was not available for 0.06% of AA CTs.

Residential Loans

For the year 2013, the geographic distribution of residential loans to low-income families was below the AA peers. There were no residential loans to borrowers in the low income census tract; however, the peer dispersion was low at 4.55 percent. The dispersion of loans to moderate-income families was somewhat lower than the AA peers. The bank’s performance is shown in the following table:

Table 3A - Geographic Distribution of 2013 Residential Real Estate Loans in Houston AA								
Census Tract Income Level	Low		Moderate		Middle		Upper	
Loan type	% of Loans by AA Lenders	% of Number of Loans	% of Loans by AA Lenders	% of Number of Loans	% of Loans by AA Lenders	% of Number of Loans	% of Loans by AA Lenders	% of Number of Loans
Home Purchase	4.55	0.00	21.94	14.29	28.91	19.04	44.60	66.67

Source: 2013 HMDA LAR; U.S. Census data.

For year 2014, the bank had no residential loans to low- and moderate-income families, which was significantly below the AA census characteristics as shown in the table below.

Table 3B - Geographic Distribution of 2014 Residential Real Estate Loans in Houston AA								
Census Tract Income Level	Low		Moderate		Middle		Upper	
Loan type	% of Loans by AA Lenders	% of Number of Loans	% of Loans by AA Lenders	% of Number of Loans	% of Loans by AA Lenders	% of Number of Loans	% of Loans by AA Lenders	% of Number of Loans
Home Purchase	13.25	0.00	29.10	0.00	25.08	29.63	32.14	70.37

Source: 2014 HMDA LAR; U.S. Census data.

Note: Income information was not available for 0.43% of AA CTs.

Responses to Complaints

Preferred received one complaint during the review period and responded in a timely manner.

Fair Lending or Other Illegal Credit Practices Review

Pursuant to 12 C.F.R. 25.28(c), or 12 C.F.R. 195.28(c), in determining a national bank's (bank) or Federal savings association's (FSA) CRA rating, respectively, the OCC considers evidence of discriminatory or other illegal credit practices in any geography by the bank or FSA, or in any assessment area by an affiliate whose loans have been considered as part of the bank's or FSA's lending performance.

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