

# SMALL BANK



Office of the Comptroller of the Currency

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## PUBLIC DISCLOSURE

June 24, 2013

## COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

First Federal Savings of Middletown  
Charter Number: 702201

22 James Street  
Middletown, New York 10940-5710

Office of the Comptroller of the Currency

New York Metro Field Office  
Harborside Financial Center Plaza Five, Suite 1600  
185 Hudson St  
Jersey City, NJ 07311

**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.**

The overall rating is based on the following factors:

- The bank's average loan-to-deposit ratio is less than reasonable.
- A substantial majority of the bank's primary lending product originated during the evaluation period was made within the bank's assessment area (AA).
- Consumer lending products, particularly home equity lines of credit, reflect a reasonable distribution of loans to low- and moderate-income borrowers when compared to area demographics.
- The geographic distribution of loans throughout census tracts of different income levels is reasonable when compared to area demographics.
- The bank has no consumer complaints regarding its community reinvestment performance.

## **Scope of Examination**

This Performance Evaluation assesses the bank's performance in meeting the credit needs of the communities in which it serves. We evaluated First Federal Savings of Middletown (FFSM) under the Small Bank performance criterion, which includes a Lending Test.

The overall evaluation period covers June 5, 2008 (date of the prior CRA evaluation) through June 24, 2013. The evaluation period for the lending test covers the bank's performance from January 1, 2010 through December 31, 2012. Under the lending test, we focused our review on the bank's consumer lending activity, which consists of home equity lines of credit (HELOCs), as this was the bank's primary lending product by number and dollar volume originated during the evaluation period. Due to the limited loan volume, each of the consumer loans originated during our evaluation period were included in our loan sample. While the bank also engages in residential mortgage lending, it is not the primary lending product, and as such, residential loans were not included in our evaluation.

In assessing the bank's CRA performance, consideration is given to the bank's financial capacity, its size, local economic and demographic factors, market competition, and any legal impediments.

## Description of Institution

FFSM is a federally chartered savings association located in Middletown, NY. The bank primarily serves the Orange County area and operates solely at the institution's main office in Middletown, NY. The main office is located in a moderate-income census tract. The Monroe Branch of the bank was sold to Hometown Bank on September 9, 2011.

FFSM offers a traditional range of loan and deposit products. The institution's primary lending product is HELOCs. Additional product offerings include residential mortgage loans, commercial real estate, and small business loans. FFSM offers the following deposit products: checking, money market, simplified employee pension plans, tax escrow accounts, certificates of deposit, and individual retirement accounts. Additionally, the institution provides direct deposit, bank-by-mail, and night depository services.

As of December 31, 2012, FFSM reported total assets of \$162 million, with \$20 million in total loans and \$97 million in total deposits. See Table 1 below for detailed information on the composition of the bank's loan portfolio.

Table 1 – Loan Distribution as of December 31, 2012		
Loan Type	Dollar Amount (000s)	Percent of Total Loans (%)
Residential Mortgage	\$3,396	16.62
Commercial Mortgage	4,781	23.40
Commercial Nonmortgage	292	1.43
Consumer Loans (including HELOCs)	11,962	58.55
<b>Total Loans</b>	<b>\$20,431</b>	<b>100%</b>

Source: December 31, 2012 Consolidated Report of Income

FFSM's continues to experience a significant decrease in its loan portfolio. Total loans have declined \$9.2 million or 31.0 percent since the previous CRA examination (as of June 5, 2008). The decline was primarily in the residential mortgage portfolio, which dropped \$5.2 million from \$8.6 million, or 60.7 percent. The bank originated only two residential mortgages during the evaluation period. Consumer loans fell by 16.7 percent, or \$2.4 million.

Management continues to maintain an ongoing relationship with a diverse selection of community groups including, but not limited to the following: The City of Middletown's Office of Economic and Community Development, Cornell Cooperative Extension of Orange County, Orange County Rural Development Corporation (OCRDAC), Regional Economic Community Action Program (RECAP), and Emergency Housing Group

(EHG). FFSM maintains a dialog with these groups in order to stay informed of local housing needs and any related financing opportunities that may develop.

There are no financial or legal factors impeding the bank's ability to help meet the credit needs of the communities it serves. FFSM received a *Satisfactory* rating for the previous CRA evaluation dated June 5, 2008.

## **Description of Assessment Area**

FFSM's AA consists of the entire political sub-division of Orange County in New York State. Orange County is located within the Poughkeepsie-Newburgh-Middletown, NY Metropolitan Statistical Area (MSA). FFSM's AA meets the requirements of the regulation and does not arbitrarily exclude any low- or moderate-income (LMI) geographies. It has not changed since the prior CRA examination. FFSM's performance in 2010 and 2011 is evaluated using 2000 US Census Data and the bank's performance in 2012 is evaluated using 2010 US Census Data.

According to the 2000 US Census, the total population of the AA was 341,367 with 114,809 households and 85,028 families. The AA consists of 67 census tracts. Of the 67 census tracts, 7.46 percent are classified as low-income geographies, 20.90 percent are moderate-income geographies, 52.24 percent are middle-income geographies, and 19.40 percent are upper-income geographies. The 2011 Housing and Urban Development Agency (HUD) adjusted median family income for this AA was \$86,100. Within this AA, 20.71 percent of the families are low-income, 18.19 percent are moderate-income, 24.08 percent are middle-income and 37.02 percent are upper-income.

The 2010 US Census reported total population of this AA at 372,813 with 124,379 households and 90,356 families. The AA consists of 79 census tracts. Of the 79 census tracts, 8.86 percent are classified as low-income geographies, 17.72 percent are moderate-income geographies, 50.63 percent are middle-income geographies, and 22.78 percent are upper-income geographies. The 2012 HUD adjusted median family income for this AA was \$87,200. Within this AA, 20.8 percent were classified as low- and moderate-income.

The unemployment rate as of year-end 2012 for Poughkeepsie, principal city of the Poughkeepsie-Newburgh-Middletown MSA, which includes all of Dutchess and Orange counties, was 8.1 percent, which is higher than the national average of 7.8 percent.

According to the January 2013 Moody's Analytics report, the largest industry sectors in the Poughkeepsie County MSA are Education and Health Services (20.7 percent)

Government (20.6 percent), Retail trade (14.7 percent), and Professional and Business Services (8.8 percent). IBM is the dominant employer (11,590 employees) within the MSA, followed by the U.S. Military Academy at West Point (3,120) and Orange Regional Medical Center (2,524). The remaining top 20 employers in the MSA are comprised primarily of the health care (8 employers) and education (5 employers) sectors.

FFSM's market for lending opportunities is competitive. The bank competes with local, regional, and nationwide financial institutions. According to the Federal Deposit Insurance Company (FDIC) deposit market share report as of June 2012, FFSM ranked 21 out of 29 institutions within the Poughkeepsie area MSA, with a deposit market share of 1.0 percent.

We interviewed a local community contact regarding community credit needs and business opportunities. The organization relies on state funds, grants, and local legislatures to service the community. With respect to residential mortgages, the contact identified credit unions as strong competitors to local institutions. Additionally, refinancing was noted as a common alternative to lines of credits due to the historically low fixed-rate mortgage market. Although some foreclosures exist within suburban and rural communities of the MSA, local institutions were not identified as related lenders. The bank was noted as having met the credit needs of the community.

## **Conclusions with Respect to Performance Tests**

### **LENDING TEST**

#### **Loan-to-Deposit Ratio**

FFSM's quarterly average loan-to-deposit (LTD) ratio is less than reasonable given the bank's size, capacity to lend, demographic and economic factors, and credit needs of the AA. The LTD ratio was calculated using quarterly information over the past twenty quarters (June 30, 2008 to March 31, 2013) since the previous CRA examination. The calculated LTD ratio was 21.4 percent. Quarterly LTD ratios for the bank ranged from a low of 18.9 percent at June 30, 2011 to 24.2 percent at September 30, 2008. The ratio is lower than the average quarterly LTD ratio of six banks in New York with similar asset sizes. The custom peer average was 60.6 percent with average ratios during the period ranging from 54.0 percent to 65.8 percent. The lowest individual ratio during the period was 33.2 percent. The local peer consisted of New York banks with total assets between \$100 million and \$200 million.

A low-rate mortgage environment, coupled with still depressed property values has hindered the bank’s HELOC loan volume. Variable rate HELOC products remain temporary out of favor as borrowers typically opt to refinance due to historically low interest rates instead of pursuing lines of credit. However, the bank attempted to address the dampened HELOC activity by aggressively pricing the loans at Prime minus 2.0 percent. Although the rate and terms offered were the lowest in Orange County for a period, few HELOCs were originated.

FFSM’s LTD ratio did not meet the standard for satisfactory performance in the prior evaluation. Although management’s risk-based business decision to remain conservative in mortgage markets is reasonable, the bank’s LTD ratio continued to decline during the evaluation period and does not compare favorably to peer institutions.

**Lending in Assessment Area**

A substantial majority of FFSM’s loans were originated inside its AA. During the evaluation period, on a combined basis, for the 3 year period 2010 and 2012, 88.9 percent by number and 93.4 percent by dollar amount of FFSM’s consumer loan originations were within the AA. Table 2 below illustrates the bank’s HELOC lending activities by volume and dollar amount of loans. Based on a sample of 2010-2011 data, approximately 91 percent of total loans by number were made within the AA.

<b>Table 2 - Lending in the AA in 2010-2011</b>										
<b>Loan Type</b>	<b>Number of Loans</b>					<b>Dollars of Loans (000s)</b>				
	<b>Inside</b>		<b>Outside</b>		<b>Total</b>	<b>Inside</b>		<b>Outside</b>		<b>Total</b>
	<b>#</b>	<b>%</b>	<b>#</b>	<b>%</b>		<b>\$</b>	<b>%</b>	<b>\$</b>	<b>%</b>	
Consumer Loans	42	91.00	4	8.70	<b>46</b>	\$2,654	95.50	\$125	4.50	<b>\$2,779</b>

Source: 2010-2011 Loan Sample; 2000 U.S. Census Data

Table 2A below illustrates the bank’s HELOC lending activities by volume and dollar amount of loans for 2012. In 2012, approximately 75.0 percent of total loans by number, and 84.4 percent by dollar amount were made within the AA.

<b>Table 2A - Lending in the AA in 2012</b>										
<b>Loan Type</b>	<b>Number of Loans</b>					<b>Dollars of Loans (000s)</b>				
	<b>Inside</b>		<b>Outside</b>		<b>Total</b>	<b>Inside</b>		<b>Outside</b>		<b>Total</b>
	<b>#</b>	<b>%</b>	<b>#</b>	<b>%</b>		<b>\$</b>	<b>%</b>	<b>\$</b>	<b>%</b>	
Consumer Loans	6	75.00	2	25.00	<b>8</b>	\$542	84.42	\$100	15.58	<b>642</b>

Source: 2012 Loan Sample; 2010 U.S. Census Data

**Lending to Borrowers of Different Incomes**

FFSM’s lending reflects reasonable distribution among borrowers of different income levels. The distribution to borrowers of different income levels for HELOC loans originated in 2010 and 2011 is reasonable. Table 3 below illustrates the bank’s HELOC lending to borrowers of different income levels for 2010-2011. Of the 42 HELOC loans, 14.29 percent were originated to low-income households which is lower than the percentage of households considered low-income. Management’s distribution of loans to moderate-income households exceeded the percentage of households considered moderate-income.

Table 3 - Borrower Distribution of HELOC Loans in AA for 2010-2011*									
Borrower Income Level		Low		Moderate		Middle		Upper	
Loan Type	# of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans
HELOC Loans	42	22.72	14.29	16.22	23.81	20.12	28.57	40.94	33.33

Source: Sample of 2010-2011 HMDA Data; 2000 U.S. Census Data.  
 \*Percents are based on loans originated during the applicable year

FFSM’s lending in 2012 also reflects reasonable distribution among borrowers of different income levels. Table 3A below illustrates the bank’s HELOC lending to borrowers of different income levels for 2012. Of the six HELOC loans, the distribution of loans to low-income households is lower than the percentage of households considered low-income. Management’s distribution of HELOC loans to moderate-income household exceeded area demographics for moderate-income households.

Table 3A - Borrower Distribution of HELOC Loans in AA for 2012*									
Borrower Income Level		Low		Moderate		Middle		Upper	
Loan Type	# of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans
Consumer Loans	6	24.27	16.67	15.44	33.33	18.71	0.0	41.58	50.00

Source: 2012 Loan Sample; 2010 U.S. Census Data.  
 \*Percents are based on loans originated during the applicable year

**Geographic Distribution of Loans**

The geographic distribution of HELOC loans within the FFSM AA reflects reasonable distribution throughout census tracts of different income levels and meets the standards for satisfactory performance in both 2010-2011 and in 2012 given consideration to office location, higher number of rental units in the AA and competitive factors.

The geographic distribution of HELOC loans originated in 2010 and 2011 is reasonable. Management did not originate any loans in low-income tracts; however, despite 6.85

percent of the households located in these tracts, there is only 2.49 percent of owner-occupied housing in these tracts. Management’s record of originating HELOC loans in moderate-income tracts exceeds the percentage of households in those tracts, and significantly exceeds the percentage of owner-occupied housing of 10.51 percent.

Table 4 below reflects the percentage of households in each income tract and the percentage of HELOC loans made by the bank in each income tract during 2010-2011.

4 - Geographic Distribution of HELOC Loans in AA for 2010-11									
Census Tract Income Level		Low		Moderate		Middle		Upper	
Loan Type	# of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans
HELOC Loans	42	6.85	0.0	16.28	19.05	58.27	73.81	18.59	7.14

Source: 2010-2011 Loan Sample; 2000 U.S. Census Data

The geographic distribution of HELOC loans originated in 2012 is reasonable. Management did not originate any HELOC loans in low-income tracts; however, despite 6.39 percent of the households located in these tracts, there is only 2.77 percent of owner-occupied housing in these tracts. Management’s record of originating HELOC loans in moderate-income tracts exceeds the percentage of households in those tracts, and significantly exceeds the percentage of owner-occupied housing of 11.65 percent.

Table 4A below reflects the percentage of households in each income tract and the percentage of HELOC loans made by the bank in each income tract in 2012.

4A - Geographic Distribution of HELOC Loans in AA for 2012									
Census Tract Income Level		Low		Moderate		Middle		Upper	
Loan Type	# of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans	% of AA Households	% of # of Loans
HELOC Loans	6	6.39	0.0	15.88	16.67	52.60	50.00	25.13	33.33

Source: 2012 Loan Sample; 2000 U.S. Census Data.

**Responses to Complaints**

A review of OCC’s Customer Assistance Group’s complaint records, as well as the bank’s Public CRA File, revealed no CRA-related complaints filed since the prior examination. Therefore, analysis of this criterion was not applicable.

**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.