



# 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 17, 2008

## COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

Palm Desert National Bank  
Charter Number: 17121

73-745 El Paseo Drive  
Palm Desert, California 92261-0000

Office of the Comptroller of the Currency

Southern California South Field Office  
1925 Palomar Oaks Way, Suite 202  
Carlsbad, California 92008-6526

**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 Lending Test is rated: Satisfactory**

**The Community Development Test is rated: Satisfactory**

The primary factors supporting the bank's rating are as follows.

- The bank originates a substantial majority of loans within its assessment area.
- The average loan-to-deposit ratio is reasonable, and the ratio has trended upward.
- Lending to businesses of different income levels is reasonable.
- The geographic distribution of loans does not meet the standard for satisfactory performance, but management has taken significant steps to improve lending in moderate income areas.
- The bank demonstrates satisfactory responsiveness to meeting community development needs.

## **Scope of Examination**

This is Palm Desert National Bank's (PDNB) first Community Reinvestment Act (CRA) examination under the "Intermediate Small Bank" examination process. This process includes an evaluation of activity under the Lending Test criteria, as well as activities under the Community Development Test. We evaluated performance under the Lending Test using a random sample of commercial loans, because they represent the substantial majority of the bank's lending activity. We tested commercial loans originated or purchased beginning January 1, 2006, through September 30, 2008. The Community Development Test covers performance since the last CRA examination, from May 5, 2004, through September 30, 2008.

## **Description of Institution**

PDNB is a wholly owned subsidiary of Palm Desert Investments, a one-bank holding company. PDNB provides a full range of banking services to customers through its main office and three branches located in the Coachella Valley in Riverside County, California. The main office in the City of Palm Desert opened in December 1981, the Rancho Mirage branch opened in March 1999, and the La Quinta branch opened in December 2001. All three of these branches are located in middle-income census tracts. In June 2007, the bank opened a new full-service branch in the City of Palm Springs; a moderate-income census tract within the bank's assessment area (AA). The bank has not closed any branches since the last evaluation. The bank is closing a loan production office at year-end 2008 given the current weak and declining market conditions. The loan production office only originated construction loans, and it had been in operations for two years.

PDNB provides traditional banking services at all of its branches. The bank offers a variety of loan and deposit products, as well as automatic teller machines (ATMs) at each branch location, online banking, wire transfer services, and safe deposit boxes. Saturday hours at two branch locations (Palm Desert and La Quinta) help working persons in the AA to access banking services more readily. The Electronic Banking Solutions (EBS) division has historically been a strong second line of business, which included providing non-proprietary ATM cash placement and cash management services. These products ultimately proved to be highly competitive and leading management to sell that portion of EBS effective September 30, 2008. Other EBS products and services remain active and include a stored value card program, ACH services, and merchant credit card services.

PDNB is a commercial bank with a primary strategic focus on lending to businesses, including commercial-industrial, commercial real estate, and construction lending. Consumer lending is not a significant business focus. The bank participates in several guaranteed loan programs that help meet business lending needs within the AA. These include the Bureau of Indian Affairs guaranteed loan program, the United States Department of Agriculture rural facilities program, the Small Business Administration 504 and 7(a) loan programs, and the State of California guaranteed loan program. Participation in these programs enables PDNB to lend to borrowers who might not otherwise qualify for direct bank financing.

As of September 30, 2008, PDNB's assets totaled \$403 million consisting of \$268 million in loans or 67 percent of assets. Deposits totaled \$321 million, and equity capital totaled \$38 million.

The following chart summarizes the loan portfolio by major loan type as reflected in the bank's September 30, 2008, Call Report of Condition and Income\*.

| <b>PALM DESERT NATIONAL BANK</b>            |                   |                |
|---------------------------------------------|-------------------|----------------|
| <b>Loan Portfolio by Major Product Type</b> |                   |                |
| <b>Loan Type</b>                            | <b>(000s)</b>     | <b>Percent</b> |
| Real Estate                                 | \$197,887         | 74%            |
| Commercial                                  | 67,651            | 25%            |
| Consumer                                    | 2,452             | < 1%           |
| Other                                       | 438               | < 1%           |
| <b>Total</b>                                | <b>*\$267,639</b> | <b>100%</b>    |

\*Individual loan categories do not equal the total amount of loans reported.

The bank has no legal, financial, or other factors impeding its ability to help meet credit needs in its AA. The bank's last performance evaluation dated May 5, 2004, under the "Small Bank" rating criteria, rated the bank as "Satisfactory."

## Description of Assessment Area(s)

PDNB's AA meets the requirements of the regulation and does not arbitrarily exclude low- or moderate-income geographies. The AA consists of the 63 whole and contiguous census tracts that largely comprise what is known as the "Coachella Valley" portion of the Riverside-San Bernardino-Ontario Metropolitan Statistical Area 40140.

The delineated area includes the cities of Palm Springs, Cathedral City, Thousand Palms, Rancho Mirage, Palm Desert, Indian Wells, Bermuda Dunes, La Quinta, Indio, and Coachella. The AA population was 274,752 according to the 2000 U.S. Census Bureau. Of the 63 AA census tracts, 2% are low-income, 33% are moderate-income, 40% are middle-income, and 25% are upper-income. The low- and moderate-income tracts are located in the northern and eastern parts of the AA.

The Demographic Research Unit of the California Department of Finance estimated the area population as 337,692 at January 1, 2008. The median housing value in the area according to the 2000 U.S. Census Bureau was \$152,315 with approximately 48% of all housing units owner occupied. The California Desert Association listed the median home value at \$311,540 as of March 2008. The Housing and Urban Development updated median household income is \$57,500.

The Coachella Valley is a national destination for tourists, conventions, and seasonal second homeowners. The local economy is heavily dependent upon those with discretionary income, and it is vulnerable to seasonal and economic fluctuations locally and nationally.

According to the California Employment Development Department, the unemployment rate in the Coachella Valley ranged from 3.3% in Indian Wells to 15.3% in Coachella as of September 30, 2008. Riverside County and the State of California had a 9.5% and 7.7% unemployment rates, respectively. The current economic conditions have hindered growth opportunities in most of the employment sectors. However, the medical community is expanding health facilities to provide care for the increasing elderly retirement population, and the education sector is adding more learning facilities to accommodate a general population increase.

Retail, hotel and amusement, small businesses, construction, agriculture, health care, and education are the primary employment sectors according to the Coachella Valley Economic Partnership. Major employers in the area include KSL Recreation Corporation, Eisenhower Medical Center, County of Riverside, Agua Caliente Band of Cahuilla Indians, and the Desert Sands Unified School District.

Banking competition is strong within the AA. Locally, a significant number of large and regional commercial banks, savings associations, credit unions, credit card companies, and non-bank institutional investors compete for the available commercial lending business. Major financial institutions in the area include Bank of America, Union Bank of California, PFF Bank and Trust, Rabobank, and California Bank and Trust.

Three community contacts by regulatory examiners in conjunction with this examination indicate a number of community development needs. These include job training programs; assistance for victims of spousal abuse; and services for low- and moderate income persons, including assistance for housing, utilities, and food. There also is a need for micro-loan funds to assist small businesses. All three organizations stated they recognize the limited resources financial institutions have in the current economic climate. One organization cited PDNB as an active participant in helping to meet community development and community credit needs.

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

### **LENDING TEST**

PDNB's performance under the Lending Test is satisfactory. The Lending Test includes an analysis of the bank's:

- quarterly average loan-to-deposit ratio;
- volume of lending within the AA;
- lending to businesses of different sizes; and
- geographic distribution of loans compared to area demographics.

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

PDNB's level of lending is reasonable. We analyzed the bank's quarterly average loan-to-deposit (LTD) ratio for the last 19 quarters: from the last CRA examination through September 30, 2008. During this period, the LTD ratio averaged 69%.

We compared the bank's average LTD ratio with that of six peer banks that are similar in asset size and operating in areas having similar demographics within the Riverside-San Bernardino-Ontario MSA. The combined average quarterly LTD ratio of peer banks was 83% over the evaluation period. The bank's average LTD ratio of 69% does not compare closely with the peer average. Favorably, the ratio is trending upward and compares more closely to peers. Over the most recent seven quarters, the LTD ratio has increased from 70% at March 31, 2007, to 81% at September 30, 2008.

Bank management expects the LTD ratio's upward trend to continue based on current and planned business strategies. Effective September 30, 2008, PDNB sold its business line of ATM cash placement services for non-proprietary ATMs and cash management services. This was an extensive operation for the bank and required a significant level of deposits for funding. Peer banks were not similarly engaged in these products during the evaluation period. As a result, this line of business limited the bank's lending ability in comparison to its peers.

PDNB's deposits totaled \$321 million at September 30, 2008, with \$106 million in brokered deposits, which funded the ATM cash placement operation. Due to the sale of

non-proprietary ATM cash placement and cash management services, the volume of brokered deposits will decrease and provide a positive effect on the bank's LTD ratio going forward.

In light of these facts and the positive trends, we conclude that PDNB's LTD ratio is reasonable and meets the standard of satisfactory performance.

**Lending in Assessment Area**

PDNB's level of lending within its AA exceeds the standard of satisfactory performance. Based on our random sample of 20 commercial loans, the bank originated a substantial majority by number and dollar amount within the AA.

Table 1 reflects the number and dollar volume of loans the bank originated or purchased inside and outside its AA.

**Table 1**

| <b>Lending in the Assessment Area<br/>Commercial Loans<br/>January 2006 through September 2008</b> |                        |            |                |            |                    |                               |            |                  |            |                          |
|----------------------------------------------------------------------------------------------------|------------------------|------------|----------------|------------|--------------------|-------------------------------|------------|------------------|------------|--------------------------|
|                                                                                                    | <b>Number of Loans</b> |            |                |            | <b>Total<br/>#</b> | <b>Dollar Amount of Loans</b> |            |                  |            | <b>Total<br/>(000's)</b> |
|                                                                                                    | <b>Inside</b>          |            | <b>Outside</b> |            |                    | <b>Inside</b>                 |            | <b>Outside</b>   |            |                          |
|                                                                                                    | <b>#</b>               | <b>%</b>   | <b>#</b>       | <b>%</b>   |                    | <b>\$(000's)</b>              | <b>%</b>   | <b>\$(000's)</b> | <b>%</b>   |                          |
| Commercial Loan Sample                                                                             | 16                     | 80%        | 4              | 20%        | 20                 | \$9,381                       | 88%        | \$1,227          | 12%        | \$10,608                 |
| <b>Percentages</b>                                                                                 |                        | <b>80%</b> |                | <b>20%</b> | <b>100%</b>        |                               | <b>88%</b> |                  | <b>12%</b> | <b>100%</b>              |

*Source: Random sample of 20 bank loan originations from January 2006 through September 2008*

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

The distribution of lending to businesses of different sizes is reasonable. For this analysis, we randomly sampled 20 commercial loans the bank originated within the AA from January 2006 through September 2008. We did not analyze consumer lending patterns because the bank is primarily a commercial lender.

PDNB originated 55 % of the number loans and 22 % of the dollar volume to small businesses (having gross annual revenues of \$1 million or less). While performance percentages for the sample do not compare closely to the Dunn and Bradstreet area demographic, the pattern is reasonably explained. Primarily, the bank's business strategies included granting loans that helped finance the high demand for construction loans within the AA during the evaluation period. This business strategy resulted in loans to businesses with higher revenues that qualified for these construction projects.

PDNB makes a concerted effort to meet the needs of small businesses within its AA. The bank granted 40 % of the number of loans in the sample to small businesses in loan amounts of less than \$500,000. Granting smaller sized loans to help meet credit needs of small businesses is an identified community credit need. (Also refer to the “Community Development Loans” section in this Performance Evaluation).

Table 2 reflects the distribution of loans to businesses of different sizes compared to area demographics.

**Table 2**

| <b>Lending to Business of Different Sizes<br/>Distribution of Commercial Loans<br/>January 2006 through September 2008</b> |              |              |       |
|----------------------------------------------------------------------------------------------------------------------------|--------------|--------------|-------|
| Business Revenue                                                                                                           | ≤\$1,000,000 | >\$1,000,000 | Total |
| % of AA Businesses *                                                                                                       | 70%          | 5%           | 100%  |
| % of Bank Loans in AA by #                                                                                                 | <b>55%</b>   | <b>45%</b>   | 100%  |
| % of Bank Loans in AA by \$                                                                                                | <b>22%</b>   | <b>78%</b>   | 100%  |

Source: \*Dunn & Bradstreet reported revenue data (25% of businesses did not report revenue data)

### **Geographic Distribution of Loans**

The geographic distribution of business loans does not meet the standard for satisfactory performance. Management has taken positive steps to improve geographic distribution of loans in the bank’s AA.

Among the 20 commercial loans in our random sample, there were none granted in the only low income census tract in PDNB’s AA. The bank does not arbitrarily avoid lending in this low-income tract and lending opportunities are limited. Dunn & Bradstreet data reflect that less than one percent of AA area businesses are located in this one tract.

PDNB originated 30 % of the number of sampled loans to businesses located in moderate-income census tracts, which is below the Dunn & Bradstreet 50 % area demographic. This is explained in large part by strong competition among other financial institutions in the AA. Management stated they are making every effort to lend throughout the bank’s AA with no arbitrary exclusions. In June 2007, the bank opened a full-service branch in a moderate-income census tract where management expects an increased level of lending going forward.

Table 3 reflects the geographic distribution of loans in the sample compared to area demographics.

**Table 3**

| Geographic Distribution of Commercial Loans<br>January 2006 through September 2008 |                     |                      |                    |                      |                    |                      |                    |                      |
|------------------------------------------------------------------------------------|---------------------|----------------------|--------------------|----------------------|--------------------|----------------------|--------------------|----------------------|
| Census Tract Income Levels                                                         | Low                 |                      | Moderate           |                      | Middle             |                      | Upper              |                      |
|                                                                                    | % 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 Loan Sample                                                             | <1%                 | <b>0%</b>            | 30%                | <b>15%</b>           | 41%                | <b>70%</b>           | 29%                | <b>15%</b>           |

\* Source: Dunn & Bradstreet business data by geographic location

**Responses to Complaints**

The bank has not received any CRA-related complaints since the previous CRA examination.

**COMMUNITY DEVELOPMENT TEST**

PDNB demonstrates satisfactory responsiveness to meeting community development (CD) needs within its AA, considering the bank's capacity and area needs.

**Community Development Loans**

The bank originated three CD loans totaling \$10.2 million, representing more than 26% of tier one capital at September 30, 2008. The loans are to various nonprofit organizations, most notably two that provide services to area residents who range from very low- to moderate-income levels.

Additionally, PDNB participates in several government-guaranteed loan programs that enable the bank to lend to borrowers who might not otherwise qualify for conventional direct bank financing. These include the SBA 7(a) loan program, the SBA 504 loan program, the State of California guaranteed loan program, the Bureau of Indian Affairs guaranteed loan program, and the USDA rural facilities loan program.

### **Qualified Community Development Investments**

During the review period, PDNB made seventeen contributions totaling \$37,000. These organizations provide a variety of services that benefit low-and moderate-income individuals and families.

### **Community Development Services**

Bank management strongly encourages its employees to participate in community activities. Many of those activities are targeted at low- and moderate-income individuals and organizations. Examiner contacts with community-based organizations during this examination confirmed they consider the bank to be a valued partner in helping to assist with needed services in the area. Of the bank's senior managers, eight participate on a total of 13 boards or committees that meet regularly to help provide financial and other services that meet the criteria for community development.

### **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.