



INTERMEDIATE SMALL BANK

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

PUBLIC DISCLOSURE

June 29, 2009

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

Hillsdale County National Bank
Charter Number 14062

One South Howell Street
Hillsdale, MI 49242

Office of the Comptroller of the Currency

Cleveland & Detroit Field Office
26877 Northwestern Highway Omni Centre, Suite 411
Southfield, MI. 48034-8418

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 major factors supporting the institution's rating are:

- The distribution of loans to borrowers of different incomes and businesses of different sizes is reasonable.
- The geographic distribution of loans is reasonable.
- The bank's loan-to-deposit ratio is more than reasonable and exceeds the standards for satisfactory performance.
- A substantial majority of lending activity has occurred within the bank's AAs. This performance exceeds the standards for satisfactory performance.
- The bank's community development performance demonstrates good responsiveness to community development needs in its AA.

Scope of Examination

The evaluation period is October 18, 2004 (date of the previous evaluation) through June 29, 2009. We analyzed home mortgage and business loan activity from January 1, 2006 through December 31, 2008. All home mortgage data was considered, including originations made by CNB Lending Services, LLC, a bank affiliate. Analyses of business loan activity were based on a sample of 60 loans. We also considered community development loan, investment, and service activity from October 18, 2004 through June 29, 2009.

For evaluation purposes the bank has two assessment areas (AAs), as discussed under the Description of Assessment Areas section. Conclusions on the bank's performance are based on full-scope reviews of each of these areas.

Information from members of the local community was considered. We contacted five community organizations that are involved with affordable housing, social services for low- and moderate-income individuals, and economic development initiatives. Refer to the Description of Assessment Areas section for additional information.

Description of Institution

Hillsdale County National Bank (HCNB) is a full-service intrastate community bank headquartered in Hillsdale, Michigan. As of December 31, 2008, the bank had total

assets of \$303 million. HCNB is a wholly owned subsidiary of CNB Community Bancorp, Inc., also headquartered in Hillsdale. The bank has 11 full-service offices plus an additional drive-through facility that serve Hillsdale County and portions of Calhoun, Jackson, and Lenawee Counties in south central Michigan. One branch in the city of Jackson was opened during the evaluation period. In 2002, CNB Lending Services, LLC was formed as a bank subsidiary to originate single-family home mortgage loans. HCNB offers a broad range of loan products, including home mortgage, consumer, commercial, and agricultural loans. As of December 31, 2008 the bank’s loan portfolio was comprised of real estate loans (74 percent), consumer loans (10 percent), commercial loans (14 percent), and other loans (2 percent). Using bank-generated loan origination reports for the evaluation period, we determined the bank’s primary products are home mortgage loans and business loans. There are no financial or legal impediments that adversely impact the bank’s ability to address community needs. The previous CRA examination was dated October 18, 2004 and resulted in a rating of ‘satisfactory.’

Description of Assessment Areas

For analysis purposes, HCNB has two assessment areas as described below:

Hillsdale Assessment Area

Demographic Information for the Hillsdale AA					
Demographic Characteristics	#	Low % of #	Moderate % of #	Middle % of #	Upper % of #
Geographies (Census Tracts)	14	0.00	0.00	100.00	0.00
Population by Geography	57,287	0.00	0.00	100.00	0.00
Owner-Occupied Housing by Geography	17,313	0.00	0.00	100.00	0.00
Businesses by Geography	3,879	0.00	0.00	100.00	0.00
Farms by Geography	406	0.00	0.00	100.00	0.00
Family Distribution by Income Level	15,585	14.54	18.13	25.21	42.12
Distribution of Low- and Moderate-Income Families throughout AA Geographies	5,092	0.00	0.00	100.00	0.00
Median Family Income	= \$44,067	Median Housing Value = \$94,900 Non-Adjusted Unemployment Rate May 2009 = 18.5%			
HUD Adjusted Median Family Income for 2008	= \$50,200				
Households Below the Poverty Level	= 7.99%				

Source: 2000 U.S. Census and 2008 HUD updated MFI.

The Hillsdale AA is a non-metropolitan area comprised of all of Hillsdale County plus two adjacent tracts in Lenawee County. This AA meets the requirements of the regulation. HCNB operates five full service offices and one drive-thru office in this AA. The bank’s main office is located in this AA. Based on the June 30, 2008 FDIC deposit

data, HCNB is ranked second with 23.56 percent share of the insured deposit market. Overall, there are ten insured deposit institutions that operate a total of 25 offices in the market area. Other major competitors include United Bank & Trust with a 28.49 percent market share, Flagstar Bank (9.99 percent), First Federal Bank of the MW (9.84 percent), and Fifth Third Bank with a 9.34 percent share of the deposit market.

The local economy weakened during the evaluation period with a continuing loss of manufacturing jobs. The area’s unemployment rate continues to outpace the state level. Michigan’s statewide non-adjusted rate was 13.9 percent in May 2009. Major employers include Tenneco Inc., Hillsdale College, Hi-Lex Controls Inc., and Wal-Mart.

Based on our discussions with the bank and members of the local community, there have been opportunities to participate in community development activities. Credit and non-credit needs in this AA include:

- A revolving loan fund to finance start-up businesses and provide gap financing
- Loans to assist new and existing downtown businesses with funds to upgrade or meet building codes related to heating, plumbing and electrical work.
- Loans to assist new downtown businesses with initial start-up costs such as legal fees, permits, & marketing efforts.
- Funding program to prevent homelessness within the community
- In-kind assistance to help with financial literacy and tax preparation programs.

Jackson Assessment Area

Demographic Information for the Jackson AA						
Demographic Characteristics	#	Low % of #	Moderate % of #	Middle % of #	Upper % of #	NA* % of #
Geographies (Census Tracts)	33	6.06	24.24	57.58	9.09	3.03
Population by Geography	136,192	2.83	16.35	68.28	10.34	2.21
Owner-Occupied Housing by Geography	37,229	0.71	13.91	72.60	12.78	0.00
Businesses by Geography	8,474	9.11	16.13	66.19	8.47	0.10
Farms by Geography	322	1.55	4.66	86.96	6.83	0.00
Family Distribution by Income Level	34,854	18.84	19.71	24.42	37.03	0.00
Distribution of Low- and Moderate-Income Families throughout AA Geographies	13,436	4.15	24.11	66.59	5.15	0.00
Median Family Income	= \$50,843	Median Housing Value = \$94,554 Non-Adjusted Unemployment Rate May 2009 = 14.1%				
HUD Adjusted Median Family Income 2008	= \$57,024					
Households Below the Poverty Level	= 9.48%					

(*) The NA category consists of geographies that have not been assigned an income classification.
Source: 2000 U.S. Census and 2008 HUD updated MFI.

The Jackson AA is comprised of a large portion of Jackson County (Jackson, Michigan MSA 27100) and one adjacent tract in Calhoun County (Battle Creek, Michigan MSA 12980). While in different MSAs, the Calhoun County tract was combined with the Jackson County tracts because meaningful analyses would be difficult for a single census tract. This AA meets the requirements of the regulation. The AA's boundaries do not extend substantially beyond the Jackson MSA, and contain all the bank's area branches. No low- or moderate-income neighborhoods are arbitrarily excluded. HCNB operates six branches in this AA, including one office opened in the city of Jackson during the evaluation period. Based on the June 30, 2008 FDIC deposit data, HCNB is ranked sixth in size with a 4.68 percent share of the insured deposit market. Competition is strong. In total, there are 11 insured deposit institutions operating 45 offices in the area. The institutions with the greatest presence are Flagstar Bank (35.71 percent market share), Citizens Bank (25.98 percent share), and Comerica Bank with a 16.44 percent market share.

The economy weakened during the evaluation period. While some job sectors have recorded increases, manufacturing jobs have declined. The area's unemployment rate is comparable to the May 2009 State of Michigan non-adjusted statewide rate of 13.9 percent. Major employers include Foote Health Systems, CMS Energy, Michigan Department of Corrections, Eaton Corporation, Michigan Automotive Compressor, and Allegiance Health.

Based on our discussions the bank and members of the local community, there have been opportunities to participate in community development activities. Credit and non-credit needs in this AA include:

- Funding for foreclosure rescue and prevention programs
- Funds for the trade skills employment programs
- In-kind assistance for education, financial literacy, and tax preparation programs
- A revolving loan fund to finance start-up businesses to create jobs

Conclusions with Respect to Performance Tests

LENDING TEST

Performance under the lending test is rated "satisfactory." The bank's performance meets or exceeds the standards of satisfactory performance for the individual components detailed below. The borrower and geographic distribution components receive the most weight.

Loan-to-Deposit Ratio

The bank's net loan-to-deposit ratio is more than reasonable and exceeds the standards for satisfactory performance given the bank's size, financial condition, and credit needs of the bank's AAs. The bank's average quarterly loan-to-deposit ratio over the past 17 quarters was 94.03 percent. This was somewhat higher than the 91.91 percent experienced by a 10-bank group of peer banks during the same time period. It is also

noted that HCNB’s loan-to-deposit ratio as of December 31, 2008 was 98.72 percent. Furthermore, HCNB is active in selling residential mortgages on the secondary market which is not reflected in the loan-to-deposit ratio. During our evaluation period, HCNB sold 729 residential mortgages totaling \$91 million.

Lending in Assessment Area

HCNB’s record of lending in the AAs area exceeds the standards for satisfactory performance. A substantial majority of lending activity has occurred within the bank’s AAs. As reflected in Table 1, approximately 86 percent of the number of loans and 80 percent of loan dollars originated during the evaluation period are located within the bank’s AAs. These percentages are based on all home mortgage activity and a sample of sixty small business loans originated by the bank during the evaluation period.

Table 1 - Lending in HCNB’s Assessment Areas										
Loan Type	Number of Loans					Dollars of Loans (000s)				
	Inside		Outside		Total	Inside		Outside		Total
	#	%	#	%		\$	%	\$	%	
Home Mortgage	1,120	85.37	192	14.63	1,312	121,280	79.57	31,141	20.43	152,421
Business	55	91.67	5	8.33	60	8,243	88.59	1,062	11.41	9,305
Totals	1,175	85.64	197	14.36	1,372	129,523	80.09	32,203	19.91	161,726

Source: Reported HMDA Data, and a sample of business loans.

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

The distribution of loans to borrowers of different incomes and businesses of different sizes is reasonable.

In evaluating the borrower distribution of home mortgage loans, we considered the number of households that live below the poverty level and the barriers that this may have on home ownership. It is especially difficult for the segment of the low-income population that lives below the poverty line to afford and maintain a home. This has an impact on the opportunity to lend to the low-income population of the community. Refer to the Description of Assessment Areas section for demographic information, including poverty rates.

Hillsdale Assessment Area

The overall borrower distribution of loans is reasonable in the Hillsdale AA. This is based on reasonable penetration of home mortgage loans among borrowers of different income levels, and excellent penetration of business loans among businesses of different sizes. Refer to Table 2a for the primary data used to assess the borrower distribution of home mortgage lending in the Hillsdale AA.

Table 2a Borrower Distribution of Home Mortgage Loans in Hillsdale 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	14.54	5.32	18.13	23.05	25.21	26.60	42.12	39.01
Home Improvement	14.54	11.11	18.13	17.17	25.21	25.25	42.12	41.41
Home Refinance	14.54	8.48	18.13	19.39	25.21	23.94	42.12	41.52

Source: data reported under HMDA; 2000 U.S. Census data

Income information was not reported for 6.0% of home purchase, 5.1% of home improvement and 6.7% of home refinance loans within the Hillsdale AA.

The distribution of home purchase loans reflects reasonable penetration among borrowers of different income levels. While the percentage of home purchase loans to low-income borrowers is significantly below the percentage of low-income families in the area, consideration is given to the impact that the area’s poverty level has on the opportunities to lend to the low-income segment of the community. The percentage of loans to moderate-income borrowers exceeds the percentage of moderate-income families in the AA.

The distribution of home improvement loans reflects reasonable penetration among borrowers of different income levels. While the percentage of loans to low-income borrowers is below the percentage of low-income families in the area, consideration is given to the impact that the area’s poverty level has on the opportunities to lend to the low-income segment of the community. The percentage of loans to moderate-income borrowers is near the percentages of moderate-income families in the area.

The distribution of home refinance loans reflects reasonable penetration among borrowers of different income levels. While the percentage of loans to low-income borrowers is significantly below the percentage of low-income families in the area, consideration is given to the impact that the area’s poverty level has on the opportunities to lend to the low-income segment of the community. The percentage of loans to moderate-income borrowers exceeds the percentage of moderate-income families in the AA.

The distribution of business loans reflects excellent penetration among businesses of different sizes. This is based on a sample of 39 loans, where all loans were made to businesses with gross annual revenues of less than \$1 million. According to Dun & Bradstreet business demographic data, 64 percent of area businesses have gross annual revenues less than or equal to \$1 million, although revenue data is not available for 29.5 percent of the AA’s businesses.

Jackson Assessment Area

The overall borrower distribution of loans is reasonable in the Jackson AA. This is based on reasonable penetration of home mortgage loans among borrowers of different

income levels, and excellent penetration of business loans among businesses of different sizes. Refer to Table 2b below for the primary data used to assess the borrower distribution of home mortgage lending in the Jackson AA.

Table 2b Borrower Distribution of Home Mortgage Loans in Jackson 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	18.84	5.45	19.71	33.17	24.42	21.29	37.03	33.66
Home Improvement	18.84	10.81	19.71	10.81	24.42	24.32	37.03	37.84
Home Refinance	18.84	5.88	19.71	17.06	24/42	20.59	37.03	46.47

Source: data reported under HMDA; 2000 U.S. Census data.

Income information was not reported for 6.4% of home purchase, 16.2% of home improvement and 10.0% of home refinance loans within the Jackson AA.

The distribution of home purchase loans reflects reasonable penetration among borrowers of different income levels. While the percentage of home purchase loans to low-income borrowers is significantly below the percentage of low-income families in the area, consideration is given to the impact that the area’s poverty level has on the opportunities to lend to the low-income segment of the community. The percentage of loans to moderate-income borrowers significantly exceeds the percentage of moderate-income families in the AA.

The distribution of home improvement loans reflects reasonable penetration among borrowers of different income levels. While the percentage of loans to low-income borrowers is well below the percentage of low-income families in the area, performance is good considering the impact that the area’s poverty level has on the opportunities to lend to the low-income segment of the community. The percentage of loans to moderate-income borrowers is well below the percentages of moderate-income families in the area.

The distribution of home refinance loans reflects reasonable penetration among borrowers of different income levels. While the percentage of loans to low-income borrowers is significantly below the percentage of low-income families in the area, consideration is given to the impact that the area’s poverty level has on the opportunities to lend to the low-income segment of the community. The percentage of loans to moderate-income borrowers is somewhat near the percentage of moderate-income families in the AA, reflecting good performance in this part of the community.

The distribution of business loans reflects excellent penetration among businesses of different sizes. This is based on a sample of 16 loans, where all loans were made to businesses with gross annual revenues of less than \$1 million. According to Dun & Bradstreet business demographic data, 65 percent of area businesses have gross annual revenues less than or equal to \$1 million, although revenue data is not available for 28.6 percent of the AA’s businesses.

Geographic Distribution of Loans

The geographic distribution of loans is reasonable. This conclusion is based on performance from the Jackson AA only. With no low- or moderate-income census tracts within the Hillsdale AA, a meaningful geographic distribution analyses could not be performed for that area.

Home Mortgage Lending – Jackson AA

In drawing conclusions, more weight is placed on moderate-income performance, as this segment of the community represents a significantly larger portion of the AA than the low-income segment. There is limited opportunity to lend in low-income areas as less than one percent of the area’s owner-occupied housing units are located in those portions of the AA. Refer to Table 3 below for the primary data used to assess the geographic distribution of home mortgage lending.

Census Tract Income Level	Low		Moderate		Middle		Upper	
	% 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	0.71	1.61	13.91	6.45	72.60	73.39	12.78	18.55
Home Improvement	0.71	7.32	13.91	19.51	72.60	58.54	12.78	14.63
Home Refinance	0.71	1.62	13.91	6.48	72.60	75.30	12.78	16.60

Source: data reported under HMDA; 2000 U.S. Census data.

The distribution of home purchase loans reflects a poor dispersion among geographies of different income levels. The percentage of loans made in low-income areas significantly exceeds the percentage of owner-occupied housing units in that segment of the community. However, the percentage of loans made in moderate-income areas is well below the percentage of owner-occupied housing units located in the moderate-income portions of the AA.

The distribution of home improvement loans reflects excellent dispersion among geographies of different income levels. In both low- and moderate-income geographies, the percentages of loans made significantly exceed the percentage of owner-occupied housing units within those segments of the community.

The distribution of home refinance loans reflects a poor dispersion of loans among geographies of different income levels. The percentage of loans made in low-income areas significantly exceeds the percentage of owner-occupied housing units in that segment of the community. However, the percentage of loans made in moderate-income areas is well below the percentage of owner-occupied housing units located in the moderate-income portions of the AA.

Business Lending – Jackson AA

The distribution of business loans among geographies of different income levels is reasonable, even though the percentages of loans in low-income and moderate-income areas are below the percentages of businesses located in those segments of the AA. This conclusion is based on a sample of 16 business loans. Refer to Table 4 below for the primary data used to assess the geographic distribution of business lending.

Table 4 - Geographic Distribution of Loans to Businesses in Jackson AA								
Census Tract Income Level	Low		Moderate		Middle		Upper	
Loan Type	% of AA Businesses /Farms	% of Number of Loans	% of AA Businesses/ Farms	% of Number of Loans	% of AA Businesses /Farms	% of Number of Loans	% of AA Businesses /Farms	% of Number of Loans
Business	9.11	6.25	16.13	12.50	66.19	81.25	8.47	0.00

Source: Loan sample; 2008 Dun & Bradstreet business data

Responses to Complaints

HCNB has not received any written complaints during the evaluation period regarding its performance meeting the credit and deposit needs of its AAs.

COMMUNITY DEVELOPMENT TEST

HCNB's community development (CD) performance demonstrates reasonable responsiveness to community development needs of the AAs through its record of CD lending, investments and services.

Number and Amount of Community Development Loans

HCNB originated eleven community development loans for \$9.4 million during the evaluation period. Seven loans were made to organizations whose purpose is to revitalize and stabilize low-income, moderate-income, and distressed middle-income geographies. The other four loans provide assistance to affordable housing programs and to purchase rental housing properties for low- and moderate-income families.

HCNB participates in several government-sponsored home loan programs for borrowers who do not typically qualify for credit under traditional loan programs. These programs address the needs of low- and moderate-income borrowers, individuals located in underserved areas, and first time homebuyers. Borrowers in each program must meet income eligibility requirements. Features include low or no down payment amounts, down payment or closing costs assistance, and flexible credit terms. As of December

30, 2008, the bank had 59 U.S. Department of Agriculture's Guaranteed Rural Housing Loans, 11 Single Family Mortgage Program Loans, through the Michigan State Housing Development Authority, and 45 loans through Freddie Mac's Home Possible 97 loan program.

HCNB participates in two programs to assist small businesses and economic development in the AA. The Michigan Economic Development Corporation's (MEDC) Capital Access Program (CAP) promotes economic business development and growth. This program combines public resources and bank financing to make loans to small businesses that might not normally be made under typical circumstances. As of December 31, 2008 the bank had 38 loans totaling \$2.9 million. Although this program was initially phased out by MEDC in 2002, it was reinstated in 2007 with HCNC being among the first six banks to provide loans under the revised program. In addition, HCNC participates in Small Business Administration Loan programs. As of December 31, 2008 the bank had made one loan.

Number and Amount of Qualified Investments

During the evaluation period HCNB purchased five municipal obligations totaling \$8.3 million. All five investments were to finance programs to revitalize and stabilize communities within the AA.

HCNB made 38 qualified donations totaling \$66 thousand to 35 organizations for community development purposes. All funds supported initiatives specifically targeted to benefit low- and moderate-income households, or to revitalize or stabilize low-income, moderate-income, and distressed middle-income tracts within the bank's AAs.

Extent to Which the Bank Provides Community Development Services

HCNB employees are actively involved with a variety of community organizations that conduct community development programs and initiatives for the local community. The organizations primarily provide social services for low- and moderate-income individuals.

Senior management is actively involved in 13 economic development organizations in Hillsdale, Jackson & Lenawee Counties to meet small business needs including start-up loans, rehabilitation and re-stabilization of central business districts, and offering assistance to existing businesses to expand or attract new businesses in the AA. In addition, HCNB participated in an entrepreneurship forum and provided financing information for individuals interested in starting their own businesses.

In support of affordable housing programs, the bank sponsored two luncheons in the community given to provide awareness of the MSHDA loan program to area realtors in Hillsdale and Adrian. Six bank employees participated in the luncheons with sixty-four realtors in attendance.

One of the bank's offices is located in a low-income part of the City of Jackson, and one branch is in a moderate-income section of the City of Jackson.

The bank has been active in offering Financial Literacy training on both its website and throughout its community. During the evaluation period, thirty-four bank employees gave twenty-one presentations about “Get Smart About Your Credit” at area high schools. As part of National Teach Children to Save Day, twenty-nine employees gave presentations to four elementary schools reaching 1,122 students covering ways to earn money, savings strategies, and safe places to keep money. In 2008, HCNB opened two in-school bank branches in elementary schools where students learn about money management and participate in age appropriate savings programs. Seventeen employees gave presentations to ten community organizations of Deter, Detect & Defend, the FTC identity theft awareness program. In addition, the bank added a Financial Education section to their website offering Teach Your Children About Money, Understanding and Using Credit, Savings and Budgeting, and Protecting Your Financial Identity. However, we cannot put any weight on these activities for CRA purposes as there is no data showing how this training serves primarily LMI families and individuals.

Responsiveness to Community Development Needs

HCNB's community development performance through its record of retail services, community development loans, qualified investments, and community development services demonstrates good responsiveness to community development needs in its AA.

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