



**SMALL BANK**

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Comptroller of the Currency  
Administrator of National Banks  
Washington, DC 20219

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## **PUBLIC DISCLOSURE**

**May 2, 2005**

# **COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION**

**NEIGHBORHOOD NATIONAL BANK  
Charter Number 22770**

**3511 National Avenue  
San Diego, CA 92113**

**Comptroller of the Currency  
Southern California South Field Office  
1925 Palomar Oaks Way Suite 202  
Carlsbad, CA 92008**

**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 “Outstanding.”**

The major factors that support this rating include the following:

- The average loan-to-deposit ratio of 86% is excellent.
- A majority percentage of loans and other lending-related activities occur within the bank's assessment area.
- The distribution of loans among businesses of different sizes in the assessment area is excellent.
- Geographic loan distribution reflects excellent dispersion throughout the assessment area.
- The bank has a high level of community development loans, investments, and services.
- There were no public complaints about the bank's CRA performance.

## **DESCRIPTION OF INSTITUTION**

Neighborhood National Bank (NNB) is a community bank headquartered in San Diego, California. Established in 1997, it is a designated Community Development Financial Institution (CDFI). As a CDFI, NNB promotes community development and revitalization in low- and moderate-income areas by providing access to credit and other financial services. NNB was the first CDFI to receive a national bank charter and has a goal of specifically addressing the financial services needs of under-served communities and low- and moderate-income persons.

NNB operates two branch offices and it is awaiting regulatory approval to open a third. The main office is located in the southeast area of the City of San Diego in a low-income census tract. In 1998 the bank opened a second branch in a middle-income tract of Paradise Valley, but closed that office in June 2001 for business-related reasons. During that same month, the bank opened a branch in nearby National City in a moderate-income tract. The bank plans to open a third branch in a middle-income tract of Spring Valley during mid-2005.

Neighborhood Bancorp owns 91.7% of NNB and the Federal National Mortgage Association (FNMA) owns 8.3%. Neighborhood Bancorp is located in National City, California. It receives investments from numerous organizations, businesses, and financial institutions. Its main purpose is capital allocation for NNB and its other holding company subsidiary, Neighborhood Capital Advisors (NCA). NCA provides investment capital for economic development projects and for micro-entrepreneurs. NCA also provides consulting services for other CDFIs in their applications for government grants and programs.

Neighborhood Bancorp and NNB also have a non-profit affiliate, Neighborhood Opportunities Corporation (NOC). NOC provides financial literacy and education working closely with NNB.

NNB offers a wide range of banking products. Loan products include commercial real estate and construction loans, Small Business Administration (SBA) loans, and a variety of personal and business loans and lines of credit. The bank assists with community access to mortgage loans through an arrangement with Nationwide Mortgage that among others includes "First Time Home Buyer" and "Credit Challenged" home loan programs. NNB's deposit products include interest bearing checking, savings, money market, and certificate of deposit accounts and personal and business checking accounts. The bank offers "Neighborhood Advantage" checking and savings accounts that require no minimum balance and no monthly service charge, and offers interest bearing checking accounts for non-profit organizations free of monthly service charges.

The bank operates an automated teller machine (ATM) at each branch location. They also operate an offsite ATM in a middle-income census tract in Paradise Valley and an ATM in an upper income tract in Mission Hills. Alternate delivery systems also include telephone banking, on-line banking, and courier services.

There are no legal or financial impediments to NNB's ability to meet the credit needs of its assessment area. As of December 31, 2004, the bank had total assets of \$79 million comprised of \$50 million in net loans, which represented 63% of total assets. The loan portfolio includes Small Business Administration, commercial, commercial real estate, and construction loans of approximately \$42 million, residential-secured loans of \$5 million, and non-residential consumer loans of \$3 million.

The bank received an "Outstanding" rating at its last CRA examination in December 1999.

## **DESCRIPTION OF ASSESSMENT AREA**

Neighborhood National Bank's assessment area meets the requirements of the regulation and does not arbitrarily exclude low- or moderate-income geographies. The area consists of 221 contiguous census tracts in southern San Diego County. Low-income census tracts comprise 19% of the area, 32% are moderate-income, 35% are middle-income, and 13% are upper-income tracts. The delineated area includes the cities of El Cajon, Chula Vista, Lemon Grove, and National City; the communities of Central San Diego, San Diego Mid-City, and Southeast San Diego, which are officially, designated sub-regions of the City of San Diego; and lastly the unincorporated communities of Rancho San Diego and Spring Valley.

San Diego County includes 4,261 square miles of urban and rural land and comprises the San Diego-Carlsbad-San Marcos Metropolitan Statistical Area, which is the southern-most major metropolitan area in California. Orange and Riverside counties border San Diego County to the north, by Imperial County to the east, by the Pacific Ocean to the west, and by Mexico to the south. The 2000 U.S. Census indicates a population of 2.8 million, a 13% increase over the 1990 Census. The San Diego Regional Planning Agency projects another 38% in population growth

over the next 20 years. The 2000 Census median housing value was \$229,602. The Department of Housing and Urban Development Housing reported 2004 median family income of \$62,400.

The most heavily populated areas are located along the coast where jobs are concentrated in the military, biotechnology, commercial, international trade, tourism, and professional services. The region's location on the Pacific Rim and proximity to the Mexican border has resulted in trade benefits for businesses seeking to take advantage of the North American Free Trade Agreement ("NAFTA"). The area unemployment rate of just under 4% in 2004, compares favorably to 5.5% for California and 6% for the nation.

San Diego is the largest city in the county with a population of approximately 1.3 million. It is also the second largest city in California and the sixth largest city in the country. The Milken Institute identified San Diego as the top-performing city in the state in terms of job, wage and salary growth, and high-tech output. Telecommunications, software, and biotechnology are the fastest growing industries.

Banking competition in the area is strong with numerous large, regional, and community banks and other financial service providers. NNB competes to some extent with other community banks in San Diego, but its focus on community development sets it apart from other competitors. The largest banks offering commercial and consumer financial products include Union Bank of California, Bank of America, and Wells Fargo. Often such large institutions have the advantages of brand recognition and marketing power over smaller local institutions.

In conjunction with this CRA examination, we contacted representatives from a community services organization to learn about credit opportunities within the community and how well financial institutions address identified credit and service needs. The contact identified affordable housing as a critical and ongoing need for ownership and for renters. The contact also identified the need for job training and employment opportunities for low- and moderate-income persons, and particularly for at-risk youth.

*Please refer to the bank's CRA public file for more information about the assessment area.*

## **CONCLUSIONS ABOUT PERFORMANCE CRITERIA**

### **LOAN-TO-DEPOSIT RATIO**

NNB's loan-to-deposit ratio is excellent given the bank's size, the credit needs of the assessment area, and the competitive banking market within the assessment area. The bank's ratio exceeds the standard for satisfactory performance.

We analyzed the bank's average quarterly loan-to-deposit ratio for the 21 quarters since the last CRA examination through December 2004. During this period, the bank's ratio averaged 86%. We compared the bank's ratio with that of peer banks in San Diego County that have similar demographics, asset size, and lending products. The average quarterly loan-to-deposit ratio for the peer group was 71%, compared to 86% for NNB. This peer group consists of 9 financial institutions, ranging in total asset size from \$39 million to \$169 million.

## **LENDING IN ASSESSMENT AREA**

A reasonable percentage of NNB's loans and other lending-related activities occur within its assessment area. The bank meets the standard for satisfactory performance.

For this analysis, we used bank-compiled data, which we tested for accuracy. The data included all loan originations during the evaluation period from January 2003 through December 2004. In order to meet the standard of performance for this criterion, a bank needs to originate at least 50% of the number of loans and 50% of the dollar volume within its defined assessment area. We found that NNB originated 70% of the number of loans and 68% of the dollar volume within its assessment area.

## **LENDING TO BORROWERS OF DIFFERENT INCOMES AND TO BUSINESSES OF DIFFERENT SIZES**

NNB's distribution of loans reflects excellent penetration among businesses of different sizes and exceeds the standard for satisfactory performance.

We focused our analysis on the bank's major loan product, which is commercial lending. We randomly sampled 28 commercial loans the bank originated in the assessment area during the evaluation period from January 2003 through December 2004. The original sample included 30 loans, but only 28 had reported income. We combined the data for both years to evaluate the bank's lending to businesses with revenues of different sizes as our analysis of demographic data showed no measurable differences between the comparison years of 2003 and 2004.

We compared the bank's pattern of lending to small businesses with the demographics of small businesses in the assessment area. Small businesses are those with gross revenues of \$1 million or less. The sample indicates that NNB granted 79% of the number of commercial loans and 79% of the dollar volume to small businesses. These percentages well exceed the area demographic, which shows that 66% of businesses in the area reported revenue as small businesses.

Table 1 below reflects the bank's lending patterns to businesses of different sizes based on our sample of commercial loans.

Table 1

| <b>Income Distribution of Loans to Businesses<br/>                     San Diego Assessment Area (AA)<br/>                     Years 2003 and 2004</b> |                     |                        |
|--|---------------------|------------------------|
| <b>Business Revenues (or Sales)</b>  | <b>≤\$1,000,000</b> | <b>&gt;\$1,000,000</b> |
| <b>% of AA Businesses*</b>   | <b>66%</b>          | <b>5%</b>              |
| % of Bank Loans in AA by #   | 79%                 | 21%                    |
| % of Bank Loans in AA by \$  | 79%                 | 21%                    |

\* Demographic Data Source: 2004 Dun & Bradstreet - 29% of AA businesses did not report revenue data.

The bank’s active involvement in SBA loan programs provides further support for its focus on lending to small business. A December 2004 SBA regional report ranked NNB twelfth out of 65 lenders for number of SBA loans generated in the San Diego area. NNB is a “Preferred SBA Lender,” a designation awarded to lenders with strong productivity and performance. Under this designation, the bank has partial delegation of authority and the SBA gives priority turn-around on the bank’s applications.

The bank originated 45 SBA loans totaling \$12 million during the period from January 2003 through March 2005. Of these loans, 36 loans (80%) totaling \$8 million (67%) were to business borrowers with gross annual revenues of \$1 million or less.

Based on the sample of loans reviewed, and other factors noted above, the bank exceeds the standard for this performance criterion.

## **GEOGRAPHIC DISTRIBUTION OF LOANS**

The geographic distribution of loans reflects excellent dispersion throughout the assessment area, and NNB exceeds the standard of satisfactory performance.

For this analysis, we used bank-compiled data of commercial loans originated in the assessment area between January 2003 and December 2004, which we tested for accuracy. The bank’s assessment area has 42 low-income tracts and 73 moderate-income tracts. NNB’s lending in low-income tracts significantly exceeds the demographics of the assessment area. Lending in moderate-income tracts is just slightly below the demographics.

Table 2 below reflects the bank's commercial lending activity within the assessment area by census tract type compared to the number of businesses those areas.

Table 2

| <b>Geographic Distribution of Loans to Businesses<br/> San Diego Assessment Area (AA)<br/> Years 2003 and 2004</b> |                               |                                |                               |                                |                               |                                |                               |                                |
|--|-------------------------------|--------------------------------|-------------------------------|--------------------------------|-------------------------------|--------------------------------|-------------------------------|--------------------------------|
| <b>Census Tract<br/> Income Level</b>  | <b>Low</b>                    |                                | <b>Moderate</b>               |                                | <b>Middle</b>                 |                                | <b>Upper</b>                  |                                |
|  | % of<br>Number<br>of<br>Loans | <b>% of AA<br/> Businesses</b> |
|  | 31%                           | <b>14%</b>                     | 35%                           | <b>40%</b>                     | 20%                           | <b>29%</b>                     | 14%                           | <b>16%</b>                     |

*Demographic Data Source: 2004 Dun & Bradstreet, 2000 U.S. Census Data*

The Bank Enterprise Award (BEA) Program adds support for the bank’s strong record of lending in low- and moderate-income tracts. The BEA Program provides financial incentives to increase lending, investment, and service activities within economically distressed communities. NNB received a total BEA award of \$4.5 million between 1999 through 2003. The funds were targeted for loans to small businesses with gross annual revenues equal to or less than \$1 million, commercial real estate loans, residential housing development projects, and home improvement loans. With the generation of these loans in the most distressed areas, the bank has provided housing units, helped to create or retain jobs, and revitalized areas with retail stores.

A recent program administered by the CDFI Fund is the New Market Tax Credit (NMTC) for small business loans and residential housing projects. Through NMTC, Neighborhood Bancorp received a \$5 million allocation of tax credits in 2003. Investors who buy a certain type of stock in Neighborhood Bancorp can receive a percentage of the tax credit allocation. The bank uses the capital raised from the investments to make loans to small businesses located in NMTC census tracts designated as distressed by the CDFI Fund. NNB’s NMTC-eligible loans from January 2003 through May 2004 totaled \$25 million.

Based on the bank’s lending performance and other innovative loan programs targeted to low- and moderate-income geographies, the geographic distribution exceeds the standard for satisfactory performance.

## **COMMUNITY DEVELOPMENT LOANS, INVESTMENTS AND SERVICES**

In addition to the lending criteria analyzed above, NNB has a strong record of community development loans, investments, and services as detailed below

## **COMMUNITY DEVELOPMENT (CD) LOANS**

The bank originated an excellent level of CD loans during the evaluation period.

- ❑ NNB has participated in loans with Bank of America in the Federal Home Loan Bank's Affordable Housing Program for the creation of housing units for low- and moderate-income individuals. During the evaluation period, the bank participated in four loans totaling \$2.7 million, which provided 399 affordable housing units.
- ❑ The bank originated 11 loans totaling \$1.9 million to non-profit organizations that provide community services or affordable housing targeted to low- and moderate-income individuals.
- ❑ The bank has an internal program, "Special Credit Opportunity Program Enterprise" (SCOPE), where consumer and business loans that are eligible for CDFI, BEA, and NMTC programs may receive a reduced interest rate, a higher loan to value ratio, a longer term, and a reduction of fees to process the loan. During the evaluation period, the bank granted \$14 million loans with SCOPE benefits, or 59% of the NMTC loan pool.

## **QUALIFIED COMMUNITY DEVELOPMENT INVESTMENTS**

The dollar volume of qualified CD investments is good given opportunities within the assessment area and the bank's capacity to address those needs.

The bank invested \$430,000, which represented 6.45% of Tier 1 capital. NNB invested \$400,000 of the total in other CDFIs located near and who benefited NNB's assessment area. The bank donated the remaining \$30,000 to community development organizations throughout its assessment area. These donations targeted organizations that provided affordable housing, economic development assistance to small businesses, and other community services targeted to low- and moderate-income persons.

## **COMMUNITY DEVELOPMENT SERVICES**

NNB's participation in CD services is good and enhances its record of serving the needs of its community.

Bank employees and directors extensively participate in services and activities that help low- and moderate-income individuals and help revitalize low- and moderate-income geographies. Below are some examples.

- ❑ Several bank employees provide technical assistance on financial matters to small businesses by lecturing on such topics as financing for start-up businesses and expansion for existing businesses.

- ❑ Since the last CRA examination, employees have given numerous lectures at workshops, college business fairs, and business forums. These outreach efforts educated low- and moderate-income individuals in the assessment area about small business lending and financing programs for women and underserved minorities.
- ❑ The CCO assisted with the formation of a San Diego-area community development corporation.
- ❑ A director serves as President and CEO of a multi-purpose non-profit business entity providing human services to low- and moderate-income families on both sides of the U.S.-Mexico border.
- ❑ A director serves as an executive for a social services agency in San Diego that provides education, employment, and affordable housing for underserved and disadvantaged minorities.
- ❑ A director serves as CEO for numerous non-profit public benefit corporations that provide job training and affordable housing to low- and moderate-income individuals.
- ❑ A bank director serves on the board of a charitable organization serving the homeless, teenagers in need, and AIDS patients.
- ❑ A director serves as President of a real estate development company, which he co-founded that specializes in affordable housing. The company has successfully developed over 1,200 housing units. This director also serves on numerous councils, task forces, and development corporations focusing on affordable housing.

## **RESPONSES TO COMPLAINTS**

There have not been any public complaints about the bank's CRA performance.

## **FAIR LENDING OR OTHER ILLEGAL CREDIT PRACTICES REVIEW**

We found no evidence of illegal discrimination or other illegal credit practices.