



SMALL BANK

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

PUBLIC DISCLOSURE

April 8, 2013

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

Heritage Bank, National Association
Charter Number 24977

2009 Browns Lane
Jonesboro, AR 72401

Office of the Comptroller of the Currency

Little Rock Field Office
1401 West Capitol Avenue, Suite 350, Little Rock, AR. 72201

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 major factors that support this rating include:

- Heritage Bank, National Association (Heritage) has a reasonable loan-to-deposit ratio.
- A majority of Heritage's primary loan products are within the assessment area.
- Heritage's overall borrower distribution for loans in the assessment area is reasonable.
- Heritage's overall geographic distribution of loans reflects reasonable dispersion.

SCOPE OF EXAMINATION

An onsite examination of the bank was performed to determine its performance under the Community Reinvestment Act (CRA). The bank was evaluated using Small Bank CRA criteria. The bank's primary loan products are residential real estate and commercial loans. Loan information used for this evaluation included Home Mortgage Disclosure Act (HMDA) data for the years 2010 through 2011 and a sample of forty commercial loans made in 2010 and 2011. A data integrity examination of the bank's 2010 through 2011 HMDA reports was performed prior to the CRA exam with no significant deficiencies noted. This performance evaluation covers the periods from May 31, 2005 to April 8, 2013.

DESCRIPTION OF INSTITUTION

Heritage Bank, National Association (Heritage) is a \$247 million dollar financial institution headquartered in Jonesboro, Arkansas with branches in Craighead and Mississippi counties. Jonesboro is located approximately 85 miles northwest of Memphis, Tennessee. Craighead County is designated as a Metropolitan Statistical Area (MSA) while Mississippi County is designated as a non-MSA county. The bank is 100% owned by First National Security Company, a two-bank holding company, located in Hot Springs, Arkansas. The holding company purchased the bank in December 2009, and the bank converted to a national charter on July 1, 2010.

The bank was formerly named Buffalo Island Bank with its headquarters located in Leachville, Arkansas. In December 1999, the bank changed its name and opened a new office building on Browns Lane in Jonesboro, Arkansas. It was at this time that the bank became a major presence in the Jonesboro banking community. The bank now has seven full service locations in Craighead County, five in Jonesboro and one each in the smaller towns of Monette and Caraway. There are also two full service branches in Mississippi County. One branch is in Leachville just east of the Craighead County line and one branch is in Manila, which is several miles south of Leachville.

The bank provides a wide array of services to the community. Financial products include numerous deposit accounts, loan products, and other traditional services. Hours of operation are accommodating to the community and the bank has Automated Teller Machines (ATMs)

machines at almost every location, with the exception of the branches in Monette and Caraway and the Caraway Road branch in Jonesboro. There are also two stand-alone ATM's in Jonesboro.

The bank's strategy is to provide financial products that meet the needs of the entire community. The bank's primary loan products are commercial and residential real estate loans. The table below presents the distribution of the bank's loan portfolio.

Loan Portfolio Composition as of December 31, 2012 (in 000s)		
Loan Type	Amount (000s)	Percent
Construction and Land Development	\$16,984	9.2%
Farmland	9,365	5.1
1-4 Family Residential	64,336	35.0
Multifamily (5 or more) Residential	7,527	4.1
Commercial (nonfarm, nonresidential)	48,911	26.6
Total Real Estate Loans	\$147,123	80.0%
Agriculture	6,543	3.6
Commercial and Industrial	22,156	12.0
Consumer and Other Loans	8,010	4.4
Total Gross Loans	\$183,832	100%

Source: Schedule RC-C: Call Report – December 31, 2012

There are no legal or financial circumstances that would prevent the bank from meeting the credit needs of its assessment area (AA). The bank's last CRA examination was performed by the FDIC as of May 31, 2005, and was rated **Satisfactory**.

DESCRIPTION OF ASSESSMENT AREA(S)

The bank's AA includes all of Craighead County Arkansas, along with one census tract located in Mississippi County, Arkansas. There are thirteen census tracts in Craighead County located in the Jonesboro MSA in their AA. According to the 2000 Census, there is one low-income, eleven middle-income, and two upper-income census tracts in the bank's AA. The AA delineation is in conformance with the CRA regulation. The AA includes only whole census tracts and does not arbitrarily exclude any low- or moderate-income areas.

The local economy is primarily health care, education, and agriculture based. Overall, economic conditions in Jonesboro appear to be improving relative to national trends primarily driven by health care and education. Based on July 2012 statistics provided by the Federal Reserve Board, the Jonesboro MSA had an unemployment rate of 7.6 percent, which is slightly above the state-

wide average of 7.4 percent. The bank’s AA is characterized by a high percentage of households that are in middle-income census tracts at 76 percent, followed by upper-income at 20 percent, and low-income at 4 percent. Banking competition is considered strong, with two locally chartered banks; numerous branches of other local, regional, and national banks; credit unions; finance companies; and mortgage companies throughout the assessment area.

One community contact was reviewed during the evaluation to obtain current information concerning the Jonesboro MSA. The contact indicated that the local economy appears to be more stable than that of many areas in the United States and that for the most part employment has remained stable. The contact indicated that credit has historically been an issue in the Jonesboro low- to moderate-income (LMI) areas, the supply of affordable housing stock is not adequate for low- to moderate-income residents, and noted an increase in the minority population, most significantly in Hispanic residents.

Demographic and Economic Characteristics Heritage Bank, National Association Assessment Area	
Population	
Total Persons	88,981
Number of Families	24,229
Number of Households	34,976
Geographies	
Number of Census Tracts/BNA	14
% Low-Income Census Tracts/BNA	7%
% Moderate-Income Census Tracts/BNA	0%
% Middle-Income Census Tracts/BNA	79%
% Upper-Income Census Tracts/BNA	14%
Median Family Income (MFI)	
Census MSA Median Family Income	\$38,379
HUD Updated MSA Median Family Income	\$50,729
Economic Indicators	
Unemployment Rate July 2012	7.6%
Median Housing Value	\$72,117
% of Households Below Poverty Level	16.3%

Source: 2000 U.S. Census data, Bureau of Labor Statistics

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Heritage’s performance under the lending test is satisfactory. The majority of the weight was placed on the bank’s reasonable loan-to-deposit ratio and lending in the assessment area. Heritage was found to have overall reasonable penetration among borrowers of different income levels and businesses of different sizes. Heritage’s overall geographical distribution of loans was also reasonable.

All criteria of the lending test are documented below.

Loan-to-Deposit Ratio

Heritage’s average loan-to-deposit ratio at 91.91 percent is reasonable given its size and assessment area’s credit needs.

The average loan-to-deposit (LTD) ratio was derived from a 30 quarter average taken from September 2005 to December 2012. For purposes of this analysis, two banks conducting business in the bank’s assessment area with similar asset sizes were used to determine the bank’s performance. These banks include Simmons First Bank of Northeast Arkansas and Farmers Bank and Trust Company, both of Jonesboro, Arkansas. The two institutions had an overall average LTD of 93.41 percent during the same quarters. These institutions had average LTDs ranging from a high of 95.44 percent to a low of 91.38 percent.

Loan-to-Deposit Ratio <i>30 Quarter Average from September 2005 to December 2012</i>		
Institution	Assets (as of 12/31/2012) \$ (000)	Average LTD Ratio
Heritage Bank, NA	\$256,534	91.91%
Simmons First Bank of Northeast Arkansas	\$351,257	95.44%
Farmers Bank and Trust Company	\$414,243	91.38%

Source: Uniform Banking Performance Reports (Call Reports)

Lending in Assessment Area

A majority of Heritage’s primary loan products were made inside its AA. The table below details the bank’s lending within the AA by number and dollar amount of loans. As indicated, approximately 82 percent of the loans were customers located in the bank's AA by number, and 83 percent by dollar volume.

Table 1 - Lending in AA (in 000s)										
Loan Type	Number of Loans					Dollars of Loans				
	Inside		Outside		Total	Inside		Outside		Total
	#	%	#	%		\$ (in 000s)	%	\$ (in 000s)	%	
Home Purchase	133	83.65	26	16.35	159	14,505	87.98	1,981	12.02	16,486
Home Improvement	30	75.00	10	25.00	40	1,562	81.69	350	18.31	1,912
Refinance	97	80.83	23	19.17	120	12,817	81.42	2,925	18.58	15,742
Commercial	34	85.00	6	15.00	40	6,161	74.47	2,112	25.53	8,273
Total	294	81.89	65	18.11	359	35,045	82.63	7,368	17.37	42,413

Source: 2010-2011 HMDA Data; Loan Sample

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

The overall borrower distribution for loans in the assessment area is reasonable. Although some areas of home lending reflect poor distribution, mitigating factors include higher cost of housing and poverty levels in the assessment area. An additional mitigating factor is the bank is concentrated in the Jonesboro MSA and only one census tract of low- and moderate-income borrowers is in this immediate area. Only 4 percent of households in the bank's AA are in low or moderate-income census tracts. It would not be reasonable to expect the bank to lend to a high proportion of borrowers outside of their immediate footprint.

Home Loans

Borrower distribution to low-income borrowers in the AA is poor for home purchase and refinance loans. The percentage of the number of loans to low-income borrowers is lower than the percentage of AA families. The bank's poor performance for home purchase and refinance loans to low-income borrowers is mitigated by a poverty level of 16 percent in the assessment area. This poverty level limits opportunities to qualify borrowers for home loan products. The bank's performance for home improvement loans is reasonable. The percentage of the number of loans to low-income borrowers is near to the percentage of AA families. Borrower distribution for residential real estate loans to moderate-income borrowers is reasonable. The percentage of home purchase, home improvement, and refinance loans to moderate-income borrowers is near to or only somewhat lower than the percentage of AA families.

The following table shows the distribution of home loans among borrowers of different income levels in the assessment area.

Table 2 - Borrower Distribution of Residential Real Estate Loans in AA										
Borrower Income Level	Low		Moderate		Middle		Upper		N/A	
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	% of AA Families	% of Number of Loans
Home Purchase	19.01	7.52	17.25	14.29	21.76	13.53	41.97	48.87	0.00	15.79
Home Improvement	19.01	16.67	17.25	10.00	21.76	13.33	41.97	36.67	0.00	23.33
Refinance	19.01	9.28	17.25	13.40	21.76	16.49	41.97	40.21	0.00	20.62

Source: 2010-2011 HMDA Data, 2000 U.S. Census Data

Business Loans

The distribution of loans to businesses reflects reasonable penetration among businesses of different sizes. Fifty-eight percent of the bank’s loans reviewed in the loan sample were made to small businesses. Small businesses are businesses with gross annual revenues of \$1 million dollars or less. These results indicate reasonable penetration compared to demographic data that shows 67 percent of the area’s businesses are considered small businesses. Because we lacked revenue data on 18 percent of loans made by the bank, we also looked at the distribution of loans by dollar amount. Loan size was used as a proxy for business revenue. The size threshold used was loans of \$250 thousand or less. We found that 85 percent of loans in our sample were loans equal to or less than \$250 thousand. This provides additional support for a reasonable distribution of loans to small businesses.

The following table shows the distribution of commercial loans among different sized businesses in the AA.

Table 2A - Borrower Distribution of Loans to Businesses in AA				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/Unknown	Total
% of AA Businesses	67.88	3.22	28.89	100%
% of Bank Loans in AA by #	57.50	25.00	17.50	100%
% of Bank Loans in AA by \$	24.97	35.59	39.44	100%

Source: Loan sample; Dunn and Bradstreet data

The table below shows the distribution of commercial loans in the AA by loan size, which was used as a proxy for business revenue.

Table 2B - Borrower Distribution of Loans to Businesses by Loan Size in AA				
Loan Size (000's)	Number of Loans	Percent of Number	Dollar Volume of Loans	Percent of Dollar Volume
\$0 - \$100,000	26	65.00%	\$895,589	13.12%
\$100,001 - \$250,000	8	20.00%	\$1,437,793	21.07%
\$250,001 - \$500,000	3	7.50%	\$1,148,683	16.83%
\$500,001 - \$1,000,000	1	2.50%	\$997,996	14.62%
Over \$1,000,000	2	5.00%	\$2,344,092	34.35%
Totals	40	100.00%	\$6,824,153	100.00%

Source: Loan sample

Geographic Distributions of Loans

Overall, geographic distribution of loans shows reasonable dispersion and reflects lending in census tracts of all income levels. Although some areas of the bank’s geographic distributions of residential real estate and business loans reflect poor dispersion, mitigating factors create an overall reasonable geographic distribution. Mitigating factors include a small volume of owner-occupied homes and businesses located in low- and moderate-income census tracts. The bank’s geographic distribution of residential real estate loans is reasonable while making up a majority of the bank’s loan portfolio.

Home Loans

Heritage’s geographic distribution of residential real estate loans reflects reasonable dispersion in the assessment area. Refinance loans at 2.06 percent reflects excellent geographic distribution based on the percentages of owner occupied housing units in low-and moderate-income census tracts. While there appears to be a concentration in middle and upper income levels, the bank has limited owner occupied housing as a percentage of the assessment area in low- and moderate-income levels. The assessment area only contains one low-income census tract, which is primarily occupied by Arkansas State University. The geographic distribution of home purchase loans at 0.75 percent is reasonable. The bank has made no home improvement loans in low- and moderate- income tracts, which reflects poor dispersion in the assessment area. This is mitigated by the low level of owner occupied housing in the total assessment area for low- and moderate- income census tracts at 0.96 percent.

Table 3 - Geographic Distribution of Residential Real Estate Loans in AA								
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	0.96	0.75	0.00	0.00	77.47	69.17	21.57	30.08
Home Improvement	0.96	0.00	0.00	0.00	77.47	86.67	21.57	13.33
Refinance	0.96	2.06	0.00	0.00	77.47	78.35	21.57	19.59

Source: 2010-2011 HMDA data; 2000 U.S. Census data.

Business Loans

Heritage’s geographic distribution of business loans is poor. As noted in the graph below, the bank has made no loans to businesses located in low- and moderate-income census tracts in the assessment area. Although there was poor dispersion, the bank had limited opportunities to lend as only 1.85 percent of businesses were included in the low and moderate-income census tracts.

Table 3A - Geographic Distribution of Loans to Businesses in AA								
Census Tract Income Level	Low		Moderate		Middle		Upper	
	% of AA	% of # of Loans	% of AA	% of # of Loans	% of AA	% of # of Loans	% of AA	% of # of Loans
Businesses	1.85	0.00	0.00	0.00	70.74	60.00	27.40	40.00

Source: 2000 Census Data, Loan Sample

Responses to Complaints

The bank has not received any CRA related complaints since its last CRE examination on May 31, 2005.

Fair Lending or Other Illegal Credit Practices Review

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