



## **PUBLIC DISCLOSURE**

**March 29, 1999**

# **COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION**

**Northern National Bank  
Charter Number 23450  
25 Smiley Road North  
Nisswa, Minnesota 56468**

**Office of the Comptroller of the Currency  
Minneapolis Field Office  
920 Second Avenue South, Suite 800  
Minneapolis, Minnesota 55402**

**NOTE: 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.**

## GENERAL INFORMATION

*The Community Reinvestment Act (CRA) requires each federal financial supervisory agency to use its authority when examining financial institutions subject to its supervision, to assess the 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. Upon conclusion of such examination, the agency must prepare a written evaluation of the institution's record of meeting the credit needs of its community.*

*This document is an evaluation of the Community Reinvestment Act (CRA) performance of **Northern National Bank** prepared by **The Office of the Comptroller of the Currency (OCC)**, the institution's supervisory agency, as of **March 29, 1999**. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 C. F. R. § Part 25.*

**INSTITUTION'S CRA RATING:** This institution is rated Needs to Improve.

Northern National Bank's distribution of residential real estate loans reflects poor penetration among individuals of different income levels, particularly low- and moderate-income borrowers, relative to assessment area demographics. The bank's minimal residential real estate lending to low- and moderate-income families cannot be fully justified by the high median housing values within the assessment area, the difference in the distribution of families by income in the geographies in close proximity to the bank, or the temporary prohibition to establish offices in other segments of the assessment area which have a slightly higher concentration of low- and moderate-income families. The bank's performance was weighted the most heavily to residential real estate lending as this product comprises the largest share of dollars outstanding. Although the bank's residential real estate loan distribution to borrowers living in moderate-income geographies appears reasonable, this distribution also benefits from the bank's high concentration of loans to middle- and upper-income borrowers. The distribution of commercial loans to businesses of different revenue sizes reflects the assessment area demographics. The bank originates a substantial number of its loans within the assessment area. The loan-to-deposit ratio is more than reasonable compared to the average ratios of other local banks.

## **DESCRIPTION OF INSTITUTION:**

Northern National Bank (Northern) is a \$29 million institution with a main office and two full service branch offices located in central Minnesota. Northern's main office and one of its two branch offices are located in the city of Nisswa. Northern's other branch office is located in the city of Crosslake which is approximately 20 miles northeast of Nisswa. The main office and both branch offices have automated teller machines onsite which are operated by the bank.

Northern's primary loan product lines are residential real estate and commercial loans, comprising 58% and 37% of total loan originations by dollar and 31% and 33% by number, respectively. Of the residential real estate loan originations, 3% by dollar and 8% by number consisted of construction or junior lien loans. Consumer instalment loans are not a major product line at 5% of total originations by dollar and 27% by number. Northern's loan portfolio represents 80% of total assets as of December 31, 1998.

Northern is owned by Anderson Financial Group, Inc., a one-bank holding company located in Golden Valley, Minnesota. The bank has no subsidiaries. This is Northern's first CRA evaluation since its opening in October 1997. Northern is not subject to any legal or financial factors which would impede its ability to help meet the credit needs of its assessment area. However, the holding company is prohibited by a 3-year non-compete agreement to establish offices in several segments of the assessment area, most notably large population centers.

## **DESCRIPTION OF NORTHERN NATIONAL BANK'S ASSESSMENT AREA:**

Northern's assessment area consists of all of Crow Wing County and five adjacent block numbering areas (BNAs) in southern Cass County. The population of the assessment area is approximately 56,000. Nisswa's 1994 estimated population was 1,500 according to a community profile provided by the Nisswa Chamber of Commerce and Crosslake's estimated population is 1,000.

The assessment area is not located within a Metropolitan Statistical Area (MSA). Therefore, the 1998 statewide non-MSA median family income of \$40,500 is used for comparative purposes. Per 1990 census data, approximately 15,500 families reside within the assessment area, 12% of which report family incomes below the poverty level. The distribution of assessment area families by income level is shown in the following table.

<b>Income Level of Family</b>	<b>Percentage of Total Families</b>
Low-Income (\$0 - \$20,250)	23%
Moderate-Income (\$20,250 - \$32,400)	20%
Middle-Income (\$32,400 - \$48,600)	23%
Upper-Income (Greater than \$48,600)	34%

Northern's assessment area is divided into 21 BNAs. Northern's offices are located in

middle-income BNAs (#9503 and #9505). The moderate-income BNAs are located to the north and northwest of the bank's offices. The upper-income BNA is located south of Nisswa in the Baxter area. The assessment area meets the requirements of the regulation and does not arbitrarily exclude low- or moderate-income geographies. The distribution of BNAs by income level is represented in the following table.

<b>Income Level of BNA</b>	<b>Proportion of Total BNAs</b>
Moderate-Income	24% (5/21)
Middle-Income	71% (15/21)
Upper-Income	5% (1/21)

The vacancy rate for the assessment area's 38,700 housing units is high at 45%. This high rate is due in part to the substantial number of seasonal vacation homes. By comparison, owner- and rental-occupied housing units compose 43% and 12% of total housing units, respectively. The median housing value of the assessment area is \$58,500.

The characteristics of the two BNAs that include the bank's offices include higher vacancy rates and higher median housing values than the aggregate assessment area. The vacancy rate for this segment is 67%. The median housing value for BNA #9505 which includes the city of Nisswa is \$72,000 while BNA #9503 which includes the city of Crosslake is \$89,700.

Recent community contacts indicate the local economy is strong and expanding. Employment is centered in the retail and service sector, with tourism significantly contributing to the local economy and employment base. Lending competition is strong with offices of several other banks, credit unions, and finance companies located within the assessment area. During this evaluation, a bank examiner met with a real estate broker to further ascertain local economic conditions and community credit needs. This interview along with other recent community contacts suggests that credit needs include affordable housing, first-time home buyer assistance, small business, and general consumer loans. In two community contacts' opinion, there is a shortage of affordable homes in the \$80,000 range in the Nisswa area.

## **CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA:**

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

To assess performance under this criteria, examiners selected a judgmental sample of 45 residential real estate loans totaling \$5.4 million, representing 68% of the dollar volume of the portfolio and 53% by number. These loans were originated since October 1997 and were for the purpose of purchasing or refinancing the borrowers' primary or secondary residence. The commercial loan sample consisted of 22 relationships totaling \$3 million, representing 30% of the dollar volume of the portfolio and 60% by number. These two loan types were selected because they are the bank's primary product lines based on the dollar volume of loans originated during 1998.

### Residential Real Estate Loans

Northern National Bank's distribution of residential real estate loans reflects poor penetration among individuals of different income levels, particularly low- and moderate-income borrowers, relative to assessment area demographics. The bank's minimal residential real estate lending to low- and moderate-income families cannot be fully justified by the high median housing values within the assessment area, the difference in the distribution of families by income in the geographies in close proximity to the bank, or the temporary prohibition to establish offices in other segments of the assessment area which have a higher concentration of low- and moderate-income families. Although a greater concentration of low- and moderate-income families reside in BNAs not in close proximity to the bank's offices including areas in which Northern is prohibited from opening a branch location until expiration of a noncompete agreement in November 2000, the two BNAs containing the bank's main and branch offices contain a distribution of families of 13% low-, 17% moderate-, 33% middle-, and 37% upper-income with only 5% reporting incomes below the poverty level.

<b>Distribution of Residential Real Estate Loans by Borrower Income Level</b>			
<b>Income Level</b>	<b>Families Within Each Income Level</b>	<b>Number of Loans Originated</b>	<b>Dollar Volume of Loans Originated</b>
Low	23%	2%	1%
Moderate	20%	2%	1%
Middle	23%	20%	13%
Upper	34%	76%	85%

### Commercial Lending

The bank's distribution of loans to businesses of different sizes reasonably compares to, but does not meet, the demographics of the assessment area. As shown in the table below, the majority of Northern's commercial loans were originated to businesses reporting less than \$500,000 in annual revenues. Additional information not illustrated in the table due to the lack of comparative demographic data reveals that the bank originated 45% of its commercial loans to businesses reporting less than \$250,000 in annual revenues.

<b>Annual Revenues (000s)</b>	<b>Percent of Businesses in the Assessment Area</b>	<b>Percent of Loan Originations by Number</b>	<b>Percent of Loan Originations by Dollar</b>
Less than \$500	87%	64%	65%
\$500 - \$1,000	6%	18%	6%
Greater than \$1,000	7%	18%	29%

### ***Geographic Distribution of Loans***

Using the sample of loans previously described, examiners evaluated the distribution of loans

throughout the assessment area based on the income level of the BNA.

### Residential Real Estate Lending

Although Northern's distribution appears to reflect reasonable dispersion of residential real estate loans to borrowers residing in moderate-income BNAs, the bank's lending in moderate- and middle-income BNAs is concentrated among upper-income borrowers. The following table compares the distribution of the bank's residential real estate lending activity to BNA demographic statistics. The second table provides additional information on the distribution of the bank's lending to borrowers by income within the moderate-, middle-, and upper-income BNAs.

Income Level of BNAs	Demographic Data from 1990 U.S. Census of Assessment Area		Bank's Residential Real Estate Loan Distribution	
	Percent of Families	Percent of Owner-Occupied Housing Units	Percent of Loans by Dollar	Percent of Loans by Number
Moderate-Income	17%	19%	28%	25%
Middle-Income	72%	72%	69%	71%
Upper-Income	11%	9%	3%	4%

<b><i>Residential Real Estate Loan Distribution by BNA and Borrower Income</i></b> <b><i>Based on Income Designation and by Number of Loans</i></b>					
<b><i>BNA Income Level</i></b>	<b><i>Borrower Income</i></b>				<b><i>Total</i></b>
	<b><i>Low</i></b>	<b><i>Moderate</i></b>	<b><i>Middle</i></b>	<b><i>Upper</i></b>	
<b><i>Moderate</i></b>	<b><i>2%</i></b>	<b><i>0%</i></b>	<b><i>7%</i></b>	<b><i>16%</i></b>	<b><i>25%</i></b>
<b><i>Middle</i></b>	<b><i>0%</i></b>	<b><i>2%</i></b>	<b><i>13%</i></b>	<b><i>56%</i></b>	<b><i>71%</i></b>
<b><i>Upper</i></b>	<b><i>0%</i></b>	<b><i>0%</i></b>	<b><i>0%</i></b>	<b><i>4%</i></b>	<b><i>4%</i></b>
<b><i>Total</i></b>	<b><i>2%</i></b>	<b><i>2%</i></b>	<b><i>20%</i></b>	<b><i>76%</i></b>	<b><i>100%</i></b>

### Commercial Lending

The bank's distribution of loans to businesses within the assessment area is reasonable given the overall location of businesses. The concentration of loans to businesses located in middle-income BNAs is reasonable as approximately 50% of the bank's lending by dollar and number is to businesses located in the two middle-income BNAs that the bank maintains offices. The following table compares commercial lending activity in BNAs with different income levels to the distribution of businesses throughout the assessment area.

<b>Income Level of BNAs</b>	<b>Percent of Businesses located in BNA</b>	<b>Percent of Loans by Number</b>	<b>Percent of Loans by Dollar</b>
Moderate-Income	18%	9%	15%
Middle-Income	69%	86%	84%
Upper-Income	13%	5%	1%

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

The bank's loan-to-deposit ratio of 98%, as of December 31, 1998, exceeds all but one of the eight banks within Northern's assessment area. These local community banks range in total asset size from \$35 million to \$185 million. The bank's quarterly loan-to-deposit ratio since opening in October 1997 has averaged approximately 92%. Northern's average quarterly loan-to-deposit ratio during this period also ranks second out of the eight banks, which showed a range from 49% to 104%.

In addition, Northern has sold 53 residential real estate loans totaling \$7.6 million through the secondary market since opening in October 1997. While these activities assist in Northern's efforts to meet local credit needs, the volume of sold loans is not reflected in the quarterly loan-to-deposit ratio. Information from a community contact indicates that the availability of secondary market loans is sufficient.

### ***Lending in Assessment Area***

The bank originates a substantial majority of its loans to borrowers and businesses located inside of its assessment area. National bank examiners reviewed and verified the accuracy of bank-generated reports to determine Northern's volume of lending in its assessment area. These reports included all types of loans originated since the bank opened which still have an outstanding balance and were found to be accurate. The reports showed that 95% by dollar and 89% by number of all loans were originated within the assessment area.

### ***Compliance with Antidiscrimination Laws***

Examiners did not identify any violations of substantive provisions of antidiscrimination laws and regulations. Examiners conducted a comparative file review of consumer loan applications received in 1998. This review compared the underwriting standards applied to five denied female consumer loan applicants to twenty-four approved male loan applicants. Based on this review, examiners did not identify any denied applicants with comparable credit worthiness to approved applicants.

### ***Response to Complaints***

The Northern National Bank has not received any CRA complaints.