

# **PUBLIC DISCLOSURE**

**May 5, 2004**

## **COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION**

**The Smith County State Bank & Trust Company  
9664**

**136 S. Main Street  
P.O. Box 307  
Smith Center, Kansas 66967-0307**

**Federal Deposit Insurance Corporation  
2345 Grand Boulevard, Suite 1200  
Kansas City, Missouri 64108**

**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.

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## 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 **The Smith County State Bank & Trust Company, Smith Center, Kansas**, prepared by the **Federal Deposit Insurance Corporation**, the institution's supervisory agency, as of **May 5, 2004**. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 CFR Part 345.*

## INSTITUTION RATING

***INSTITUTION'S CRA RATING:*** This institution is rated Satisfactory.

The Smith County State Bank & Trust's CRA performance depicts a satisfactory record of helping meet the credit needs of its assessment area. The following supports this rating:

- The bank's average net loan-to-deposit ratio of 45 percent demonstrates a reasonable level of effort to make loans considering the area demographics and the level of strong competition among area lending institutions.
- An analysis of agricultural loans, the bank's primary lending focus, indicates a substantial majority of the bank's loans have been extended to farmers located within the assessment area, which reflects the bank's commitment to its assessment area.
- The review of agricultural loans revealed the bank's lending to farms of varying sizes is reasonable considering the demographic composition of the bank's assessment area.
- The bank's agricultural loans are adequately disbursed throughout its assessment area, with no unusual lending gaps identified.
- There have been no CRA-related complaints since the prior evaluation dated September 27, 1999.

## DESCRIPTION OF INSTITUTION

The Smith County State Bank & Trust (SCSB&T) is a full-service community bank with its main office located in Smith Center, Kansas, and a branch office in Lebanon, Kansas. Smith Center is centrally located in Smith County while Lebanon is centrally located in the eastern portion of the county approximately 15 miles to the east of Smith Center, Kansas. Smith Center is also the county seat for Smith County. The bank operates a cash dispensing automated teller machine in Smith Center, Kansas.

The bank's December 31, 2004, Report of Condition reflected total assets of \$62,932,000, gross loans of \$24,521,000, and total deposits of \$55,685,000. Gross loans represented approximately 39 percent of the bank's total assets and 44 percent of its total deposits. The bank was rated "Satisfactory" at the previous evaluation dated September 27, 1999. A comparison of financial information from the September 30, 1999, Report of Condition to the December 31, 2003, Report of Condition, reveals the bank has experienced some growth in net loans (16 percent), total assets (8 percent) and total deposits (11 percent) since the prior evaluation.

SCSB&T offers standard loan and deposit products. The bank's loan products include agricultural, commercial, residential real estate, and consumer loans. The loan products offered are considered capable of helping to meet the assessment area's credit needs. The bank offers government guaranteed loan products to small farm operations through the Farm Service Agency (FSA). The bank's loan portfolio currently includes 29 FSA loans, 23 of which have been originated since the previous evaluation. According to bank officials, SCSB&T's lending is focused on agricultural-related loans, as reflected in Table 1 below.

<b>Table 1: Distribution of Bank's Loans as of December 31, 2003</b>		
<b>Loan Type</b>	<b>Dollar Volume of Loans (000s)</b>	<b>Percent of Total Loans (rounded)</b>
Loans secured by farmland (including farm residential and other improvements)	\$7,150	29%
Revolving, open-end loans secured by 1-4 family residential properties and extended under lines of credit	\$12	0%
Closed-end loans secured by 1-4 family residential properties (first liens)	\$4,151	17%
Loans secured by non-farm nonresidential properties	\$648	3%
Loans to finance agricultural production and other loans to farmers	\$8,137	33%
Commercial and industrial loans	\$2,356	10%
Other consumer loans – (includes single payment, installment, and all student loans)	\$2,050	8%
Obligations (other than securities and leases) of states and political subdivisions in the U.S.	\$17	0%
<b>GROSS LOANS</b>	<b>\$24,521</b>	<b>100%</b>

Source: December 31, 2003 Report of Condition

Affiliates of the bank include Smith County State Bank and Trust Company Charitable Trust, a subsidiary formed for the purpose of funding discretionary economic development and community improvement projects that might not otherwise receive funding. The charitable trust distributes \$10,000 to \$12,000 annually, and has funded such community improvement efforts and quality of life projects as the community movie theater, the library for computer equipment, the construction of the veterans memorial, the local golf courses, the Harlan park project, the grade school playground, and various block signs and street banners. Smith Center, Inc., (SCI) a jointly owned venture with First National Bank, Smith Center, Kansas, was established to promote the local business infrastructure. Its current project involves the purchase of a building which was then leased back to a local business. SCI and the two financial institutions have been subsidizing the project. This business has created at least two new jobs and provides significant economic activity for community. No legal or financial impediments exist which would prohibit the bank from helping to meet the credit needs of its assessment area.

## DESCRIPTION OF ASSESSMENT AREA

The Community Reinvestment Act (CRA) requires financial institutions to identify one or more “assessment area(s)” within which the appropriate regulatory agency will evaluate the bank’s CRA performance. Typically, an institution’s assessment area will include the towns, cities, counties, or other political subdivisions in which its offices are located and a substantial portion of its loans are made. Assessment areas must consist of one or more “census tracts (CTs)”, which are statistical subdivisions of a county. The assessment area may not reflect illegal discrimination or arbitrarily exclude low- or moderate-income geographies.

Each CT is also designated as low, moderate, middle, or upper income based on the following definitions in relation to the 2000 Census Bureau non-metropolitan median family income figure of \$42,116 for the State of Kansas.

<u>Designation</u>	<u>Percent of the Area Median Family Income</u>	<u>Income Range</u>
<i>Low-income</i>	<i>Less than 50 percent</i>	<i>&lt;\$21,058</i>
<i>Moderate-income</i>	<i>At least 50 percent but less than 80 percent</i>	<i>\$21,058 to &lt;\$33,693</i>
<i>Middle-income</i>	<i>At least 80 percent and less than 120 percent</i>	<i>\$33,693 to &lt;\$50,539</i>
<i>Upper-income</i>	<i>120 percent or more</i>	<i>\$50,539 or more</i>

The bank’s assessment area consists of Smith County, which is located in north central Kansas. Smith County is bordered on the east, south, and west by four Kansas counties, and on the north by two Nebraska counties. The assessment area is divided into two middle-income CTs (9758 and 9759). This represents a change from the prior evaluation when the assessment area consisted of two moderate-income and one middle-income block numbering areas. Prior to the 2000 Census, rural geographies were referred to as block numbering areas rather than CTs.

The bank’s main office in Smith Center, Kansas, is located in CT 9758. The bank’s branch office in Lebanon, Kansas, is located in CT 9759. Additional towns located in CT 9759 include Athol, Cedar, Gaylord, and Kensington. Data from the 2000 Census shows the total population for the bank’s assessment area at 4,536 representing a decrease of 10.7 percent since the 1990 Census, compared to an 8.5 percent increase for Kansas overall. Based on this information, Smith County was ranked as the ninth county with the fastest declining population in the State of Kansas. Current Census information also reveals that while only 13 percent of the population in the State of Kansas is 65 years old or older, 28 percent of the population in the assessment area is in this age group. Additionally, Smith County was ranked first in the State of Kansas and fourth

in the United States as the oldest county with 5.5 percent of the county's population 85 years old or older. Additionally, approximately 22 percent of the population of the assessment area is under the age of 18. These findings indicate that 50 percent of the population in the assessment area either cannot borrow or may not have the need to borrow. A local community member stated that while the population of the city of Smith Center actually increased in 2003, overall the population in Smith County continues to decline. Bank officials indicated that the biggest migration continues to be in the college age group. The assessment area just doesn't have the higher paying jobs or positions to draw them back to the area. Data from the 2000 census showed that the 25 to 34 age group decreased 41 percent from 1990.

According to 2000 Census data, the assessment area has 1,336 families, of which 21 percent are low-income, 25 percent are moderate-income, 24 percent are middle-income, and 30 percent are upper-income. Approximately 9 percent of families live below the poverty level.

Housing data from the 2000 Census shows that the assessment area has 2,326 housing units. Approximately 67 percent of the housing units are owner occupied, 17 percent rental occupied, and 16 percent are vacant. The median age of homes is 55 years, and the median housing value is \$41,306. Bank officials indicated the local residential real estate market is considered stable.

The assessment area is predominately rural with agriculture considered the driving force in the community. The major grain products are wheat, milo, corn, soy beans, sunflowers, and hay. Livestock also continues to be an important part of the local agriculture economy. There is also some light manufacturing which offers some diversity to SCSB&T's assessment area. Bank officials believe that the current economy is stable; however, it is showing some signs of stress mainly due to the agriculture sector. Bank officials described the current agricultural real estate market as stable to strong.

Demographic data from the 1997 Agricultural Census for the farms in Smith County reveals that a large percentage of farmers have off-farm employment (approximately 33 percent of all farmers in this county stated that farming is not their principal occupation). Additionally, 35 percent of the farmers in the assessment area do not borrow to support their agricultural operations. The average sales per farm in Smith County total \$51,974. This information is referenced later in the evaluation in the section discussing the bank's record of lending to different size farm operations.

Competition for loans and deposits is relatively strong from the one national bank headquartered in the assessment area, the two branch offices of national banks chartered outside the assessment area, and several other financial service entities that operate offices and extend credit in the assessment area. Bank officials stated some of the strongest competition for loans is currently coming from nontraditional funding sources, such as implement dealers, seed companies, and chemical companies.

## CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

The CRA rating for a small bank is based on five performance tests, four of which are related to the bank's lending performance. The fifth criterion is related to the bank's response to CRA-related complaints. A small bank is defined by the CRA regulation as having total assets of less than \$250 million.

### **1. Loan-to-Deposit Ratio**

SCSB&T's average net loan-to-deposit ratio since the previous CRA evaluation is reasonable and indicates the bank is willing to extend loans. Since the previous evaluation, the net loan-to-deposit ratio averaged 45 percent as reflected in the 18 quarterly Reports of Condition for September 30, 1999, through December 31, 2003, up from an average of 41 percent at the previous evaluation.

There are three other financial institutions located in the bank's assessment area that can be considered similar<sup>1</sup>; however, only one of those institutions is headquartered in the assessment area. Table 2 reflects selected information about these institutions compared to SCSB&T. For the same period (18 quarters, September 30, 1999, through December 31, 2003), the average net loan-to-deposit ratios ranged between 45 percent and 68 percent for the similarly situated institutions.

<b>Table 2: Comparison of Similarly Situated Banks</b>			
<b>Bank name and location</b>	<b>County</b>	<b>Total Assets December 31, 2003 (000s)</b>	<b>Average Net Loan to Deposit Ratio (Rounded)</b>
The Farmers National Bank Osborne, Kansas Branches: Gaylord, Kansas                      9759	Osborne	\$40,304	59%
The Farmers National Bank Phillipsburg, Kansas Branches: Agra, Kansas Kensington, Kansas                      9759 Logan, Kansas	Phillips	\$68,048	68%
The First National Bank of Smith Center, Kansas                      9758	Smith	\$37,831	49%
The Smith County State Bank & Trust Smith, Kansas                      9758 Branches: Lebanon, Kansas                      9759	Smith	\$62,932	45%

Source: December 31, 2003 Report of Condition

Although both of the bank's located in Smith Center have lower net loan-to-deposit ratios than the other similarly situated banks, SCSB&T has maintained a loan-to-deposit ratio that is

<sup>1</sup> A similar financial institution, for these purposes, is located in or near the bank's assessment area, has a similar structure, offers similar products, has a similar loan portfolio composition, serves a similar customer base, and has similar resources (total assets).

considered reasonable given the institution's size, financial condition, assessment area credit needs, and age of population.

## **Loan Sampling**

According to the loan portfolio composition and bank management, the primary lending focus is agricultural lending. A sample of outstanding agricultural loans (real estate secured and operating) originated and renewed during the previous six months (August 5, 2003, through February 5, 2004) were reviewed in order to evaluate the bank's lending performance under the next three criteria. The universe of agricultural loans included 123 loans totaling \$6,488,231. A sample of 32 agricultural loans totaling \$2,150,406 was reviewed, and represents a statistical sample based on a 90 percent confidence interval with a 15 percent precision level.

## **2. Lending in the Assessment Area**

SCSB&T exhibits an overall high level of lending within the assessment area, reflecting management's strong commitment to providing credit within the assessment area. The analysis of agricultural loans indicates that the bank originates a substantial majority of these types of loans within the assessment area. Of the 32 agricultural loans reviewed, 29 (91 percent) totaling \$1,815,406 (84 percent) were extended to farm operations located within the assessment area, indicating management's strong commitment to helping to meet the credit needs of the assessment area.

## **3. Lending to Farmers and Businesses of Different Sizes and Borrowers of Various Income Levels**

### **Agricultural Lending**

SCSB&T's record of lending to farmers of different sizes is considered reasonable, as reflected in Table 3 on the following page. This conclusion was based on the results derived from the analysis of the agricultural loan sample. For this analysis, the sampled agricultural loans extended within the assessment area were categorized into different size operations according to the annual gross revenue generated by the farming operation. Table 3 summarizes the agricultural loan sample distribution to farmers of different sizes.

<b>Gross Revenues</b>	<b>Number of Loans</b>	<b>Percent of Total Number (rounded)</b>	<b>Dollar Volume of Loans</b>	<b>Percent of Total Dollar Volume (rounded)</b>	<b>Farms in Assessment Area* (rounded)</b>
\$0 to \$49,999	8	28%	\$141,706	8%	55%**
\$50,000 to \$99,999	8	28%	\$512,200	28%	19%
\$100,000 to \$249,999	6	20%	\$373,000	21%	18%
\$250,000 to \$499,999	3	10%	\$300,000	16%	6%
\$500,000 and Greater	4	14%	\$488,500	27%	2%
<b>Totals</b>	<b>29</b>	<b>100%</b>	<b>\$1,815,406</b>	<b>100%</b>	<b>100%</b>

Source: Bank records and \* 1997 Census of Agriculture for farms located in Smith County. \*\*This figure is only 40 percent if the non-borrowing farms with less than \$10,000 in annual sales volume are excluded. Also, 23 percent of all farms in the assessment area reported gross revenues of under \$10,000.

As reflected in the tables above, the bank is lending to farms of different sizes, including the small farm operations. This is evidenced by the fact that 56 percent of the number of loans were extended to farm operations having less than \$100,000 in gross revenues. The bank's lending to farmers in the lowest gross annual sales category (28 percent by number and 8 percent by dollar volume) indicates a willingness to lend to the smallest of farms, when compared to the number of farms in the assessment area in that category (55 percent). This is more evident when hobby farms<sup>2</sup> are excluded, leaving only 40 percent of the farms in the assessment area in the lowest sales category, further supporting a good record of lending to the smallest of farms.

Additionally, when reviewing the bank's agricultural lending, there are several other factors that should also be considered. The first factor to consider is that many farmers in the assessment area do not borrow to support their operations. According to the 1997 Agricultural Census 35 percent of the farmers in Smith County did not report any interest expense (i.e. non-borrowing farmers). In the State of Kansas, 93 percent of the non-borrowing farmers reported revenues of less than \$100,000 per year. Therefore, the bank does not have the opportunity to lend to all small farmers. A second factor to consider in evaluating the bank's record of lending to farms of all sizes is the fact that many local operators appear to be "hobby farmers." For instance, 33 percent of all farmers in Smith County indicated that "farming" is not their principal occupation. Additionally, 23 percent of all farmers in Smith County reported gross farm revenues of less than \$10,000 per year. These small farmers typically have lower borrowing needs than large farmers and often do not require traditional bank financing. In view of these additional factors, the bank's record of lending to farm operations of different sizes, including small and medium-sized farms, is considered reasonable.

#### **4. Geographic Distribution of Loans**

A brief analysis of the geographic distribution of agricultural loans was conducted. The bank's assessment area consists of two census tracts that are classified as middle-income according to

<sup>2</sup> Hobby farms are defined as non-borrowing farms with less than \$10,000 in annual sales volume.

the 2000 Census. A geographic distribution analysis of the bank's lending activity within geographies of varying income levels has limited meaning in this evaluation because the entire area is considered homogeneous with regard to income levels. However, examiner review of those loans originated in the assessment area revealed an acceptable distribution of loans throughout the assessment area.

## **5. Response to Complaints & Compliance with Anti-Discrimination Laws and Regulations**

SCSB&T has not received any written CRA-related complaints since the previous evaluation of September 27, 1999. This neither enhances nor detracts from the bank's CRA performance. Additionally, a review of the bank's compliance with the anti-discriminatory rules and regulations revealed no substantive violations involving discrimination on a prohibited basis.