

PUBLIC DISCLOSURE

February 17, 2004

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**Vermillion State Bank
Certificate Number 16404**

**Third and Main Streets
P. O. Box 106
Vermillion, Kansas 66544-0106**

**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.

TABLE OF CONTENTS

I.	General Information.....	1
II.	Institution Rating	1
III.	Description of Institution	2
IV.	Description of Assessment Area.....	3
V.	Conclusions with Respect to Performance Criteria	5

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 Vermillion State Bank, Vermillion, Kansas, prepared by the Federal Deposit Insurance Corporation, the institution's supervisory agency, as of February 17, 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**.

Vermillion State Bank has demonstrated a satisfactory commitment to community reinvestment that is supported by the following conclusions.

- A majority of the reviewed agricultural and residential real estate loans originated by the bank are within the bank's assessment area, reflecting a good commitment to meeting the credit needs of the assessment area.
- An analysis of reviewed agricultural and residential real estate loans revealed a reasonable distribution of loans among farms of different sizes and to borrowers of different incomes. Only loans originated within the assessment area are included in the analysis.
- A geographic distribution analysis of the two aforementioned loan products revealed a reasonable dispersion of loans among the two census tracts within the assessment area, considering demographic information and the location of the bank's offices within the assessment area.
- The bank's average net loan-to-deposit ratio reflects an adequate willingness to provide credit given the bank's size, financial condition, and community credit needs.

DESCRIPTION OF INSTITUTION

The sole office of the Vermillion State Bank is located at Third and Main Streets, Vermillion, Kansas (population 277). The bank does not have any automated teller machines.

As of September 30, 2003, the institution's total assets equaled \$15,868,000, of which total loans represented \$7,955,000. The bank's largest loan products by dollar volume are agricultural loans (agricultural real estate and agricultural production), and residential real estate loans, which represent 45 and 34 percent of total loans, respectively. While agricultural loans constitute the largest percentage of the bank's loan portfolio, management indicated the overall focus of the bank is to meet the credit needs of the community. A distribution of the bank's entire loan portfolio is reflected in Table 1.

<i>Table 1 – Loan Distribution as of September 30, 2003</i>		
<i>Loan Type</i>	<i>Dollar Amount (000s)</i>	<i>Percent of Total Loans (%)</i>
<i>Construction and Land Development</i>	\$0	0%
<i>Secured by Farmland</i>	\$1,320	16%
<i>1-4 Family Residential Real Estate</i>	\$2,676	34%
<i>Multifamily (5 or more) Residential</i>	\$0	0%
<i>Commercial Real Estate</i>	\$110	1%
<i>Commercial and Industrial</i>	\$453	6%
<i>Agricultural Production</i>	\$2,295	29%
<i>Consumer</i>	\$1,095	14%
<i>All Other</i>	\$6	0%
<i>Total Loans Net of Unearned Income</i>	\$7,955	100%

Source: September 30, 2003, Report of Condition.

The bank is owned by a one bank-holding company, Vermillion Bankshares, Inc., Vermillion, Kansas. The institution is not subject to any financial or legal impediments that would impede its ability to help meet the credit needs of its assessment area. The bank was rated Satisfactory at the previous CRA Performance Evaluation dated March 29, 1999.

DESCRIPTION OF ASSESSMENT AREA

The Community Reinvestment Act (CRA) requires a bank to identify one or more “assessment areas” within which its regulatory agency will evaluate the bank’s performance. Assessment areas always consist of one or more census tracts, which are statistical subdivisions of a county.

The bank has defined its assessment area as census tract 9794 in Marshall County and census tract 9803 in Nemaha County, both in Kansas. Marshall and Nemaha Counties are part of the non-metropolitan area of Kansas. The assessment area is a rural, agricultural area which encompasses numerous small towns, including Corning, Centralia, and Wetmore. The bank’s office is located in census tract 9794, a middle-income tract. Throughout the description of the bank’s assessment area geographies, census tracts and tracts are used interchangeably.

Census tracts are classified as low-, moderate-, middle-, or upper-income based on the 2000 U.S. Census median family income (MFI) for non-metropolitan Kansas, which is \$42,116. A breakdown of census tract income levels is presented in Table 2.

<i>Table 2 – Census Tract Income Levels</i>		
<i>Census Tract Income Level</i>	<i>Percent of MFI</i>	<i>Non-metropolitan Kansas MFI = \$42,116</i>
<i>Low</i>	< 50%	< \$21,058
<i>Moderate</i>	50% to < 80%	\$21,058 to < \$33,693
<i>Middle</i>	80% to < 120%	\$33,693 to < \$50,539
<i>Upper</i>	120% and over	\$50,539 and over

Source: 2000 U.S. Census.

Based on the categories described in Table 2, both of the census tracts in the assessment area are classified as middle-income. Unless otherwise stated, all demographic information presented is from the 2000 U.S. Census.

According to the 1997 Census of Agriculture, there are 1,929 total farms in Marshall and Nemaha Counties. Of these, 76 percent had gross annual revenues of less than \$100,000. In Marshall County, the number of farms decreased 9 percent from 1,102 farms in 1992 to 1,007 farms in 1997. The number of farms also decreased in Nemaha County by 9 percent from 1008 farms to 922 farms within the same timeframe.

There are 1,305 families in the assessment area. Low- and moderate-income families comprise 19 percent and 24 percent, respectively, of all families residing in the assessment area. Middle- and upper-income families represent 25 and 32 percent, respectively, of the families in the assessment area. Of the 2,076 housing units in the assessment area, 76 percent are owner-occupied, 13 percent are occupied rental units, and 11 percent are vacant. The median housing value in the assessment area is \$48,877, significantly lower than the state of Kansas non-metropolitan median of \$61,200. The median housing age within the assessment area is 60

years, which is 18 years older compared to the non-metropolitan median housing age. The median gross rent in the assessment area is \$282 which is lower than the non-metropolitan median of \$415.

The top six large employers in the assessment area and the immediate surrounding area are Landoll Corporation, Moose International, Inc., Wenger Manufacturing, Inc., SKF USA, Inc., Community Memorial Healthcare, and Apostolic Christian Home.

According to the Kansas Department of Labor, the unemployment rates for Marshall and Nemaha Counties were 2.7 percent and 2.2 percent, respectively, for December 2003. The December 2003 statewide unemployment rate for Kansas was 4.5 percent.

Management stated that the bank's primary competitors for loan products are those banks located in surrounding communities, such as Axtell, Centralia, Frankfort, and Seneca, Kansas. Due to a substantial decline in interest rates, the bank has experienced increased competition from mortgage companies and the finance divisions of automobile manufacturers.

During the evaluation, examiners reviewed a recent contact with a representative from the assessment area (community contact) to obtain a profile of the community, identify community development opportunities and general credit needs, and assess opportunities for participation by local financial institutions. The community contact indicated that farm sizes are continuing to decrease and the contact was not aware of any new housing developments in the area. In addition, the community contact was unaware of any unmet credit or community development needs.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Conclusions with respect to the following three performance criteria, Lending in Assessment Area, Lending among Farms of Different Sizes and to Borrowers of Different Income Levels, and Geographic Distribution of Loans, are based on a review of the institution's loan portfolio. Examiners reviewed agricultural loans (including agricultural real estate and agricultural production) and residential real estate loans, which together comprise 79 percent of the loan portfolio. A sample of outstanding agricultural loans originated in 2003 was reviewed for purposes of this evaluation. The agricultural loan sample consisted of 36 loans totaling \$507,557 from a universe of 158 loans totaling \$3,085,611. All residential real estate loans originated and outstanding in 2003 were reviewed; this consisted of 34 loans totaling \$1,803,524. Since the bank's commercial lending activity only represented seven percent of the bank's loan portfolio, commercial-related loans were not reviewed.

a) Lending in Assessment Area

A majority of the reviewed agricultural and residential real estate loans originated by the bank are within the bank's assessment area, reflecting an adequate commitment to meeting the credit needs of the assessment area.

Agricultural Loans

Of the 36 agricultural loans reviewed, 31, or 86 percent, were originated within the assessment area. The 31 loans represented 91 percent of the dollar volume of sampled agriculture loans.

Residential Real Estate Loans

Of the 34 residential real estate loans reviewed, 28, or 82 percent, were originated within the assessment area. The 28 loans originated inside the assessment area represent 83 percent of the dollar volume of reviewed residential real estate loans.

b) Lending among Farms of Different Sizes and to Borrowers of Different Income Levels.

An analysis of agricultural and residential real estate loans reveals an adequate penetration of loans among farms of different sizes and to borrowers of different income levels. Only loans originated within the assessment area are included in the analysis.

Lending among Farms of Different Sizes – Agricultural Loans

Table 3 shows the distribution of the reviewed agricultural loans among farms of varying sizes based on gross farm revenue levels and shows the percentage of farms in Marshall and Nemaha Counties by sales volume based on the 1997 Census of Agriculture.

Table 3 – Distribution of Farm Loans by Gross Annual Farm Revenue					
Gross Annual Revenue of the Farm	Percentage of Farms in Marshall and Nemaha Counties by Sales Volume	Number of Loans	Percent of Total Number of Loans	Dollar Amount of Loans	Percent of Dollar Amount of Loans
< \$100,000	76%	23	74%	\$243,357	53%
\$100,000 to < \$250,000	17%	8	26%	\$217,900	47%
\$250,000 to < \$500,000	5%	0	0%	\$0	0%
≥ \$500,000	2%	0	0%	\$0	0%
TOTALS	100%	31	100%	\$461,257	100%

Source: 1997 Census of Agriculture and bank data.

Overall, the bank has achieved an adequate loan penetration among farms of different sizes. The bank originated 74 percent of the agricultural loans to farms with gross farm revenue of less than \$100,000, which is similar to the percentage of farms within the assessment area in the same revenue category. The bank originated 26 percent of its agricultural loans, by number, to farms with gross annual revenue ranging from \$100,000 to less than \$250,000. The bank’s percentage of loans exceeds the percentage of farms in the assessment area within this revenue category. From the information presented in Table 3, the bank’s lending to farms with revenues of less than \$250,000 is adequate.

Lending to Borrowers of Different Income Levels – Residential Real Estate Loans

Examiners used the 2003 adjusted HUD MFI of \$44,900 for the non-metropolitan area of Kansas, to evaluate the bank’s lending to borrowers of different incomes. Table 4 defines each income category.

Table 4 - Borrower Income Levels		
Borrower Income Level	Percent of MFI	2003 Non-Metro Kansas MFI = \$44,900
<i>Low</i>	< 50%	< \$22,450
<i>Moderate</i>	50% to < 80%	\$22,450 to < \$35,920
<i>Middle</i>	80% to < 120%	\$35,920 to < \$53,880
<i>Upper</i>	120% and over	\$53,880 and over

Source: HUD Estimated 2003 MFI.

Table 5 shows the distribution of residential real estate loans among borrowers of different income levels. In addition, the table includes the percentage of assessment area families within each income level according to 2000 U.S. Census data.

Table 5 – Distribution of Residential Real Estate Loans by Borrower Income					
<i>Borrower Income Level</i>	<i>Percent of Assessment Area Families</i>	<i>Number of Loans</i>	<i>Percent of Total Number of Loans</i>	<i>Dollar Amount of Loans</i>	<i>Percent of Dollar Amount of Loans</i>
<i>Low</i>	19%	6	21%	\$ 196,800	13%
<i>Moderate</i>	24%	6	21%	\$ 273,152	19%
<i>Middle</i>	25%	5	18%	\$ 153,343	10%
<i>Upper</i>	32%	11	40%	\$ 869,384	58%
<i>TOTALS</i>	100%	28	100%	\$1,492,679	100%

Source: 2000 U.S. Census and bank data.

Based on the information presented in Table 5, the bank has a good penetration of residential real estate loans among borrowers of different income levels. The information reveals that the bank originated 21 percent, by number, of its residential real estate loans to low-income borrowers. The bank's lending performance is slightly higher than that of the assessment area demographics in this category. In addition, the bank originated 21 percent, by number, of its residential real estate loans to moderate-income borrowers, which is slightly less than the percentage of moderate-income families in the assessment area. The bank's record of lending to middle-income borrowers is also less than the percent of middle-income families in the assessment area. With regard to upper-income borrowers, the bank's percent of residential real estate loans is above that of assessment area families designated as upper-income. Overall, the bank's lending to borrowers of different income levels reflects the assessment area demographics.

c) Geographic Distribution of Loans

A geographic distribution analysis of the two loan products revealed a reasonable dispersion of loans among the two census tracts within the assessment area, considering demographic information and the location of the bank's office within the assessment area. Only loans originated within the assessment area are included in the analysis.

The bank originated 61 percent of its agricultural loans and 61 percent of its residential real estate loans in census tract 9794, the location of bank's sole office. As discussed in *Description of Assessment Area*, both of the census tracts in the assessment area are classified as middle-income. Accordingly, all of the agricultural and residential real estate loans were originated in middle-income tracts.

d) Loan-to-Deposit Ratio

The bank's average net loan-to-deposit ratio (ratio) reflects an adequate willingness to provide credit given the bank's size, financial condition, and community credit needs. The bank's ratio,

based on 19 quarters (ending September 30, 2003) since the previous evaluation, is 66 percent. The ratio has increased from the ratio at the previous evaluation when it was 64 percent. During the period, the ratio has been as low as 57 percent (March 31, 1999) and as high as 74 percent (June 30, 2001).

To evaluate the reasonableness of the bank's ratio, examiners compared it to the ratio of similarly situated banks (banks with similar asset size, structure, loan portfolio mix, or area served). Management concurred with the similarly situated bank listed in Table 6.

<i>Table 6 – Similarly Situated Banks</i>					
<i>Bank Name</i>	<i>Branches</i>	<i>Total Assets (000s)</i>	<i>Total Deposits (000s)</i>	<i>Net Loans (000s)</i>	<i>Average Net Loan to Deposit Ratio</i>
<i>The Baileyville State Bank Seneca, Kansas</i>	0	\$23,758	\$21,482	\$12,803	70%
<i>Vermillion State Bank Vermillion, Kansas</i>	0	\$15,868	\$12,809	\$8,206	66%

Source: September 30, 2003, Report of Condition and Report of Condition data over the previous 19 quarters. The banks are listed in alphabetical order by city.

Table 6 shows that Vermillion State Bank's ratio of 66 percent is adequate when compared to the ratio of the other bank identified as similarly situated. Over the past 19 quarters, the bank's net loans have increased \$1,995,000 (32 percent), whereas total deposits have increased \$1,870,000 (17 percent), which favorably impacts the ratio.

e) Response to CRA-Related Complaints

Neither the bank, nor the Federal Deposit Insurance Corporation, has received a CRA-related complaint.

f) Compliance with Anti-Discrimination Laws and Regulations

No violations of the substantive provisions of the anti-discriminatory laws and regulations were identified during the evaluation.