

PUBLIC DISCLOSURE

September 6, 2005

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**Heritage Bank of Ashland, Inc.
34561**

**855 Central Avenue
Ashland, Kentucky 41101**

**Federal Deposit Insurance Corporation
Division of Supervision and Consumer Protection
Chicago Regional Office
500 West Monroe Street, Suite 3500
Chicago, Illinois 60661**

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 **Heritage Bank of Ashland, Inc.** prepared by the **Federal Deposit Insurance Corporation**, the institution's supervisory agency, as of **September 6, 2005**. 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 bank's CRA performance depicts a satisfactory practice of providing for the credit needs of its assessment areas. The rating is supported by the following information:

- The average net loan-to-deposit ratio reflects reasonable lending performance and demonstrates management's willingness to extend loans even though the bank is operating under lending restrictions.
- A majority of both residential real estate loans and small business loans are extended within the assessment areas.
- The bank has an adequate record of extending residential real estate loans to low-income borrowers, and a good record of extending residential real estate loans to moderate-income borrowers. In addition, the bank is extending loans to businesses of varying sizes, particularly small and very small businesses.
- Both residential real estate loans and small business loans are reasonably dispersed throughout all geographies of the bank's MSA assessment area, including the moderate-income geographies.

DESCRIPTION OF INSTITUTION

Heritage Bank of Ashland, Inc., Ashland, Kentucky, (hereafter referred to as HB) is a relatively new independent community bank which began operations during 1998. Total assets of the institution were \$85,347,000, as of June 30, 2005. The bank operates three full-service offices. The Main Office is located in Boyd County, which is located in extreme northeastern Kentucky. The bank has opened two new offices since the October 25, 2000, CRA evaluation. One branch was opened during August 2003 in Russell, Kentucky, in eastern Greenup County. Another branch was opened during August 2001 in Grayson, Kentucky located in Carter County. All offices offer full-service automated teller machines (ATMs).

HB operates under the ownership of a one-bank holding company, Heritage Capital Corporation, Ashland, Kentucky. There are no affiliated banks of HB.

HB has a gross loan base of \$60,666,000 as of June 30, 2005. A wide variety of lending products are offered including mortgage loans, business loans, consumer loans and farm loans. Residential mortgage loans can be for a variety of purposes including home purchase, home refinance and home improvement. Mobile home loans are also offered. In-house loans are written as 1, 3 or 5-year adjustable-rate mortgages. Long-term fixed-rate residential loans are originated by the bank and sold on the secondary market to Countrywide Financial. Other types of loans, such as business, farm and consumer loans (not secured by real estate), can be either fixed or variable-rate. Table 1, below, depicts the bank's loan portfolio, by type of loan, as of June 30, 2005.

Table 1		
HB – Loan Distribution as of June 30, 2005		
Loan Type	Dollar Amount (000s)	Percent of Total Loans (%)
Construction and Land Development	426	1%
Secured by Farmland	129	<1%
1-4 Family Residential	24,824	41%
Multi-Family (5 or more) Residential	620	1%
Commercial	9,605	16%
Total Real Estate Loans	35,604	59%
Commercial and Industrial	15,143	25%
Agricultural	23	<1%
Consumer	9,673	16%
Other	223	<1%
Gross Loans	\$60,666	100%

Source: Report of Condition for June 30, 2005

There are certain legal and financial impediments that prevent the bank from helping to meet assessment area credit needs. HB has operated under a written agreement with the FDIC since April 2004. At that time, the bank and the Federal Deposit Insurance Corporation (FDIC) entered into a “Cease and Desist Order.” The Order has acted as a constraint on loan originations. Gross loans grew since the 2000 CRA evaluation and reached \$100 million, but loans have since declined to the current level of almost \$61 million due to the restrictions that have been present.

Residential real estate lending and commercial lending (which consists of commercial real estate and commercial and industrial loans) are the bank’s primary lending categories based on the loan portfolio mix. As depicted in Table 1, 1-4 family residential real estate lending and commercial lending each comprise 41 percent of the loan portfolio. Consumer lending makes up the next largest percentage at 16 percent.

The lending percentages are reflective of the credit needs of HB’s assessment areas. Housing continues to be a need for both assessment areas. There is a lesser need for business lending, due to the limited economic growth in the areas over recent years.

Banking competition is strong throughout the assessment areas. There are numerous financial institutions in Boyd County, where the bank’s main office is located. In the assessment area including Boyd and Greenup Counties, the bank ranked 9th out of eleven banks reporting deposits. HB’s deposit market share for this assessment area is 7 percent. Carter County has fewer financial institutions. The bank ranked 4th out of five institutions reporting deposits in Carter County. HB has a 4 percent market share in this assessment area. There are two banks in Carter County which hold 88 percent of the market share. HB is somewhat new to this community.

DESCRIPTION OF ASSESSMENT AREAS (BOYD & GREENUP COUNTIES)

Management has defined the bank’s assessment areas as Boyd County and portions of Greenup County in the Huntington-Ashland, WV-KY-OH Metropolitan Statistical Area (MSA) #26580, which is one assessment area. Carter County, which is located in the Non-Metropolitan area (Non-MSA) of the State of Kentucky, is the bank’s second assessment area. The three counties are contiguous and include all the bank’s branches. However, the two areas must be analyzed separately to assess the bank’s performance in the MSA and the Non-MSA areas.

MSA ASSESSMENT AREA (Boyd and Greenup Counties)

Management has defined the bank’s assessment area as all of Boyd County, Kentucky, and a portion of eastern Greenup County, which are contiguous counties located in extreme northeastern Kentucky along the Ohio River. The assessment area is part of the Huntington-Ashland, West Virginia-Kentucky-Ohio Metropolitan Statistical Area (MSA) #26580. The two counties are the only Kentucky counties included in the MSA. This assessment area is defined in

accordance with the CRA regulation and does not arbitrarily exclude any low- or moderate-income areas.

According to 2000 Census data, the MSA assessment area consists of 16 census tracts (CTs). None of these census tracts are low-income geographies. Two of the census tracts, both located in Boyd County, are considered moderate-income areas. Eight census tracts are considered middle-income areas, and the remaining six census tracts are considered upper-income areas. HB's Main Office is located in CT 303, a moderate-income tract located in Boyd County. The Russell Branch is located in CT 401, an upper-income tract located in Greenup County.

Boyd and Greenup Counties, from an economic standpoint, are considered one area. The counties are primarily rural in nature. Residential developments are located throughout the assessment area, with commercial development mainly confined to the City of Ashland, which technically crosses into Greenup County into the City of Russell. The cities of Russell and Ashland are joined at the county borders. According to 2000 U.S. Census data, the population of the assessment area is 71,695. Ashland is the largest city with a population of 21,491.

A previous evaluation of the area included an interview with a local community contact involved with economic development. According to this contact, the area has seen a decreasing population base primarily because of the exodus of many younger residents due to the lack of sufficient employment opportunities in these counties. The area economy has been declining over recent years. There have been significant job losses, primarily in the manufacturing industry, over the past several years. The most significant of these job losses occurred when Ashland Petroleum moved its operations to Covington, Kentucky in the late 1990s resulting in a loss of over 1,200 jobs.

The contact also stated that the area has some difficulty in attracting and maintaining new industry primarily because of a lack of infrastructure available throughout this region of Kentucky. Specifically, water and sewer service is not available to all parts of the area. In addition, the contact stated the lack of a major airport also contributes to the difficulty in attracting new industry. Finally, the contact stated the area has gained some new jobs in recent months; however, these jobs are mainly service industry jobs, such as retail stores or food service jobs, which typically offer much lower wages than the lost manufacturing jobs.

The unemployment rates for each county almost mirror each other. Boyd and Greenup experienced unemployment rates of 6.6 and 6.7 percent, respectively, during June 2004, decreasing slightly to 6.3 percent for both counties during June 2005. These rates are in line with the State of Kentucky, which reported unemployment of 6 percent for June 2005.

In the two county area, there are two major regional hospitals Kings Daughter Medical Center which employs 3,000, and Our Lady of Bellefonte Hospital is also a major employer with around 1,200 workers. Other significant non-medical employers include Cingular Wireless, which employs 1,150; AK Steel, which employs 1,131; and Marathon Petroleum, LLC, which employs 1,050. The school systems and Wal-Mart are other primary employers.

Despite the decrease in population and the downturn in the local economy, the housing market is relatively stable. This is due in part to relatively lower median home values in relation to median household income as compared to the entire state of Kentucky. Specifically, according to recent housing data, the median value of a home for both counties is \$70,000. However, even though homes are affordable in the area, the community contact stated that many newer homes are in the middle- and upper-income range, and there is a continuing need for more affordable housing for low- and moderate-income residents.

U.S. Census data indicates that the 2000 MSA Median Family Income (MFI) for the assessment area is \$37,894. The Department of Housing and Urban Development (HUD) estimates 2003 and 2004 MFI to be \$43,200 and \$43,700, respectively. The CRA definition for each income level is defined in Table 2. For brevity, only 2003 and 2004 figures are shown. For purposes of this evaluation, geographic income level classifications are based upon the 2000 Census income data.

TABLE 2			
INCOME LEVEL	PERCENT OF MFI	2003 RANGE	2004 RANGE
Low-income	Less than 50%	Under \$21,600	Under \$21,850
Moderate-income	50% to < than 80%	\$21,600 - <\$34,560	\$21,850 - <\$34,960
Middle-income	80% to < than 120%	\$34,560 - <\$51,840	\$34,960 - <\$52,440
Upper-income	120% and over	\$51,840 and over	\$52,440 and over

Table 3, below, reflects the number of assessment area families within the various income level ranges based on the 2000 Census data. The information is used for comparative purposes to assess performance in lending to borrowers of different income levels, as detailed in the “Lending to Borrowers of Different Incomes and Businesses of Different Sizes” section of this evaluation.

TABLE 3	
Income Level	2000 Percent of Families
Low	18%
Moderate	15%
Middle	20%
Upper	47%
Totals	100%

The motto for this assessment area is “Ashland-A Proud Past, A Bright Future.” On a positive note, the MSA assessment area serves as a regional community with regional medical centers, a community college, and somewhat diverse employment. However, the area continues to battle the population loss and is attempting to stabilize jobs after some large employment losses.

NON-MSA ASSESSMENT AREA (CARTER COUNTY)

HB has defined its Non-MSA assessment area as Carter County, which consists of seven census tracts—all of which are middle-income geographies. Carter County is located in the northeast corner of Kentucky, contiguous to both Boyd and Greenup Counties. Carter County was part of the Huntington-Ashland, West Virginia-Kentucky-Ohio Metropolitan Statistical Area until the MSA changes which were effective January 1, 2004. At that time, Carter County was excluded from the MSA. The City of Grayson is the county seat of Carter County. The closest metropolitan city is Ashland, which is approximately 25 miles from Grayson. Highway access to Carter County and the City of Grayson is very good. HB has one office located in Carter County in the City of Grayson, in CT 9606.

All the tracts in Carter County, while middle-income, are classified as distressed or underserved nonmetropolitan middle-income geographies for CRA purposes. The reason for the “distressed” designation is because of the high poverty level and unemployment rate in Carter County. The unemployment rate in Carter County for June 2005 was 8.8 percent, which is a slight decline from one year prior when the rate was 9.2 percent. In comparison, Carter County has a much higher rate than the State of Kentucky, which reported an unemployment rate of 6 percent for June 2005.

Carter County has an estimated population of 26,889 based on the 2000 U. S. Census Bureau figure. The population has grown about 3,600 from 1990 to 2000. The county’s largest population center is the City of Grayson, with a 2003 population of 3,980. The next-largest city is Olive Hill, with a population of 1,794 residents. These population figures provide evidence of the largely rural nature of the assessment area. Approximately 79 percent of the assessment area population lives outside these two cities.

The county’s largest employer is Carter County Public Schools, which employs approximately 1,000 persons. According to the Kentucky Cabinet for Economic Development (KCED), Carter County’s largest manufacturer is Con Agra Foods, which employs 800 persons and produces ham products. Data from KCED further indicates that, while no existing industrial businesses have significantly expanded in Carter County in recent years; one new manufacturing firm has been reported as locating in the County since the year 2001. This firm, Fresh ‘N Ready Foods, Inc., opened in 2003, creating 160 new jobs.

According to a community contact interviewed during early 2005, there is very little credit growth in the market area. However, there is growth in the residential housing market as persons retire and locate to Carter County. Carter County serves as a bedroom community. The contact stated that the local economy is sluggish and unemployment is high, but the retail sector seems to be improving slightly. Grayson’s access to Interstate 64 brings income through services gained from this access. The community contact stated that there is very little expansion in Carter County. Although there is not a current need, there is land available within the city where housing units could be built to accommodate an influx of relocating employees. Carter County also has an industrial park located near Interstate 64.

The 2000 median home value is affordable at \$57,100. In 2000, 98 percent of owner-occupied homes in Carter County were valued at less than \$100,000.

According to U.S. Census Bureau data, the 2000 Median Family Income (MFI) was \$40,426 for the statewide non-metropolitan portion of Kentucky. For 2003, the Department of Housing and Urban Development (HUD) estimated the MFI for these non-metropolitan areas to be \$38,600 and \$38,400 for 2004. For purposes of this evaluation, geographic income level classifications are based upon the 2000 Census income data. The HUD estimated income data for 2003 and 2004 was used to analyze lending to borrowers of different incomes.

The Kentucky statewide non-MSA income levels are defined for 2003 and 2004 in Table 4.

TABLE 4			
INCOME LEVEL	PERCENT OF MFI	2003 RANGE	2004 RANGE
Low-income	Less than 50%	Under \$19,300	Under \$19,200
Moderate-income	50% to < than 80%	\$19,300 - <\$30,880	\$19,200 - <\$30,720
Middle-income	80% to < than 120%	\$30,880 - <\$46,320	\$30,720 - <\$46,080
Upper-income	120% and over	\$46,320 and over	\$46,080 and over

Table 5 shows the distribution of assessment area families by income level.

TABLE 5	
Income Level	2000 Percent of Families
Low	26%
Moderate	16%
Middle	20%
Upper	38%
Totals	100%

The poverty level in Carter County is high. According to the 2000 Census Information, 19 percent of families live below the poverty level, when the State of Kentucky is at 11 percent.

The community contact indicated that, despite efforts to grow the local economy, it has remained lethargic but stable for a number of years. As was mentioned earlier, there has been no significant industrial expansion and very little new industry in the area; however, on a positive note, Carter County has experienced some population growth.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Scope of the Evaluation

HB qualifies as a small bank as defined in the CRA regulation. According to the CRA regulation, a small bank is defined as a bank that had total assets of less than \$250,000,000 as of December 31 of either of the prior two calendar years. The CRA performance of a small bank is evaluated based on the following criteria:

- Loan-to-deposit ratio
- Lending in the assessment areas
- Lending to borrowers of different income categories and to businesses of different sizes
- Geographic distribution of loans within the assessment areas by geography
- Response to consumer complaints

The evaluation of the bank's lending performance is based upon a review of two loan types, residential loans and commercial/small business loans. These two loan categories were chosen for review because they aggregately represent approximately 82 percent of the bank's total loan portfolio and are considered the greater credit needs for the assessment area.

For residential mortgage loans, all originated loans reported under the Home Mortgage Disclosure Act (HMDA) for 2003 and 2004 are included in the analysis. There were a total of 163 loans reported in 2003 totaling \$12,418,000, and 156 reported for 2004 totaling \$13,546,000. All 319 loans were used in assessing the bank's residential lending performance. The first six months of lending for 2005 was reviewed but was not included in the analysis.

For commercial/small business loans, all loans extended over a one year period from June 1, 2004, through May 31, 2005, were included in the universe. There were a total of 65 business loans totaling \$4,633,000 identified for analysis. A sample of 25 small business loans was reviewed totaling \$1,399,000.

For purposes of this evaluation, census tract income level classifications used in the "Geographic Distribution of Loans" section of this evaluation are based upon the 2000 income data. However, the HUD-estimated 2003 and 2004 income figures and business information were used to define various income levels of borrowers in the "Lending to Borrowers of Different Incomes and Businesses of Different Sizes" section of this evaluation.

Loan-to-Deposit Ratio

HB's lending activity, as measured by its loan-to-deposit (LTD) ratio, indicates a reasonable responsiveness to community credit needs.

The average net LTD ratio, based on 19 quarters since the previous CRA evaluation of October 25, 2000, is 85 percent. The bank's ratio has shown some fluctuation since 2000. Loans grew until mid-2003 and have shrunk since that time, in part due to regulatory constraints. The regulatory factors discussed previously contributed to the changes in the bank's lending. In

comparison to other financial institutions located in the assessment areas, the bank's most recent loan-to-deposit ratio, as of June 30, 2005, is reasonable.

Lending in the Assessment Areas

When considering both types of loans reviewed, HB has a good record of extending loans within its assessment areas.

Table 6, below, shows the distribution of both the residential real estate and business loans reviewed, which were extended both inside and outside the assessment areas.

Table 6 – HB's Distribution of Loans Inside and Outside of the Assessment Areas								
Loan Type	Number of Loans				Dollar of Loans			
	Inside		Outside		Inside		Outside	
	#	%	#	%	\$(000s)	%	\$(000s)	%
Residential	263	82%	56	18%	\$20,070	77%	\$5,894	23%
Business	15	60%	10	40%	\$921	66%	\$478	34%
Total	278	81%	66	19%	\$20,991	77%	\$6,372	23%

Bank records, HMDA data for 2003 and 2004

When analyzing both types of loans reviewed aggregately, the bank has extended 81 percent (by number) and 77 percent (by dollar amount) within its assessment areas. These relatively high percentages demonstrate management's willingness to serve its assessment areas credit needs first, before seeking loans elsewhere.

MSA PERFORMANCE

The following analysis describes the bank's performance in the MSA assessment area which includes Boyd County and portions of Greenup County. The performance within this assessment area is given the most weight because the bank has two offices penetrating this assessment area.

Lending to Borrowers of Different Incomes and Businesses of Different Sizes

When considering both types of loans reviewed, the bank has a reasonable record of extending loans to low-income borrowers and a good record to moderate-income borrowers. The bank also has a good record of lending to businesses of all sizes, including small and very small businesses.

Residential Lending

Table 7, below, displays the lending distribution of the residential loans extended in 2003 and 2004. The lending information for the two years is combined because the bank's performance to low- and moderate-income borrowers was so similar. For comparative purposes, the table also includes the percentages of families within each income level according to the 2000 census data. The 2003 Aggregate Lending Data column represents all HMDA-reportable loans extended

within the bank's assessment area reported by all HMDA-reporters. This information is used for comparative purposes.

Table 7 – 2003 and 2004 Distribution of Residential Loans by Borrower Income Level						
Borrower Income Level	% of Total Assessment Area Families	2003 Aggregate Lending Data	HB 2003 and 2004 Lending			
		% (By #)	#	%	\$ (000s)	%
Low	18%	8%	9	5%	\$408	3%
Moderate	15%	16%	31	16%	\$1,611	10%
Middle	20%	26%	54	27%	\$3,508	22%
Upper	47%	50%	103	52%	\$10,122	65%
Total	100%	100%	197	100%	\$15,649	100%

*Income was not available for 1 loan during 2003 totaling \$20,000 and 8 loans during 2004 totaling \$898,000.

As shown in the above tables, HB's lending percentages to low-income borrowers is somewhat below aggregate data. This indicates that the bank has slightly lower lending in comparison to other HMDA-reporting financial institutions that extended residential real estate loans to low-income borrowers within the assessment area. The volume and percentages to low-income borrowers for the bank were almost at the same level for both 2003 and 2004, with 5 and 4 reported, respectively.

HB's lending percentages to low-income borrowers is also somewhat below the percent of families in this income category. However, this lending percentage is still considered reasonable for the following reason. The 2000 Census data indicates that 11 percent of low-income families have incomes below the poverty level. Therefore, due to their limited income, these families often experience economic barriers to homeownership resulting in a smaller potential borrowing base to which the bank can extend loans. Reducing the low-income family representation by the percent of families below the poverty level yields a potential borrowing base in this income category of 7 percent. HB's lending percentage to low-income borrowers at 5 percent is still below this percentage, but is considered adequate. The banking competition in this assessment area is strong; therefore, making it competitive to reach the lower-income borrowers. The bank has become involved in the Federal Home Loan Bank's Welcome Home Program and has originated fewer than five loans through this program. The bank lends through this program as funds are available. Also, the bank's secondary market program offers numerous products for customers with minimal income and no down payment. The bank is making efforts to lend to low-income borrowers.

The bank's lending to moderate-income borrowers is good. The bank compares favorably to the aggregate data and to the percentage of moderate-income families. There were 19 loans extended to moderate-income borrowers during 2003 and 12 during 2004.

Small Business Lending

The CRA regulation defines a “small business” loan on the basis of loan amount. Specifically, business loans in the amount of \$1,000,000 or less are considered “small business” loans. Table 8, below, displays the distribution of the business loans analyzed. Only those loans extended within the assessment area are included in the table.

Table 8 – Distribution of Commercial/Small Business Loans By Loan Size				
Loan Size	Number	Percent	Amount (\$000)	Percent
\$100,000 or less	6	100%	\$246	100%
\$100,001 - \$250,000	0	0	0	0
\$ 250,001 - \$1,000,000	0	0	0	0
TOTALS	6	100%	\$246	100%

The bank’s small business lending distribution is very good. As shown above, all of the commercial loans analyzed are considered small business loans, per the CRA regulation definition. In fact, as shown, all the commercial loans analyzed were extended in an amount of \$100,000 or less. This data indicates the bank’s willingness to extend loans to very small businesses in its assessment area. Using loan size as a proxy for the revenue size of the business, the bank’s performance demonstrates a very strong willingness to fund the credit needs of small business owners. These high lending percentages are expected considering that 92 percent of all assessment area businesses reporting revenues have revenues of \$1,000,000 or less according to a 2004 Dun & Bradstreet Business Report.

Geographic Distribution of Loans

The bank has achieved a reasonable penetration of both residential and commercial loans throughout its assessment area, including the moderate-income geographies.

Table 9, on the following page, displays the geographic dispersion of residential real estate loans extended for 2003 and 2004. For comparative purposes, the percentages of owner-occupied housing units (OOHUs) located within each census tract income designation are also included. The 2003 Aggregate Lending Data column represents all HMDA-reportable loans extended within the bank’s assessment area reported by all HMDA-reporters. This information is used for comparative purposes.

Table 9 – 2003 and 2004 Distribution of Residential Loans by Census Tract Income Level						
Census Tract Income Level	% of Total Assessment Area Owner-occupied Housing Units	2003 Aggregate Lending Data	HB 2003 and 2004 Lending			
		% (By #)	#	%	\$(000s)	%
Moderate	6%	6%	11	5%	\$756	5%
Middle	49%	35%	92	45%	\$6,912	42%
Upper	45%	59%	103	50%	\$8,899	53%
Total	100%	100%	206	100%	\$16,567	100%

As shown in Table 9 above, during 2003 and 2004, HB's percentage of residential loans extended in the two moderate-income census tracts is in alignment with the aggregate data reported and the percentage of OOHUs in these geographies. This indicates good performance in serving residential borrower credit needs in the moderate-income areas for 2003 and 2004. The number and dollar volume extended in the moderate-income geographies for 2003 totaled 6 originations amounting to \$332,000, and the amount for 2004 totaled 5 for \$424,000.

Table 10, below displays the geographic distribution of the business loans reviewed. For comparative purposes, the percentage of businesses located within each Census Tract income designation (according to a 2004 Dun & Bradstreet Business report) is also included.

TABLE 10 – Distribution of Commercial/Small Business Loans By Census Tract Income Level					
Census Tract Income Level	Percent of Business	Number	Percent	Dollar Amount (\$000)	Percent
Moderate	9%	0	0%	0	0%
Middle	52%	2	33%	\$34	14%
Upper	39%	4	67%	\$212	86%
TOTAL	100%	6	100%	\$246	100%

As shown in the above table, the bank has not extended any loans to businesses located in the two moderate-income geographies, based on the sample reviewed. Further review of the bank's loan portfolio identified that the bank has originated loans in this area; however, none were in the sample.

NON-MSA PERFORMANCE

The following analysis describes the bank's lending performance in Carter County.

Lending to Borrowers of Different Incomes and Businesses of Different Sizes

When considering both types of loans reviewed, the bank has a reasonable record of extending loans to low-income borrowers and a good record to moderate-income borrowers. The bank is lending to businesses of all sizes, including small and very small businesses.

Residential Lending

Table 11, below, displays the lending distribution of the residential loans extended for the combined years of 2003 and 2004, reported on the bank's HMDA registers. For comparative purposes, the table also includes the percentages of families within each income level according to the 2000 Census data. The 2003 Aggregate Lending Data column represents all HMDA-reportable loans extended within the bank's assessment area reported by all HMDA-reporters. During 2003 Carter County was still included in the MSA. This information is used for comparative purposes.

Table 11 – 2003 and 2004 Distribution of Residential Loans by Borrower Income Level						
Borrower Income Level	% of Total Assessment Area Families	2003 Aggregate Lending Data	HB 2003 and 2004 Lending			
		% (By #)	#	%	\$ (000s)	%
Low	26%	9%	1	2%	\$19	1%
Moderate	16%	25%	21	38%	\$868	25%
Middle	20%	26%	12	21%	\$156	4%
Upper	38%	40%	22	39%	\$2,440	70%
Total	100%	100%	56	100%	\$3,483	100%

*Income was not available for 1 loan for \$20,000.

As shown in the above tables, HB's lending percentages to low-income borrowers is below aggregate data. This indicates that the bank has lower lending in comparison to other HMDA-reporting financial institutions that extended residential real estate loans to low-income borrowers within the assessment area.

HB's lending percentage to low-income borrowers is also considerably below the percent of families in this income category. However, this lending percentage is still reasonable for the following reason. The 2000 Census data indicates that 19 percent of the low-income families have incomes below the poverty level. Therefore, due to their limited income, these families experience economic barriers to homeownership resulting in a smaller potential borrowing base to which the bank can extend loans. Reducing the low-income family representation by the

percent of families below the poverty level yields a potential borrowing base in this income category of 7 percent. HB's lending percentage to low-income borrowers at 2 percent is still below this percentage, but is considered adequate in light of the distressed nature of the area and the competition for these low-income credits, only 42 of which were extended by the aggregate in the assessment area in 2003.

HB's lending percentages to moderate-income borrowers for both years is very good at 38 percent. The bank's performance compares favorably to the aggregate percentage and the percentage of moderate-income families in the assessment area. The bank's performance for 2003 produced 10 loans, with 11 originations during 2004 to moderate-income borrowers.

Small Business Lending

The CRA regulation defines a "small business" loan on the basis of loan amount. Specifically, business loans in the amount of \$1,000,000 or less are considered "small business" loans. Table 12, below, displays the distribution of the business loans analyzed. Loans extended only within the assessment area are included in the table.

Table 12 – Distribution of Commercial/Small Business Loans By Loan Size				
Loan Size	Number	Percent	Amount (\$000)	Percent
\$100,000 or less	7	78%	\$126	19%
\$100,001 - \$250,000	1	11%	\$176	26%
\$ 250,001 - \$1,000,000	1	11%	\$373	55%
TOTALS	9	100%	\$675	100%

As shown above, 78 percent of the small business loan originations in this assessment area were extended to the very smallest of businesses in amounts of \$100,000 and less. Using loan size as a proxy for the revenue size of a business, indicates the bank's willingness to lend to the smallest of businesses. High lending percentages are expected considering that 94 percent of all assessment area businesses have revenues of \$1,000,000 or less according to a 2004 Dun & Bradstreet Business Report.

Geographic Distribution of Loans

The assessment area consists of seven census tracts, all of which are middle-income geographies. Since there are no low- or moderate-income census tracts in the assessment area, the performance criterion for the geographic distribution of loans does not bear any weight in the assignment of the bank's overall CRA rating.

Response to Complaints

No complaints concerning the bank's Community Reinvestment Act performance have been received by the bank or the FDIC Regional Office since the prior evaluation on October 25, 2000.

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.