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**SMALL BANK**

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Comptroller of the Currency  
Administrator of National Banks

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Washington, DC 20219

## **PUBLIC DISCLOSURE**

**May 5, 2004**

# **COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION**

**Palm Desert National Bank  
Charter Number 17121**

**73-745 El Paseo  
Palm Desert, California 92260**

**Office of the Comptroller of the Currency  
Southern California South Field Office  
1925 Palomar Oaks Way, Suite 202  
Carlsbad, California 92008**

**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:

- ❑ The average loan-to-deposit (LTD) ratio of 57% is reasonable.
- ❑ The majority of loans are in the bank's assessment area (AA).
- ❑ Business loan distribution reflects reasonable penetration among businesses of different sizes.
- ❑ Geographic loan distribution does not meet the standard for satisfactory dispersion throughout the assessment area.
- ❑ There have not been any public complaints about the bank's CRA performance.

## DESCRIPTION OF INSTITUTION

Palm Desert National Bank (“the bank”), a wholly-owned subsidiary of Palm Desert Investments, provides a full range of banking services to its commercial and consumer customers through its main office and two branches located in the Palm Desert area. The bank opened its Rancho Mirage branch in March 1999, and the La Quinta branch in December 2001. These two branches are located in middle-income tracts. The bank has not closed any branches since the last evaluation. The bank's business is concentrated in Palm Desert and the surrounding areas of the Coachella Valley.

The bank provides traditional banking services with a commercial focus. Consumer and retail services are available, but represent a small portion of the bank's overall lending portfolio. Lending activities are centered in real estate, construction, and commercial lending. The bank is a participant in the Bureau of Indian Affairs' loan guarantee program, Small Business Administration (SBA) guarantee program, SBA/CDC 504 real estate loan program, and the State of California loan guarantee program. This is discussed in detail in the **Lending to Businesses of Different Sizes** section of this Performance Evaluation. The bank also provides a variety of electronic banking services, including automated teller machines (ATMs) and point of sale sponsorship. Electronic banking is a major line of business and has showed continued growth since its inception in 1999. As of December 31, 2003, the bank provided cash management services for 8,682 ATMs nationwide (including 22 owned by the bank). The majority of these ATMs do not accept deposits, but ATMs located at the bank's main office and branch locations do accept deposits.

There are no financial or legal impediments that hinder the bank's ability to meet the credit needs of the community. As of December 31, 2003, total assets were \$296 million, including net loans of \$108 million.

The bank received a Satisfactory rating at the last CRA examination, dated December 7, 1998.

*Please refer to the bank's CRA public file for more information about the institution.*

## DESCRIPTION OF ASSESSMENT AREA

The AA is comprised of the central portion of Riverside-San Bernardino Metropolitan Area (MA) 6780. The assessment area is located in the Coachella Valley, which includes the unincorporated area of Bermuda Dunes and the following cities: Cathedral City, Coachella, Indian Wells, Indio, La Quinta, Palm Desert, Palm Springs, and Rancho Mirage. This area encompasses 312 square miles and has a population of 274,711 (based on 2000 US Census data). The population increased 19% between 1990 and 2000.

According to the 2000 US Census, the AA consists of 63 census tracts. Of these tracts, 35% are defined as low- to moderate-income (LMI) areas. This is a decrease from the 1990 US Census,

which defined 45% of the area as LMI. The bank's assessment area meets the requirements of the regulation and does not arbitrarily exclude any low- or moderate-income areas. Competition within the AA is strong. Other financial institutions include branches of large multi-national banks, savings and thrift associations, credit unions, and larger community banks.

In conjunction with this CRA examination, we conducted a community contact interview to learn about credit needs within the community and how well financial institutions address its credit and service needs. The contacts for this examination included representatives from a county economic development agency located in the Riverside-San Bernardino MA. These representatives indicated the need for affordable housing, small business financing, and small business education. One contact stated she has seen small businesses being denied credit due to poor money management. She would like to see bank representatives work with the economic development council to assist them in conducting workshops targeted for small business owners, such as financial statement preparation, establishing a good credit record, and workforce training & retention.

## DETERMINATION OF PRIMARY LOAN PRODUCTS

Table 1 lists the outstanding balance of the bank's major loan products as of March 31, 2004.

Table 1

<b>Palm Desert National Bank Loan Portfolio Composition As of March 31, 2004</b>				
<b>Loan Type</b>	<b>Number</b>	<b>Percentage</b>	<b>Dollar (000)*</b>	<b>Percentage</b>
Commercial	352	68%	150,423	90%
Residential Real Estate	119	23%	4,930	3%
Consumer	44	9%	12,098	7%
Other	1	<1%	52	<1%
<b>Total</b>	<b>516</b>	<b>100%</b>	<b>167,503</b>	<b>100%</b>

\*Reflects total commitment amount

Commercial loans are the bank's primary loan product; therefore, we reviewed a sample of commercial loans originated between January 1, 1999 and December 31, 2003. The percentage of the bank's AA defined as LMI, per the US Census, decreased from 45% in 1990 to 35% in 2000. To improve the accuracy of our results and compensate for that change, we compared loans originated between 1999 and 2002 to the 1990 US Census data, and compared loans originated during 2003 to the 2000 US Census data.

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

### **LOAN-TO-DEPOSIT RATIO**

The loan-to-deposit (LTD) ratio is an indicator of a bank's willingness to lend. The bank's degree of lending is reasonable given its size, the credit needs of the assessment area, and the competitive banking market within the AA. We analyzed the bank's quarterly LTD ratio from March 1999 to December 2003. During this period, the LTD ratio averaged 57%, with a low of 41% and a high of 64%.

We compared the bank's LTD ratio with that of peer banks operating in Palm Desert National Bank's AA and other areas within the Riverside-San Bernardino MA that have similar demographics and asset size. This peer group consists of four financial institutions, ranging in total asset size from \$127 million to \$254 million. Palm Desert National Bank's asset size was inflated as of December 31, 2003, because \$146 million of the bank's \$296 million total assets funded the ATM operations.

The bank's LTD ratio does not compare favorably to the peer average. The four-bank peer group's average quarterly LTD ratio was 72%, compared to 57% for Palm Desert National Bank. However, 27% of the bank's deposits are brokered deposits, which are used to help fund growth in its ATM operations. Consequently, the bank could not originate more loans without obtaining more deposits (e.g. the LTD ratio is skewed by the brokered deposits and would not necessarily increase if the bank originated more loans). Management is investigating funding sources outside of brokered deposits for the ATM operations. If we exclude brokered deposits from the bank's LTD ratio, the bank compares reasonably well to peer. Considering the negative impact of the brokered deposits on the LTD ratio, the bank's LTD ratio is considered reasonable and meets the standard for satisfactory performance.

### **LENDING IN THE ASSESSMENT AREA**

A majority of loans and other lending-related activities occur in the bank's assessment area.

Analysis for lending in the AA included a sample of 40 commercial and industrial loans originated from January 1, 1999 through December 31, 2003. The bank originated 90% of loans (by number) and 77% (by dollar volume) within the AA. To meet the standard in this performance criterion, the bank needs to originate at least 50% of its loans within its AA. Consequently, the bank's lending to businesses within the assessment area meets the standard for satisfactory performance.

## LENDING TO BUSINESSES OF DIFFERENT SIZES

Given the demographics of the AA, the bank's distribution of loans reflects reasonable penetration among businesses of different sizes.

We used the same random loan sample described in the prior section to evaluate the bank's performance. We selected the commercial loan product for review because the bank is primarily a commercial lender.

We compared the bank's lending to businesses in the AA to the demographics of small businesses of the assessment area. Small businesses are those with gross revenues of up to \$1 million.

Table 2 displays the bank's lending practices based on our sample of 1999 through 2002 business borrowers.

Table 2

<b>Income Distribution –Loans to Businesses Loans Originated Between 1999 and 2002 Riverside-San Bernardino MA</b>		
<b>Business Revenues (or Sales)</b>	<b>≤\$1,000,000</b>	<b>&gt;\$1,000,000</b>
<b>% of AA Businesses*</b>	<b>69%</b>	<b>5%</b>
% of Bank Loans in AA by #	60%	40%
% of Bank Loans in AA by \$	41%	59%

*\* Demographic Data Source: 2002 Dun & Bradstreet, 26% of AA businesses did not report revenue data*

Table 2 shows 60% of the number of the bank's business borrowers in 2001 and 2002 generated gross annual revenues of \$1 million or less. This compares reasonably to 2002 Dun & Bradstreet data that shows 69% of reporting businesses had gross annual revenues of \$1 million or less. When we look at small business penetration based on the dollar amount of the loan, the bank is below the demographics. However, for this examination, we placed greater emphasis on the number of loans rather than the dollar volume, because large businesses tend to borrow larger amounts of money.

The following table displays the bank’s lending practices based on our sample of 2003 business borrowers.

Table 3

<b>Income Distribution - Loans to Businesses Loans Originated During 2003 Riverside-San Bernardino MA</b>		
<b>Business Revenues (or Sales)</b>	<b>≤\$1,000,000</b>	<b>&gt;\$1,000,000</b>
<b>% of AA Businesses*</b>	<b>64%</b>	<b>5%</b>
% of Bank Loans in AA by #	45%	55%
% of Bank Loans in AA by \$	22%	78%

*\*Demographic Data Source: 2003 Dun & Bradstreet, 31% of AA businesses did not report revenue data*

Table 3 shows 45% of the bank’s 2003 commercial originations (by number of loans) were to borrowers with gross annual revenues of \$1 million or less. This is below the Dun & Bradstreet data, which show 64% of reporting businesses had gross annual revenues of \$1 million or less.

To mitigate poor penetration to small businesses in the AA, the bank is involved in several small business lending programs. The bank originated one loan totaling \$363 thousand through a loan participation with the Inland Empire Small Business Financial Development Corporation. This program allows a business to obtain a loan for which it would not ordinarily qualify, and also to establish a favorable credit history.

The bank participates in the SBA and State of California Loan Guarantee Programs. The SBA program enables the bank to assist small business owners with acquisition and/or expansion of their business, purchase of equipment, leasehold improvements, and other business-related purposes. This program benefits persons interested in starting a new business. During the evaluation period, the bank originated six SBA loans, totaling \$1.5 million. The State of California program is similar to the SBA program, but it has lower maximum loan amounts and may provide guarantees up to 90% of the loan amount (which is higher than that provided by the SBA). The bank originated one loan totaling \$735 thousand with the State of California program during the evaluation period.

The bank also participates in a lending program in conjunction with the Bureau of Indian Affairs. This unique program provides loan guarantees up to 90% of the loan amount for loans granted to individual Native Americans, Tribes, or Tribal Corporations. Loan proceeds must be used to start or expand a non-gaming related business on or off the reservation. Allowable loan purposes include acquisition or construction of income-generating real estate, business acquisition or start-up, or other projects designed to promote economic development and self-reliance for Native Americans. During the evaluation period, the bank originated six loans totaling \$10.9 million.

Based on the factors above, bank lending to businesses of different sizes meets the standard for satisfactory performance.



## GEOGRAPHIC DISTRIBUTION OF LOANS

The geographic distribution of loans throughout the assessment area does not meet the standard for satisfactory performance.

We reviewed the pattern for geographic distribution of lending between LMI tracts within the assessment area. Table 4 below details the bank's commercial lending activity within the AA. We used the same sample of commercial loans from the **Lending to Businesses of Different Sizes** section of this Performance Evaluation.

Table 4

Geographic Distribution - Loans to Businesses Loans Originated Between 1999 and 2003 Riverside-San Bernardino MA								
Census Tract Income Level*	Low		Moderate		Middle		Upper	
	% of Number of Loans	% of AA Businesses	% of Number of Loans	% of AA Businesses	% of Number of Loans	% of AA Businesses	% of Number of Loans	% of AA Businesses
1999 - 2002 Sample	5%	1%	10%	25%	45%	41%	40%	43%
2003 Sample	0%	1%	15%	28%	50%	44%	35%	28%

*\*Demographic Data Source: 2002 & 2003 Dun & Bradstreet*

Table 4 above reflects excellent penetration in the low-income census tract based on the 1999-2002 loan sample, but in the 2003 loan sample there were no loans originated in low-income census tracts. However, this appears reasonable since only one percent of the businesses are located in low-income census tracts.

For this performance criterion, more emphasis is placed on the bank's lending to businesses located in moderate-income census tracts, because that is where a majority of the businesses are located. The sample indicated that lending to businesses in moderate-income tracts is below the demographics of the area (10% compared to 25%, and 15% compared to 28%). We did note that lending to businesses located in moderate-income tracts has improved since the last examination, but the overall performance is below the demographics of the AA. Management could not provide a specific answer to address the poor penetration. Going forward, management has committed to expand lending efforts in LMI housing projects located in moderate-income areas to mitigate poor penetration. Affordable housing is an identified need based on our community contact. However, for this evaluation period, the bank does not meet the standard for satisfactory performance.

## **RESPONSE TO COMPLAINTS**

Palm Desert National Bank has not received any written complaints associated with its performance under the Community Reinvestment Act.

## **FAIR LENDING OR OTHER ILLEGAL CREDIT PRACTICES REVIEW**

We found no evidence of illegal discrimination or other illegal credit practices.