



**SMALL BANK**

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Comptroller of the Currency  
Administrator of National Banks

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Washington, DC 20219

## **PUBLIC DISCLOSURE**

**October 28, 2009**

### **COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION**

The Farmers and Merchants National Bank of Hatton  
Charter Number 7905

415 7th Street  
Hatton, ND 58240

Office of the Comptroller of the Currency

Minneapolis Field Office  
222 South Ninth Street, Suite 800  
Minneapolis, MN. 55402-3393

**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 bank has reasonable distribution of credit among business and agricultural borrowers of different sizes and households of different income levels.
- The bank's average loan to deposit ratio is reasonable.
- A majority of bank loans were originated within the bank's assessment area.
- The bank did not receive any CRA related complaints during this evaluation period.

**SCOPE OF EXAMINATION**

We assessed Farmers and Merchants National Bank of Hatton's (FMNB) record of meeting the credit needs of the community, consistent with the provisions set forth in the Community Reinvestment Act (CRA).

In order to determine the bank's lending performance, we selected primary products based on loan originations for the period beginning January 1, 2007 and ending June 30, 2009. Our examination focused on the bank's two assessment areas (AA), Hatton and Fargo. We determined that agricultural (65% by dollar) and consumer (57% by number) loans are the primary products for the Hatton AA and agricultural (46% by dollar) and commercial (36% by dollar) loans are the primary products for the Fargo AA. We selected a random sample of 20 loans from each of the primary products in order to conduct our analysis.

**DESCRIPTION OF INSTITUTION**

FMNB is a \$34 million bank chartered in Hatton, ND. The bank is wholly owned by Hatton Bancshares, Inc., a one bank holding company headquartered in Fargo, ND. FMNB has two full service locations. The main office is located in Hatton, ND in eastern North Dakota. The Fargo branch is located approximately 75 miles southeast of FMNB Hatton in the Fargo ND-MN Metropolitan Statistical Area (MSA). This branch was opened February 19, 2008. The bank does not have any automatic teller machines.

FMNB offers a variety of banking products designed to meet the needs of the AA. As of June 30, 2009, the bank's \$26 million loan portfolio consisted of 31% real estate loans, 31% agricultural loans, 29% commercial loans and 9% consumer loans. Net loans equal 76% of total assets.

There are no legal, financial or other factors that impede FMNB's ability to help meet the credit needs in the AA. At their last CRA examination, dated October 27, 2003, the bank received a Satisfactory rating.

## **DESCRIPTION OF ASSESSMENT AREA(S)**

FMNB's AA's comply with regulatory requirements. These areas do not arbitrarily exclude any low- or moderate-income census tracts (CT).

### ***Hatton, ND AA***

The Hatton AA includes all of Steele County and a portion of Traill County in eastern North Dakota. This area has three CT, all classified as middle-income. There are no low- moderate-, or upper- income CT in the AA.

The population of the area declined at a rate of 6% from 2000 to 2009, according to 2009 geodemographic data. The area consists of 1,838 families. Nearly 13% are low-income, 14% moderate-income and over 10% of households live below the poverty level. According to the Department of Housing and Urban Development, the median family income was \$55,100 in 2009.

The services industry is the area's leader in employment and provides 32% of total jobs. Agriculture provides the second most employment opportunities at 17% of total jobs. Unemployment is usually higher in the winter months but averages just over 4%.

Competition in the AA is moderate. There are seven similarly situated financial institutions in the AA with total assets ranging from \$21 million to \$51 million. FMNB holds 10% of the market share.

During our evaluation, we contacted a local community organization to better understand the demographics and to determine the primary credit needs of the AA. Primary credit needs identified by the contact include small business lending and consumer loans.

### ***Fargo, ND AA***

The Fargo AA includes all CT in Cass County. This is located in the Fargo ND-MN MSA. The AA includes 4 moderate-, 19 middle- and 4 upper-income CT. No Minnesota CT are a part of the bank's AA due to the location of the branch and it's proximity to these tracts.

The population of the area increased by 15% from 2000 to 2009, according to 2009 geodemographic data. The area consists of 34,289 families. Of these families, 16% are low-income, 17% are moderate-income, 29% are middle-income and 38% are upper-income. According to the Department of Housing and Urban Development, the median family income is \$68,200 in 2009.

The major employment sector for the area is the service industry which provides 47% of the jobs in the area. Retail trade provides the second most employment opportunities at 11% of total jobs. According to the Bureau of Labor statistics the unemployment rate for Cass County is 4%, as of August 2009, which is below the national average of 9.8%.

Competition in the AA is strong. There are six similarly situated financial institutions in the area. State Bank and Trust, Wells Fargo and US Bank comprise more than 50% of the market share for the area, increasing competition among the smaller community banks. FMNB holds only 0.2% of the market share.

During our evaluation, we contacted a local community organization to better understand the AA demographics and to determine the primary credit needs of the AA. Primary credit needs identified by the contact were small business/farm lending.

## CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

### Loan-to-Deposit (LTD) Ratio

The bank's LTD ratio is reasonable based on its financial capacity and lending opportunities. The quarterly LTD ratio averaged 73% in the 26 calendar quarters from June 30, 2003 to June 30, 2009.

LOAN-TO-DEPOSIT RATIO		
Institution	Assets 6/30/09	Average Ratio
Union State Bank of Fargo	\$51 Million	100%
The First and Farmers Bank	\$46 Million	87%
First State Bank of Sharon	\$41 Million	78%
<b><i>Farmers and Merchants National Bank of Hatton</i></b>	<b><i>\$34 Million</i></b>	<b><i>73%</i></b>
Harwood State Bank	\$29 Million	61%
Kindred State Bank	\$21 Million	51%

FMNB's LTD compares reasonably to other community banks of similar size in the AA. The average LTD ratio for the five similarly situated banks is 75%.

### Lending in the AA

FMNB's record of lending within its AA is reasonable. The majority of the loans originated during the evaluation period are located in one of the bank's two AAs. The table on the following page shows the results of our analysis.

Lending in FMNB's AAs										
LOAN TYPE	Number of loans					Dollars of Loans				
	Inside AA		Outside AA		Total #	Inside AA		Outside AA		Total \$ (000s)
	#	%	#	%		\$ (000s)	%	\$ (000s)	%	
Farm	31	78%	9	22%	40	\$3,478	81%	\$830	19%	\$4,308
Commercial	14	70%	6	30%	20	\$2,133	73%	\$773	27%	\$2,906
Consumer	13	65%	7	35%	20	\$226	60%	\$149	40%	\$375
<b>Total reviewed</b>	<b>58</b>	<b>73%</b>	<b>22</b>	<b>27%</b>	<b>80</b>	<b>\$5,837</b>	<b>77%</b>	<b>\$1,751</b>	<b>23%</b>	<b>\$7,589</b>

\*Source: loan sample

## Lending to Borrowers of Different Incomes and to Farms of Different Sizes

The distribution of borrowers reflects reasonable penetration among businesses and farms of different sizes and excellent penetration among individuals of different income levels.

### Hatton AA

#### Farm Loans

FMNB's lending to farms with different revenue levels is reasonable. Based on our sample, FNB originated 74% by dollar and 95% by number to farms with gross revenues of \$1 million or less. The following table illustrates this distribution.

Income Distribution of Farm Loans			
Farm Revenues	≤1,000,000	>1,000,000	Unknown
% of AA Farms	98%	1%	1%
% of Bank Loans in AA by #	95%	5%	5%
% of Bank Loans in AA by \$	74%	24%	1%

\*Source: loan sample and 2009 geo demographic data

#### Consumer Loans

The bank's distribution of consumer loans among borrowers of different income levels is excellent. Based on our sample of 20 consumer loans, lending to both low- and moderate-income households exceeds demographic information.

Borrower Distribution of Consumer Loans								
Borrower Income Level	Low		Moderate		Middle		Upper	
	% of AA Households	% of Number of Loans	% of AA Households	% of Number of Loans	% of AA Households	% of Number of Loans	% of AA Households	% of Number of Loans
Consumer Loans	19%	39%	15%	18%	20%	36%	46%	7%

Source: Loan sample; 2000 U.S. Census data.

## Lending to Businesses and Farms of Different Sizes

### Fargo AA

#### Commercial Loans

FMNB's lending to small businesses is reasonable. The following chart shows FMNB's lending compared to demographics.

Income Distribution of Commercial Loans			
Business Revenues	≤1,000,000	>1,000,000	Unknown
% of AA Businesses	73%	6%	21%
% of Bank Loans in AA by #	70%	20%	10%
% of Bank Loans in AA by \$	95%	4%	1%

\*Source: loan sample and 2009 geo demographic data

#### Farm Loans

Lending to small farms in the AA is less than reasonable. The following chart shows FMNB's lending compared to demographics.

Income Distribution of Farm Loans			
Farm Revenues	≤1,000,000	>1,000,000	Unknown
% of AA Farms	97%	2%	1%
% of Bank Loans in AA by #	85%	10%	5%
% of Bank Loans in AA by \$	85%	11%	4%

\*Source: loan sample and 2009 geo demographic data

## Geographic Distribution of Loans

### Hatton AA

Geographic distribution analysis is not meaningful as only middle-income CTs are located within the AA.

### Fargo AA

Dispersion of loans to businesses and farms across different CTs displays reasonable dispersion.

#### Commercial Loans

FMNB's lending to businesses located in moderate-income CTs is reasonable. The following chart shows FMNB's lending compared to demographics. Demographic data indicates 29% of businesses in the AA are located in moderate-income CTs.

Geographic Distribution of Loans to Businesses in the Fargo MSA								
Census Tract Income Level	Low		Moderate		Middle		Upper	
Loan Type	% of AA Businesses	% 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
Business	0%	0%	29%	20%	52%	25%	18%	55%

\*Source: loan sample and 2009 geo demographic data

**Farm Loans**

Lending to farms located in moderate-income CT’s demonstrates poor dispersion. The following chart shows FMNB’s lending compared to demographics. Demographic data indicates only 8% (or 52) of farms in the AA are located in moderate-income CTs. These tracts are centrally located within the city of Fargo and contain hospitals and other businesses. The few farms located in those tracts are established and had relationships with other financial institutions before FMNB opened the Fargo branch.

Geographic Distribution of Loans to Farms in the Fargo MSA								
Census Tract Income Level	Low		Moderate		Middle		Upper	
Loan Type	% of AA Businesses	% 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
Business	0%	0%	8%	0%	78%	85%	14%	15%

\*Source: loan sample and 2009 geo demographic data

**Responses to Complaints**

FMNB has not received any CRA related complaints since the last CRA evaluation.

**Fair Lending or Other Illegal Credit Practices Review**

We found no evidence of discriminatory or other illegal credit practices inconsistent with helping to meet community credit needs.