



Office of the  
Comptroller of the Currency  
Washington, DC 20219

# INTERMEDIATE SMALL BANK

## PUBLIC DISCLOSURE

July 09, 2018

### COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

The Karnes County National Bank of Karnes City  
Charter Number 5614

301 E. Calvert Street, Karnes City, TX 78118

Office of the Comptroller of the Currency  
10001 Reunion Place, Suite 250  
San Antonio, TX 78216

**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, and should not 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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## **Overall CRA Rating: SATISFACTORY**

**The Lending Test is rated: SATISFACTORY**

**The Community Development Test is rated: SATISFACTORY**

The bank has a satisfactory record of meeting community credit needs. The rating is based on the following findings:

- The bank's quarterly average loan-to-deposit (LTD) ratio is reasonable given the bank's size, financial condition, and credit needs in the assessment areas (AAs).
- Although the bank originated a substantial majority of loans outside of its AA by dollar volume, it is satisfactory after consideration of performance context factors.
- The distribution of loans reflects reasonable penetration to borrowers of different income levels and to businesses of different sizes.
- The geographic distribution of loans reflects reasonable dispersion.
- Community development (CD) performance demonstrates adequate responsiveness to CD needs in the AAs.

## Definitions and Common Abbreviations

The following terms and abbreviations are used throughout this performance evaluation, including the CRA tables. The definitions are intended to provide the reader with a general understanding of the terms, not a strict legal definition.

**Affiliate:** Any company that controls, is controlled by, or is under common control with another company. A company is under common control with another company if the same company directly or indirectly controls both companies. A bank subsidiary is controlled by the bank and is, therefore, an affiliate.

**Aggregate Lending:** The number of loans originated and purchased by all reporting lenders in specified income categories as a percentage of the aggregate number of loans originated and purchased by all reporting lenders in the MA/assessment area.

**Census Tract (CT):** A small subdivision of metropolitan and other densely populated counties. Census tract boundaries do not cross county lines; however, they may cross the boundaries of metropolitan areas. Census tracts generally have a population between 1,200 and 8,000 people, with an optimal size of 4,000 people. Their physical size varies widely depending upon population density. Census tracts are designed to be homogeneous with respect to population characteristics, economic status, and living conditions to allow for statistical comparisons.

**Community Development:** Affordable housing (including multifamily rental housing) for low- or moderate-income individuals; community services targeted to low- or moderate-income individuals; activities that promote economic development by financing businesses or farms that meet Small Business Administration Development Company or Small Business Investment Company programs size eligibility standards or have gross annual revenues of \$1 million or less; activities that revitalize or stabilize low- or moderate-income geographies, distressed or underserved nonmetropolitan middle-income geographies, or designated disaster areas; or loans, investments, and services that support, enable or facilitate projects or activities under HUD Neighborhood Stabilization Program criteria that benefit low-, moderate-, and middle-income individuals and geographies in the bank's assessment area(s) or outside the assessment area(s) provided the bank has adequately addressed the community development needs of its assessment area(s).

**Community Reinvestment Act (CRA):** the statute that requires the OCC to evaluate a bank's record of meeting the credit needs of its local community, consistent with the safe and sound operation of the bank, and to take this record into account when evaluating certain corporate applications filed by the bank.

**Consumer Loan(s):** A loan(s) to one or more individuals for household, family, or other personal expenditures. A consumer loan does not include a home mortgage, small business, or small farm loan. This definition includes the following categories: motor vehicle loans, credit card loans, home equity loans, other secured consumer loans, and other unsecured consumer loans.

**Family:** Includes a householder and one or more other persons living in the same household who are related to the householder by birth, marriage, or adoption. The number of family households always equals the number of families; however, a family household may also include non-relatives living with the family. Families are classified by type as either a married-couple family or other family, which is further classified into 'male householder' (a family with a male householder' and no wife present) or 'female householder' (a family with a female householder and no husband present).

**Full Review:** Performance under the Lending, Investment, and Service Tests is analyzed considering performance context, quantitative factors (e.g., geographic distribution, borrower distribution, and total number and dollar amount of investments), and qualitative factors (e.g., innovativeness, complexity, and responsiveness).

**Geography:** A census tract delineated by the United States Bureau of the Census in the most recent decennial census.

**Home Mortgage Disclosure Act (HMDA):** The statute that requires certain mortgage lenders that conduct business or have banking offices in a metropolitan statistical area to file annual summary reports of their mortgage lending activity. The reports include such data as the race, gender, and the income of applicants, the amount of loan requested, the disposition of the application (e.g., approved, denied, and withdrawn, loan pricing, the lien status of the collateral, any requests for preapproval, and loans for manufactured housing.

**Home Mortgage Loans:** Such loans include home purchase, home improvement, and refinancings, as defined in the HMDA regulation. These include loans for multifamily (five or more families) dwellings, manufactured housing and one-to-four family dwellings other than manufactured housing.

**Household:** Includes all persons occupying a housing unit. Persons not living in households are classified as living in group quarters. In 100 percent tabulations, the count of households always equals the count of occupied housing units.

**Limited Review:** Performance under the Lending, Investment, and Service Tests is analyzed using only quantitative factors (e.g., geographic distribution, borrower distribution, total number and dollar amount of investments, and branch distribution).

**Low-Income:** Individual income that is less than 50 percent of the area median income, or a median family income that is less than 50 percent, in the case of a geography.

**Market Share:** The number of loans originated and purchased by the institution as a percentage of the aggregate number of loans originated and purchased by all reporting lenders in the MA/assessment area.

**Median Family Income (MFI):** The median income determined by the U.S. Census Bureau every five years and used to determine the income level category of geographies. Also, the median income determined by the Federal Financial Institutions Examination Council (FFIEC) annually that is used to determine the income level category of individuals. For any given area, the median is the point at which half of the families have income above it and half below it.

**Metropolitan Area (MA):** Any metropolitan statistical area or metropolitan division, as defined by the Office of Management and Budget, and any other area designated as such by the appropriate federal financial supervisory agency.

**Metropolitan Division:** As defined by Office of Management and Budget, a county or group of counties within a Core Based Statistical Area that contains an urbanized population of at least 2.5 million. A Metropolitan Division consists of one or more main/secondary counties that represent an employment center or centers, plus adjacent counties associated with the main/secondary county or counties through commuting ties.

**Metropolitan Statistical Area:** An area, defined by the Office of Management and Budget, as a core based statistical area associated with at least one urbanized area that has a population of at least 50,000. The Metropolitan Statistical Area comprises the central county or counties containing the core, plus adjacent outlying counties having a high degree of social and economic integration with the central county or counties as measured through commuting.

**Middle-Income:** Individual income that is at least 80 percent and less than 120 percent of the area median income, or a median family income that is at least 80 percent and less than 120 percent, in the case of a geography

**Moderate-Income:** Individual income that is at least 50 percent and less than 80 percent of the area median income, or a median family income that is at least 50 percent and less than 80 percent, in the case of a geography.

**Multifamily:** Refers to a residential structure that contains five or more units.

**Other Products:** Includes any unreported optional category of loans for which the institution collects and maintains data for consideration during a CRA examination. Examples of such activity include consumer loans and other loan data an institution may provide concerning its lending performance.

**Owner-Occupied Units:** Includes units occupied by the owner or co-owner, even if the unit has not been fully paid for or is mortgaged.

**Qualified Investment:** A qualified investment is defined as any lawful investment, deposit, membership share, or grant that has as its primary purpose community development.

**Rated Area:** A rated area is a state or multi-state metropolitan area. For an institution with domestic branches in only one state, the institution's CRA rating would be the state rating. If an institution maintains domestic branches in more than one state, the institution will receive a rating for each state in which those branches are located. If an institution maintains domestic branches in two or more states within a multi-state metropolitan area, the institution will receive a rating for the multi-state metropolitan area.

**Small Loan(s) to Business(es):** A loan included in 'loans to small businesses' as defined in the Consolidated Report of Condition and Income (Call Report) instructions. These loans have original amounts of \$1 million or less and typically are either secured by nonfarm or nonresidential real estate or are classified as commercial and industrial loans.

**Small Loan(s) to Farm(s):** A loan included in 'loans to small farms' as defined in the instructions for preparation of the Consolidated Report of Condition and Income (Call Report). These loans have original amounts of \$500,000 or less and are either secured by farmland, or are classified as loans to finance agricultural production and other loans to farmers.

**Tier One Capital:** The total of common shareholders' equity, perpetual preferred shareholders' equity with non-cumulative dividends, retained earnings and minority interests in the equity accounts of consolidated subsidiaries.

**Upper-Income:** Individual income that is at least 120 percent of the area median income, or a median family income that is at least 120 percent, in the case of a geography.

## Description of Institution

The Karnes County National Bank of Karnes City (KCNB) is a single state community bank headquartered in Karnes City, Texas. The bank was chartered in 1900 and does not have a holding company. As of March 31, 2018, the bank reported total assets of \$385 million, total capital of \$31 million, and a tier one capital leverage ratio of 10 percent.

The bank's only AA consists of the entirety of Karnes County. KCNB has two offices, both located in Karnes County, Texas. The main branch is located in Karnes City, and the second branch is located five miles away in Kenedy, Texas. Both locations have a walk-in lobby with tellers and loan officers, a drive-through motor bank, and an automated teller machine (ATM). There has been no new locations, closed locations, or merger and acquisition activity since the last CRA examination.

KCNB offers traditional residential and commercial banking products and services, and online banking through [www.kcnb.com](http://www.kcnb.com). Online capabilities include checking account statements, transactions within the institution, and bill pay. The bank's strategy is to continue offering its traditional products and services and projects modest growth. KCNB's competition comes primarily from regional banks making large commercial loans, and a national bank that is also located in the AA.

As of March 31, 2018, net loans totaled \$64 million and represented 17 percent of total assets and 18 percent of total deposits. The following table summarizes the loan portfolio's composition.

Loan Portfolio Composition as of March 31, 2018		
Loan Type	Volume (\$000s)	% of Total Loan Portfolio
Residential Real Estate Loans	\$21,968	33%
Commercial Loans	\$29,671	45%
Consumer Installment Loans	\$4,508	7%
Agricultural Loans	\$10,053	15%
<i>Total</i>	<i>\$66,100</i>	<i>100%</i>

Source: March 31, 2018 Call Report

The bank's AA which consists of KCNB faces a unique economic situation. The area the bank resides in is heavily reliant on oil and gas activity from the Eagle Ford Shale formation. As oil and gas activity has increased, bank deposits have also increased as bank customers receive royalty checks that they then deposit into the bank. Likewise, as oil and gas activity increases, loan volume generally declines as customers begin to pay off their loans more quickly and demand for new loans weakens. These local market factors suppress the bank's LTD ratio and limit opportunities to provide credit to its AA.

There are no legal, financial or other factors impeding the bank's ability to meet the credit needs in its AA. The bank received a CRA rating of **SATISFACTORY** at its last CRA evaluation, dated July 13, 2015.



# Scope of the Evaluation

## Evaluation Period/Products Evaluated

The Performance Evaluation assesses the bank’s performance using intermediate small bank (ISB) CRA procedures, which include the lending and CD tests. The lending test evaluates the bank’s record of meeting the credit needs of its AA through primary lending activities. The CD test evaluates the bank’s responsiveness to identified CD needs in its AA through its qualified CD lending, investments, and services.

The evaluation period for this CRA examination is from July 13, 2015 (the date of the last examination) through December 31, 2017. Examiners performed separate analyses on the 2015-2016 data and the 2017 data, due to changes in census data.

The table below shows the breakdown of all loans originated or purchased by KCNB over the evaluation period. As shown, the primary product by dollar volume was commercial real estate (CRE) and the primary product by loan number was consumer loans. A sample of 20 loans for both of these types was tested for the bank’s only AA.

Loan Originations and Purchases By Loan Type During the Evaluation Period				
Loan Type	Dollar of Loans	% of Total Dollar	Number of Loans	% of Total Number
Commercial Real Estate	11,935	30%	26	3%
Residential Real Estate	6,772	17%	42	4%
Agricultural	4,808	12%	43	4%
Commercial & Industrial	8,284	21%	91	9%
Consumer	7,861	20%	829	80%
<i>Total</i>	<i>39,660</i>	<i>100%</i>	<i>1,031</i>	<i>100%</i>

Source: Internal Bank Reports

## Data Integrity

The bank is not a HMDA data reporter, therefore, full-scope data integrity procedures were not performed. Data integrity was validated through analysis of the loan files as part of the lending test. Examiners also reviewed community development loans, investments, and services submitted by management to determine if they qualified to meet the regulatory definition for community development. There were no data integrity issues identified during the CRA evaluation.

## Selection of Areas for Full-Scope Review

The OCC completed a full-scope review of the Karnes County Non-MSA AA as it is the bank’s only AA as it contributes to all bank activity. KCNB’s only AA is not located in an MSA and is comprised of the entirety of Karnes County including all census tracts. The AA meets regulatory requirements, as it consists of a whole geography and does not reflect any illegal or suspicious discrimination or gerrymandering. Refer to **Appendix A: Scope of Examination** for additional details.

## **Ratings**

The bank's overall rating is based upon the full scope review of its AA. Both identified primary products (CRE and consumer) were given equal weight in determining the lending test rating.

## **Discriminatory or Other Illegal Credit Practices Review**

Pursuant to 12 CFR 25.28(c) or 195.28(c), respectively, in determining a national bank's or federal savings association's (collectively, bank) CRA rating, the OCC considers evidence of discriminatory or other illegal credit practices in any geography by the bank, or in any assessment area by an affiliate whose loans have been considered as part of the bank's lending performance. As part of this evaluation process, the OCC consults with other federal agencies with responsibility for compliance with the relevant laws and regulations, including the U.S. Department of Justice, the U.S. Department of Housing and Urban Development, and the Consumer Financial Protection Bureau, as applicable.

The OCC has not identified that this institution has engaged in discriminatory or other illegal credit practices that require consideration in this evaluation.

The OCC will consider any information that this institution engaged in discriminatory or other illegal credit practices, identified by or provided to the OCC before the end of the institution's next performance evaluation in that subsequent evaluation, even if the information concerns activities that occurred during the evaluation period addressed in this performance evaluation.

## Conclusions with Respect to Performance Tests

KCNB achieved **SATISFACTORY** performance under the lending test and **SATISFACTORY** performance under the CD test. There were no discriminatory lending practices identified during the evaluation period.

### LENDING TEST

KCNB's performance under the lending test is **SATISFACTORY** and management has been successful in meeting the credit needs of its AAs. KCNB has demonstrated satisfactory performance based on its reasonable average quarterly LTD ratio, reasonable lending penetration to borrowers of various income levels and businesses of different sizes, and reasonable lending dispersion to low- and moderate-income geographies.

### Loan-to-Deposit Ratio

The bank's quarterly average LTD is reasonable and reflects satisfactory performance given the bank's capacity to lend, market competition, local demographics, economic factors, and lending opportunities available in the AA. KCNB's quarterly average LTD since the last CRA evaluation was 27 percent, and has been steadily decreasing every quarter in the past year in correlation with the increase in deposits and decrease in loans. It was 18 percent as of March 31, 2018. Despite the declining trend, the bank's LTD is reasonable after consideration of performance context factors. The most impactful factor is the influx of deposits due to oil and gas activity from the Eagle Ford Shale play. The county's economy is largely dependent on oil and gas activity. Many customers of the bank that live in the area receive significant royalty checks, which increase bank deposits and decrease loan demand. Of the comparable banks in the surrounding area, the only ones with significantly better LTDs are the two banks with significant footprints outside of the area. These banks are Southtrust and Beeville, which have locations in Houston, Corpus Christi, and New Braunfels. The institutions with comparable footprints centered in the local market have similar LTDs to KCNB.

Loan to Deposit Ratio					
BANK NAME	CITY	STATE	COUNTY	TOTAL ASSETS (000s)	Avg. LTD Ratio
The Karnes County National Bank of Karnes City	Karnes City	TX	Karnes County	385,054	<b>27.25</b>
The Falls City National Bank	Falls City	TX	Karnes County	384,489	36.97
The First National Bank of Beeville	Beeville	TX	Bee County	393,762	76.85
Southtrust Bank, National Association	George West	TX	Live Oak County	361,200	78.59
Atascosa Bank	Atascosa	TX	Atascosa County	91,564	15.97
Dilley State Bank	Dilley	TX	Frio County	128,123	14.50

Source Data: Call Reports from 6/30/2015 to 3/31/2018

## Lending in Assessment Area

Lending in the AA is satisfactory. KCNB originated a majority of loans inside its AA by number, but a substantial majority outside its AA by dollar volume. 53 percent of loans were originated inside the bank's AA by number, but only 7 percent were originated inside the AA by dollar volume. The aggregate dollar volume was heavily influenced by CRE loans, whose larger size muted the impact of 67 percent of consumer loans being originated within the AA. Examiners reviewed all of the bank's CRE denials since January 2016, which is the farthest back that they keep denial records. Examiners found that the bank had zero CRE denials in their AA during this time period. Despite the percentage of loan originations within the AA by dollar volume, lending in the AA is satisfactory after consideration of the local economy's suppression of loan demand, the absence of CRE loan denials the bank has had in its AA, and the majority of consumer loans by dollar and number having originated in the AA.

Table D - Lending Inside and Outside of the Karnes County Assessment Area										
Loan Category	Number of Loans					Dollar Amount of Loans (000s)				
	Inside		Outside		Total	Inside		Outside		Total
	#	%	#	%	#	\$	%	\$	%	(000s)
Commercial RE	8	33%	16	67%	24	\$505	5%	\$9,773	95%	\$10,278
Consumer	26	65%	14	35%	40	\$229	67%	\$114	33%	\$343
Totals	<b>34</b>	<b>53%</b>	30	47%	<b>64</b>	<b>\$734</b>	<b>7%</b>	\$9,887	93%	\$10,621

Source: Internal bank reports; Due to rounding, totals may not equal 100

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

The bank's distribution of loans to borrowers of different income levels and businesses of different sizes reflects reasonable penetration and meets the standards for satisfactory performance.

### Commercial Loans

The bank's borrower distribution for loans to businesses within its AA exceeds standards and reflects excellent penetration to small businesses, defined as businesses with gross annual revenues of \$1 million or less. All eight CRE loans that were originated in the AA during the evaluation period were to small businesses. The bank's lending to small business exceeded aggregate data of CRA reporting institutions who on average extended 41 percent of their commercial loans in the AA to small businesses. The following tables show the distribution of CRE loans among different sized businesses in the AA.

Borrower Distribution of Loans to Businesses in the Karnes County AA – 2015/16				
Business Revenues (or Sales)	≤\$1,000,000	>\$1,000,000	Unavailable/ Unknown	Total
% of AA Businesses	<b>79%</b>	3%	18%	100%
% of Bank Loans in AA by #	<b>100%</b>	0%	0%	100%
% of Bank Loans in AA by \$	<b>100%</b>	0%	0%	100%

Source: Loan sample; Dunn and Bradstreet Data

**Borrower Distribution of Loans to Businesses in the Karnes County AA - 2017**

**No meaningful analysis – only one CRE loan in AA in 2017 (loan was to a business with less than \$1MM in gross revenue)**

*Consumer Loans*

The bank’s borrower distribution for consumer lending within its AA meets standards and reflects reasonable penetration for borrowers of different income levels. The results show that the bank’s consumer lending practices are in line with AA borrower income statistics for LMI families. The following tables show the distribution of consumer loans to borrowers of different income levels compared to the percent of families in each income category.

<b>Lending to Borrowers of Different Income Levels in Karnes County Non-MSA AA – 2015/16</b>								
Borrower Income Level	<b>Low</b>		<b>Moderate</b>		Middle		Upper	
Loan type	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans
Consumer	25%	<b>25%</b>	17%	<b>17%</b>	17%	25%	41%	25%

*Source: 2010 U.S Census; loan sample*

*% of loans do not total 100% as one consumer loan (8% of sample) had an unknown borrower income amount*

<b>Lending to Borrowers of Different Income Levels in Karnes County Non-MSA AA - 2017</b>								
Borrower Income Level	<b>Low</b>		<b>Moderate</b>		Middle		Upper	
Loan type	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans	% of AA Families	% of Number of Loans
Consumer	24%	<b>21%</b>	14%	<b>29%</b>	16%	36%	47%	14%

*Source: 2015 ACS Census; loan sample*

**Geographic Distribution of Loans**

The geographic distribution of the bank’s loans in its AA is outstanding and reflects excellent dispersion. While the bank’s actual distribution to LMI tracts reflects satisfactory performance (excellent commercial dispersion and poor consumer dispersion), the bank’s performance is outstanding when considering that 17 of the 19 loans (89 percent) originated in the bank’s AA in 2015 and 2016 were in a distressed or underserved census tract. Due to a change in census data, there were no LMI tracts for 2017, but 13 of 15 of the loans (87 percent) originated in the bank’s AA during this time period were in a distressed or underserved tract.

*Commercial Loans*

The bank’s geographic distribution for CRE loans exceeds standards and represents excellent dispersion to distressed or underserved tracts. Six of the seven CRE loans originated within the AA in 2015 and 2016 were located in a distressed or underserved tract. The following tables show the distribution of CRE loans among different sized businesses within its AA.

Geographic Distribution of Loans Businesses in Karnes County – 2015/16								
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
Commercial RE	<b>0%</b>	0%	<b>7%</b>	14%	<b>77%</b>	86%	<b>16%</b>	0%

Source: 2016 Dunn & Bradstreet data; loan sample

Geographic Distribution of Loans to Businesses in Karnes County - 2017
No meaningful analysis as there were no LMI tracts in 2017

### Consumer Loans

The bank’s geographic distribution for consumer loans exceeds the standards as lending activities demonstrate excellent dispersion to distressed or underserved tracts. Of the 12 consumer loans reviewed within the bank’s AA in 2015 and 2016, none of them were in an LMI tract. However, examiners noted that while the loan sample didn’t include loans from LMI tracts, 11 of these 12 loans were originated in distressed or underserved tracts. The following tables show the distribution of consumer loans in the bank’s AA.

Geographic Distribution of Consumer Loans in Karnes County – 2015/16								
Census Tract Income Level	Low		Moderate		Middle		Upper	
Loan type	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans	% of AA Owner Occupied Housing	% of Number of Loans
Consumer	<b>0%</b>	0%	<b>8.46%</b>	0%	<b>68.40%</b>	91.66%	<b>23.13%</b>	8.33%

Source: 2010 US Census; loan sample

Geographic Distribution of Consumer Loans in Karnes County – 2017
No meaningful analysis as there were no LMI tracts in 2017

### Responses to Complaints

KCNB has not received any complaints related to CRA during the evaluation period. This has a neutral impact on the bank’s overall performance.

## **COMMUNITY DEVELOPMENT TEST**

KCNB's CD performance is **SATISFACTORY** and demonstrates adequate responsiveness to CD needs.

### **Number and Amount of Community Development Loans**

KCNB originated no qualifying CD loans during the evaluation period. The economic condition in the area has led to low loan demand overall. The bank has not denied a single CRE loan in its AA since 2016.

### **Number and Amount of Qualified Investments**

The bank's level of CD investments is satisfactory. KCNB had five qualified CD investments totaling \$939 thousand. These were all municipal investments located in the bank's AA, and they all addressed the needs of a distressed or underserved census tract.

### **Extent to Which the Bank Provides Community Development Services**

The bank has only had one applicable CD service since the past performance evaluation, but this has been performed every year. Kenedy Branch President Robert Homeyer serves as a Board member for the Kenedy ISD Education Foundation, which provides grant money to local schools that are located in a distressed and underserved area. This is adequate to meet CRA requirements.

### **Responsiveness to Community Development Needs**

KCNB's responsiveness to community development needs is satisfactory. KCNB has demonstrated adequate responsiveness to CD needs in its AA through CD investments and services.



## Appendix A: Scope of Examination

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The following table identifies the time period covered in this evaluation, affiliate activities that were reviewed, and loan products considered. The table also reflects the metropolitan and nonmetropolitan areas that received comprehensive examination review (designated by the term “full-scope”) and those that received a less comprehensive review (designated by the term “limited-scope”).

<b>Time Period Reviewed</b>	Lending Test: 07/13/2015 to 12/31/2017 <ul style="list-style-type: none"> <li>• Commercial RE</li> <li>• Consumer Loans</li> </ul> Investment, Service Tests and CD Loans: 07/13/2015 to 12/31/2017	
<b>Financial Institution</b>		<b>Products Reviewed</b>
Karnes County National Bank Karnes City, TX		Commercial and Consumer lending
<b>Affiliate(s)</b>	<b>Affiliate Relationship</b>	<b>Products Reviewed</b>
None	None	N/A
<b>List of Assessment Areas and Type of Examination</b>		
<b>Assessment Area</b>	<b>Type of Exam</b>	<b>Other Information</b>
Karnes County AA	Full Scope	Non-MSA; contains only 1 upper and 3 middle income census tracts. However, one of the middle income census tracts changed from moderate to middle. All 3 of the middle income census tracts are considered distressed and/or underserved.

## Appendix B: Community Profiles for Full-Scope Areas

Karnes County Non-MSA AA 2015-2016						
Demographic Characteristics	#	Low % of #	Moderate % of #	Middle % of #	Upper % of #	NA* % of #
Geographies (Census Tracts)	4	0.0	25.0	50.0	25.0	0.0
Population by Geography	14,824	0.0	9.6	75.4	14.9	0.0
Housing Units by Geography	5,533	0.0	11.5	67.1	21.4	0.0
Owner-Occupied Units by Geography	3,203	0.0	8.5	68.4	23.1	0.0
Occupied Rental Units by Geography	1,454	0.0	14.3	69.5	16.2	0.0
Vacant Units by Geography	876	0.0	18.0	58.4	23.5	0.0
Businesses by Geography	805	0.0	6.5	79.6	13.9	0.0
Farms by Geography	87	0.0	9.2	52.9	37.9	0.0
Family Distribution by Income Level	3,452	25.5	16.5	16.9	41.1	0.0
Household Distribution by Income Level	4,657	27.0	15.3	16.8	40.9	0.0
Median Family Income Non-MSAs - TX	\$47,817	Median Housing Value				<b>\$74,114</b>
		Median Gross Rent				<b>\$565</b>
		Families Below Poverty Level				<b>17.4%</b>
<i>Source: 2010 U.S. Census and 2016 D&amp;B Data</i> <i>Due to rounding, totals may not equal 100</i>						

Karnes County Non-MSA AA 2017						
Demographic Characteristics	#	Low % of #	Moderate % of #	Middle % of #	Upper % of #	NA* % of #
Geographies (Census Tracts)	4	0.0	0.0	75.0	25.0	0.0
Population by Geography	14,879	0.0	0.0	83.5	16.5	0.0
Housing Units by Geography	5,773	0.0	0.0	77.9	22.1	0.0
Owner-Occupied Units by Geography	3,243	0.0	0.0	75.8	24.2	0.0
Occupied Rental Units by Geography	1,066	0.0	0.0	88.9	11.1	0.0
Vacant Units by Geography	1,464	0.0	0.0	74.7	25.3	0.0
Businesses by Geography	798	0.0	0.0	85.1	14.9	0.0
Farms by Geography	77	0.0	0.0	61.0	39.0	0.0
Family Distribution by Income Level	2,931	23.8	13.5	16.0	46.6	0.0
Household Distribution by Income Level	4,309	27.7	12.8	14.1	45.4	0.0
Median Family Income Non-MSAs - TX	\$52,076	Median Housing Value				\$88,450
		Median Gross Rent				\$618
		Families Below Poverty Level				19.6%
<i>Source: 2015 ACS Census and 2017 D&amp;B Data</i> <i>Due to rounding, totals may not equal 100</i>						

The Karnes County Non-MSA AA includes all four CTs in Karnes County and is not located in an MSA. In 2015 and 2016, there was one moderate, two middle, and one upper income census tract. Due to changes in census data, in 2017 one of the moderate income tracts became listed as middle, resulting in three middle income CTs, one upper income CT, and no LMI CTs. The three middle income CTs were designated as distressed or underserved due to poverty rates.

KCNB's main office is located in Karnes City, Texas, with its only branch being located in nearby Kenedy. Karnes City is the county seat of Karnes County and is located in the southern region of Texas. Both offices are located in the Karnes County AA. The US Bureau of Labor Statistics stated a 2017 average unemployment rate of 3.5%, which is lower than the state average of 4.3%. KCNB's competition comes primarily from regional banks making large commercial loans, and a national bank that is also located in the AA.

The local economy is largely oil and gas related due to the proximity of the Eagle Ford Shale play. As such, the economy is heavily influenced by energy prices and oil and gas activity. An increase in oil and gas activity generates labor demand which attracts non-local laborers. The influx of non-local laborers benefits the local economy, notably income producing CRE such as hotels and restaurants. Additionally, increased oil and gas activity leads to an influx of deposits from customers who receive royalty checks and reduces loan demand as the customer base no longer has a borrowing need.

The OCC contacted a local community organization to gain perspective on credit needs in the AA. The contact noted that local institutions, but especially KCNB, have done a good job of meeting the needs of the community. When asked about any banks in the area they would consider to be outstanding in meeting community needs, they specifically mentioned KCNB by name.