



SMALL BANK

Comptroller of the Currency
Administrator of National Banks

PUBLIC DISCLOSURE

September 2, 2003

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

**The Luzerne National Bank
Charter Number 8921**

**118 Main Street
Luzerne, PA 18709**

**Comptroller of the Currency
Northern Pennsylvania Field Office
100 Hazle Street Suite 202
Wilkes-Barre, PA 18702**

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.

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INSTITUTION'S CRA RATING

This institution is rated Satisfactory.

The overall rating is based on the following factors:

- The loan-to-deposit ratio meets standards for satisfactory performance;
- A substantial majority of the bank's loans are originated in its assessment area (AA);
- The bank has had no consumer complaints regarding its community reinvestment performance; and
- The bank's record of lending to borrowers of different incomes meets the standards for satisfactory performance.

DESCRIPTION OF INSTITUTION

The Luzerne National Bank (LNB) is a \$175 million intrastate community bank founded in 1907, with its main office and headquarters in Luzerne, Pennsylvania. LNB is located in Luzerne County in northeastern Pennsylvania, less than five miles from the city of Wilkes-Barre.

The bank operates one subsidiary: Firststar, Inc., which facilitates the bank's trust department transactions. LNB is a wholly owned subsidiary of the Luzerne National Bank Corporation, a \$175 million holding company also headquartered in Luzerne. This holding company also operates the following subsidiaries: Firststar Financial Corp., a nondeposit investment holding company; Firststar Abstract Company, a title insurance referral firm; and Firststar Insurance Services, Inc., which sells insurance products and services.

The bank operates six full service offices in the Scranton—Wilkes-Barre—Hazleton Metropolitan Statistical Area (SWH MSA). The bank has six ATMs located at the branch sites and five drive-up facilities. The branch office without a drive-up facility is located in a supermarket. A remote ATM is also operated in the MSA. The bank maintains a website which offers information on branch hours of service and bank products. Online banking is also available. LNB does not have any legal or financial condition restrictions that would impede its ability to help meet the credit needs of the communities it serves.

As of June 30, 2003, LNB reported \$113 million in net loans and \$147 million in total deposits. Net loans represented 65% of total assets. The bank's loan portfolio consists of residential real estate loans (40%), consumer loans (16%) and commercial loans (44%). The primary lending product is residential mortgage loans, which is a primary business focus of the bank. Net Tier 1 Capital was \$14 million as of that same date.

According to the June 30, 2002 FDIC/OTS Summary of Deposits Market Share Report, LNB was ranked 20th out of 33 institutions in the Scranton—Wilkes-Barre—Hazleton, PA MSA with 1.43% of deposits. PNC Bank, N.A. was ranked first with 43 offices in the MSA and 21.63% of the deposits. Other financial institutions include Wachovia Bank, N.A. (formerly First Union), in second place, with 19 offices and 9.81% of the deposits, and Manufacturers and Traders Trust Company, ranked third with 23 offices and 8.49% of the deposits.

The evaluation period for the Lending Test for home mortgages reported under the Home Mortgage Disclosure Act (HMDA) is from January 1, 1997 through December 31, 2002.

LNB's last Public Evaluation (PE) was dated June 11, 1997 and the overall CRA rating assigned was **Satisfactory**. Since the previous PE, LNB has opened four of its branches. None have been closed.

DESCRIPTION OF SCRANTON--WILKES-BARRE--HAZLETON MSA

LNB has identified 62 census tracts (CTs) in the SWH MSA (MSA 7560) as its AA. All of the CTs are in northern Luzerne County, where the bank is headquartered. This AA meets regulatory requirements and does not arbitrarily exclude low- or moderate-income geographies. These tracts are located in a mix of urban, suburban, and rural areas in and outside of the Wyoming Valley.

Of the 62 CTs in the AA, 9 are moderate-income (15%), 47 are middle-income (76%), and 6 are upper-income (10%). There are no low-income tracts in the AA. The total population in the AA was 186,790 as of the 1990 U.S. Census. The unemployment rate as of June 30, 2003 in the SWH MSA was 6.2%. This rate is higher than the state rate of 5.8%. Major employers in the bank's MSA include the federal, state and local governments, and local hospitals.

The median cost of housing in the AA is \$56,239. The Updated Median Family Income for 2002 is \$45,100. The percentage of households below the poverty level is 13%. The AA's population comprises 49,508 families with the following family income distribution: 20% are low-income, 19% are moderate-income, 24% are middle-income, and 37% are upper-income.

In 2001, 196 lenders originated HMDA loans in the AA, according to the HMDA Peer Mortgage Data. LNB was ranked 8th in the AA with a market share of 2.43%. PNC Bank, N.A. was ranked first with a market share of 12.14%. Other competitors consisted of large national banks and mortgage companies, large regional banks, local community banks, and mortgage brokers with nationwide sources of funding.

A community contact was made with a small business owner and representative of a local merchants association. The contact could not identify unmet credit needs, as financial institutions were perceived as being able to meet the various credit needs in the community. However, it was perceived that the downtown area could be physically improved by the local

government to attract more small businesses. It also was noted that very few areas are available for new development as Luzerne is a very old and established community.

Community development opportunities in the AA are limited. Competition for these types of investments is very strong. During the evaluation period, LNB did not originate any community development loans.

CONCLUSIONS ABOUT PERFORMANCE CRITERIA

The evaluation period covered lending activity for home mortgages (purchase money, refinance and home improvement loans) reported under the Home Mortgage Disclosure Act (HMDA) from January 1, 1997 through December 31, 2002. These loan products were the only products reviewed due to the business focus of the bank.

Loan-to-Deposit Ratio

An analysis of LNB's loan-to-deposit ratios from the first quarter of 1997 through the second quarter of 2003 reveals that the bank meets the standards for satisfactory performance. The bank's average loan-to-deposit ratio for these 26 quarters was 75%, ranging from 69% to 84%. This ratio is higher than the average quarterly ratios of similarly situated banks in a peer group of banks with similar asset size in Pennsylvania. The custom peer average was 72%, with average ratios during the period ranging from 66% to 78%.

Lending in Assessment Area

A substantial majority of the home mortgage loans originated during the evaluation period were within the AA. LNB exceeds the standards for satisfactory performance for lending in their AA. An analysis of the HMDA data disclosed that 85% of the loans were originated in the AA.

The following table is an analysis of the distribution of home mortgage loans inside and outside of the bank's AA.

HOME MORTGAGE LOANS ORIGINATED DURING EVALUATION PERIOD 01/01/97 THROUGH 12/31/02				
	<i>INSIDE ASSESSMENT AREA</i>		<i>OUTSIDE ASSESSMENT AREA</i>	
	# Loans	\$(000)	# Loans	\$(000)
Home Purchase Loans	223	20,246	57	5,976
Home Refinance Loans	333	25,662	52	4,201
Home Improvement Loans	324	6,017	51	1,614
Multifamily	0	0	0	0
Total Loans	880	51,925	160	11,791
Percentage	85%	81%	15%	19%

Source: 1997-2002 LNB HMDA-LAR

Lending to Borrowers of Different Incomes

LNB's record of lending to borrowers of different incomes meets the standard for satisfactory performance. The level of home mortgage loans originated to low-income borrowers is less than the percentage of low-income families in the AA. However, when considering the affordability of housing in the MSA, this performance is good. The median cost of housing in the MSA is \$56 thousand, based on 1990 U.S. Census data. The HUD updated median family income for 2002 is \$45,100. This means that a low-income person earns less than \$22,550. Based on these statistics, it would be difficult for a low-income individual to purchase housing in the AA. Also, in 2001, of the 84 lenders to low-income individuals in the AA, LNB was ranked 4th, with a market share of 4.52%.

The percentage of loans made to moderate-income borrowers meets the percentage of moderate-income families in the MSA. This performance is also satisfactory. In 2001, of the 129 lenders to moderate-income individuals in the AA, LNB was ranked 12th with a market share of 2.43%.

The following table is an analysis of the distribution of home mortgage loans by borrower income level.

BORROWER DISTRIBUTION OF HOME MORTGAGE LOANS					
01/01/97 THROUGH 12/31/02					
Income Level	# of Loans	% of Loans	\$ (000) of Loans	% of \$ of Loans	Income Level of Families in AA
Low	126	14.3%	3,083	5.9%	19.77%
Moderate	175	19.9%	6,356	12.2%	19.27%
Middle	209	23.8%	9,228	17.8%	24.00%
Upper	370	42.0%	33,258	64.1%	36.96%
Total	880	100.00%	51,925	100.00%	100.00%

Source: 1997-2002 LNB HMDA-LAR

Geographic Distribution of Loans

The geographic distribution of loans in the AA meets the standards for satisfactory performance. There are no low-income geographies in the AA. Nine of the 62 CTs in the AA are moderate-income geographies. The percentage of loans originated in the moderate-income geography is near to the percentage of owner-occupied units in the AA. Please refer to the following table for the geographic distribution of home mortgage loans.

GEOGRAPHIC DISTRIBUTION OF HOME MORTGAGE LOANS					
01/01/97 THROUGH 12/31/02					
Census Tract	# of Loans	% of Total Loans	\$ (000) of Total Loans	% of \$ of Total Loans	% of Owner-Occupied Units
Low	N/A	N/A	N/A	N/A	N/A
Moderate	72	8.2%	3,255	6.3%	9.8%
Middle	557	63.3%	27,559	53.1%	75.0%
Upper	251	28.5%	21,111	40.6%	15.2%
Total	880	100.00%	51,925	100.00%	100.00%

Source: 1997-2002 LNB HMDA-LAR

Responses to Complaints

The bank has not received any CRA-related consumer complaints since the last CRA examination.

Fair Lending Review

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