TEXAS BANK REPORT

Texas Department of Banking, Commissioner Charles G. Cooper   Data as of June 30, 2013

Commissioner's Comments

It is hard to believe we are heading into the last few weeks of the year! The summer and early fall were full of projects, initiatives, and other countless important tasks. During the same period, the Department strived to keep community bankers involved and abreast of current issues and events. We appreciate everyone's feedback and support and hope to continue to provide our bankers the regulatory guidance and support they deserve.

One of the initiatives we are most proud of is our participation in the inaugural "Community Banking in the 21st Century" Research Conference held October 2-3, 2013, at the Federal Reserve Bank in St. Louis, co-sponsored by the Conference of State Bank Supervisors (CSBS) and the Federal Reserve System. The day-and-a-half conference brought banking regulators, community bankers, and researchers together to discuss the challenges and opportunities for community bankers.

Prior to the event, Department staff worked to compile information and data gathered from community bank surveys in conjunction with four town hall meetings which were held in May and June, hosted by the Department with the assistance of Independent Bankers Association of Texas and Texas Bankers Association. The first-hand accounts from community bankers provided insight into the realities of banking today. Concern was expressed over the level of regulatory burden and the one-size-fits-all approach, but the conversation was not limited to burdens and concerns. Opportunities were also part of the initiative and a community bank's ability to differentiate itself from larger banks and deploy new technology. Town hall meetings with community bankers were held in 28 states from April to July, and I highly encourage everyone to review the Community Banking in the 21st Century: Opportunities, Challenges and Perspectives Report which is on the CSBS.org website under White Papers. Having the opportunity to work with community bankers on a project of this magnitude exemplified unity and cooperation.

As a regulator, we perform examinations of regulated entities to ensure they are operating in a safe and sound manner and are in compliance with applicable laws. The Department is no different and also receives similar audits and evaluations of our practices, procedures, and compliance with laws. In September, final preparations were made in order for the Department to receive its evaluation for reaccreditation by the CSBS. This review takes place every five years, and the Department has successfully been accredited since 1993. During the assessment, we are evaluated on critical aspects of the agency's operations, including its administration and finances, personnel policies and practices, training programs, examination policies and practices, supervisory procedures and statutory powers. I am pleased to report that on October 30, 2013, CSBS announced that the Texas Department of Banking received its certificate of accreditation, certifying that the Department maintains the highest standards and practices in state banking supervision set by the CSBS Accreditation Program. This is the Department's fifth consecutive accreditation.

With all that transpires day-in and day-out, we can each appreciate the opportunities and struggles we face. This past year has given bankers and regulators the ability to communicate these experiences and the ability to work together towards preserving the community banking and the dual banking system. I look forward to continuing the open communication and developing action items on these issues.

Charles G. Cooper
Banking Commissioner

Less Frequent Board Meetings

Is it the right move for your bank?

Chris Robinson

REGULATORY ISSUES

At the onset let's acknowledge that management is the most important component in the CAMELS ratings and adequate oversight by the bank's board of directors is an integral part of the evaluation. Statutes that govern state-chartered banks in Texas have long contained requirements for conducting meetings of the bank's board of directors.

The Texas Banking Code of 1943 required board meetings to be held monthly. The regulation also gave specific direction about board composition and items to be reviewed. A codification of the Banking Code occurred in 1997 and continued the requirement for monthly board meetings but eliminated most specificity by substituting language giving the board discretion to review and act upon reports necessary for the sound management of the institution. In the most recent legislative session, Texas Finance Code, §33.105 was revised again to allow the Banking Commissioner to approve board meetings less frequently than monthly. The revised section is:

§33.105. Required Monthly Board Meeting.

(a) Except as provided by Subsection (b), the board of a state bank shall hold at least one regular meeting each month.

(b) On application by the board, the banking commissioner may grant the board approval to hold regular meetings on a less frequent basis than the period prescribed by Subsection (a). The commissioner may revoke or modify a prior approval granted under this subsection if the commissioner determines that more frequent regular meetings of the board are necessary to promote the safety and soundness of the bank.

(c) At each regular meeting the board shall review and approve the minutes of the prior meeting and review the operations, activities, and financial condition of the bank. The board may designate a committee from among its members to perform those duties and approve or disapprove the committee's report at each regular meeting. Each action of the board must be recorded in its minutes.

While this most recent revision may appear to be a significant reduction of the regulatory requirements for monthly board meetings, the Department has established very high standards for banks that wish to hold less frequent meetings. The standards established in statute for a monthly review of the operations, activities, and financial condition do not diminish simply because the bank receives approval to conduct less frequent board meetings. Commissioner Cooper states, "I believe the vast majority of our commercial banks should continue to have monthly board meetings."

REGULATORY EXPECTATIONS

Changes to the regulation, which were supported by the Department, should not be interpreted as lessening of regulatory expectations regarding risk management practices. Any request should include a detailed explanation of the adequacy of ongoing board oversight and risk management practices after the proposed change in full board meeting frequency. As discussed below the request should include specific bank policies and procedures that evidence a level of ongoing risk management processes by an appropriately-composed, duly-appointed committee, or group of committees, that meets with sufficient frequency, reviews sufficient information, and oversees the major functional areas of the bank.

Absent a monthly meeting of the board of directors, the expectation is that there is a robust committee structure in place. This would involve committees that meet monthly and include significant board representation. The typical committees that would have a level of involvement required for consideration includes those responsible for Loans, Loan Review, Investments, Audit, Risk Management/Compliance, Budget, and Asset and Liability Management. The table below discusses the typical documentation that should accompany a bank's request, and it provides the Department's expectation regarding committee practices.

REQUIRED DOCUMENTATION	PURPOSE AND EXPECTATION
Organizational Chart with Names of Members	A graphic display of the organizations structure is necessary to determine the lines of reporting of the organization. Specifically, the chart should show how the bank's committee structure functions in relation to the overall management structure. The expectation is that all major functional areas report to committees held up by the applicant as maintaining the appropriate risk management practices and oversight in the post approval environment. Additionally, the line of reporting from these committees should be directly to the board.
Committee Charters	The typical committee charter is a presentation of much of the information needed to determine if less frequent board meetings are appropriate. This document should include the following to guide the committee's activities: the overall role/mission; specific items of responsibility; frequency of meetings; requirements for membership; list of members and support staff; and committee goals. The expectation is that committees, composed of senior management and board members, have been charged by the board with a mission and have been given the appropriate authority and resources to fulfill their mission. Additionally, missions of the major committees should be such that an appropriate level of risk management and oversight exists in the event that Board meetings are not held monthly.
Approved Policies Establishing Committees	The written policies of major functional areas would often serve the same purpose or would serve to update or clarify the composition or the functions of individual committees. Lines of reporting may also be articulated here. The Department's expectations are identical to the charter expectations expressed above.
Board Minutes	In the application review process, the Department will review minutes to determine the scope and level of board review of committee actions. The expectation is that there is sufficient board review of a duly appointed committee's actions to be fully informed of the risk management practices the committee provides during their oversight.
Committee Minutes	The Department will review the minutes of the major functional committees to determine the scope of their oversight activities. The expectation is that the committee functions as a true oversight body. There should be evidence of a detailed review of their functional area and decision making in accordance with their mission, as designated by the board in the committee charter or in policy.
Committee Information Packets	This review will determine the depth of the committee review. The expectation is that the committees are provided a sufficient level of information to fully understand the condition of the functional areas to which they are responsible. This information should enable the committee to make informed decisions regarding any corrective action or change of direction that needs to occur.

Many community banks, especially those that carry a 1 management rating, have excellent risk management and oversight practices. However, we have found that frequent and active board involvement is the underlying pillars for sound management. The Department's review will focus on the question of whether the quality of oversight would be diminished with less frequent board meetings.

If you have any questions, please contact Chris Robinson at 512-475-1329.

Importance of a STRONG Management and Board

Chris Robinson

Understanding the banking trends over the last ten years and how bank management and its board influenced the performance and risk profile of their institution give us an insight into the vital roles each party plays.

BACKGROUND

In the last thirty years, Texas experienced two significant declines in the overall condition of the banking industry. The most recent, which just now seems to be subsiding, was the result of a downturn in the national economy brought about primarily by a collapse in financing of the housing market. Texas suffered a ripple effect in other sectors, such as commercial real estate along with construction and land development. Causes for the decline were well publicized derivative transactions with excessive counterparty risk and pushing off credit risk through securitization. But, the fall of the mortgage financing sector caused the housing market collapse, which began the chain reaction affecting most economic sectors. Decades of expansion in the troubled real estate sectors, including price increases that masked the emergence of problems, only made the fall steeper.

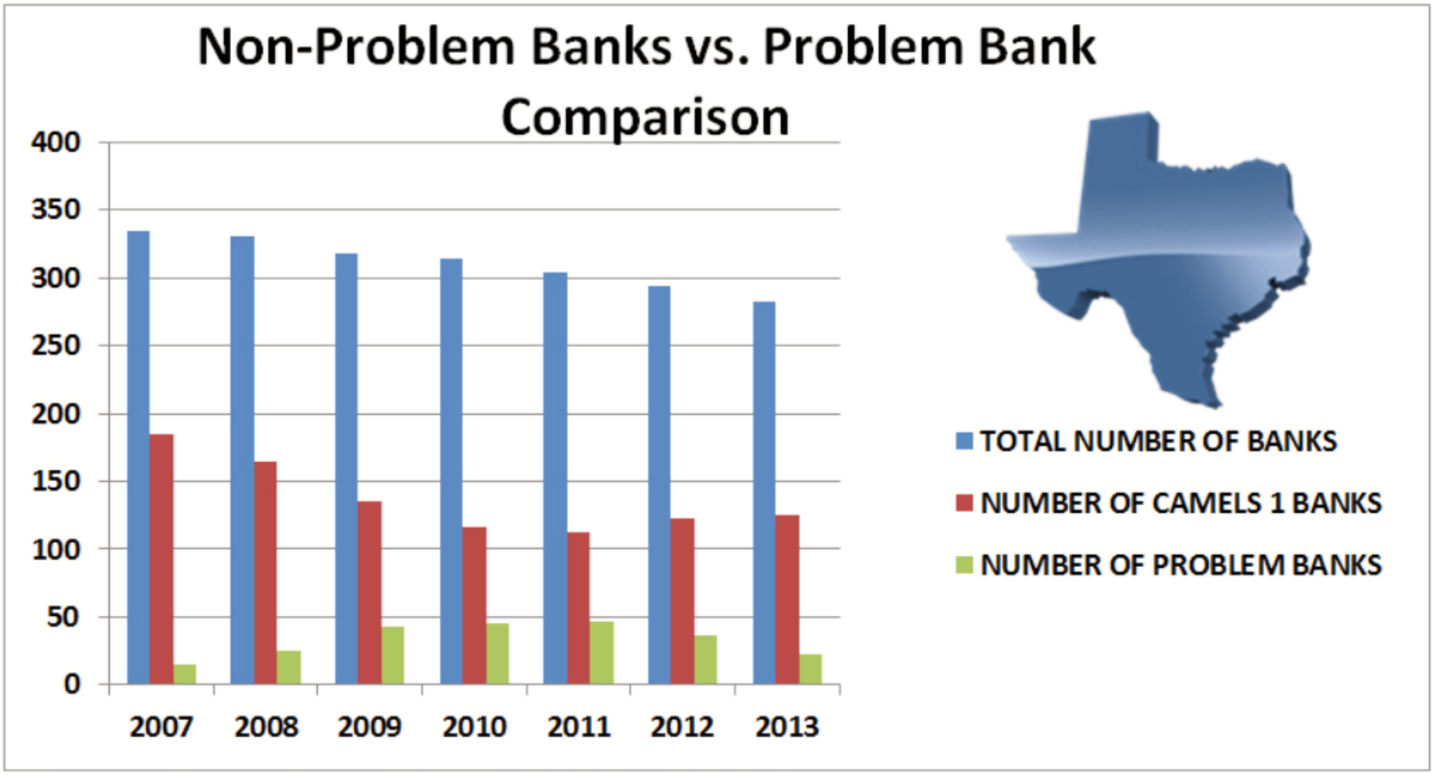
Texas was dragged into the downturn, but the state's economy did not suffer to the same extent as other areas of the country. A relatively diversified state economy, robust economic sectors important to Texas, along with continued population, job growth, and sound fiscal policy by state government, helped protect the state. However, one of the best protections for Texas was the bankers, borrowers, developers, and purchasers associated with real estate transactions that learned the hard lessons from the previous downturn.

The late 1980s were marked with severe problems that hit very specific industries in a less diversified Texas economy. Just as the agricultural sector was experiencing low prices for corn, cotton, and rice, spurred by increased foreign competition, the bottom dropped out of oil prices. The downturn of these two vital sectors in Texas along with a dramatic change in the federal income tax treatment for real estate transactions devastated our state economy causing substantial declines in real estate prices and a record number of bank failures.

BANK MANAGEMENT IN ECONOMIC DOWNTURNS

The importance of the oversight provided by an active board, especially outside directors, or those not involved in the daily affairs of the bank, should never be underestimated.

At the height of the latest economic downturn, the number of problem state-chartered banks (rated 3, 4, or 5) in Texas approximated 18% of the total number of state banks. This percentage was much higher in other parts of the country. However, in this downturn, unlike the 80s, the number of banks that were virtually free of problems was far greater. As can be seen from the graph, even in the worst period of the most recent economic downturn, the number of Texas state-chartered banks that carried a 1 rating was typically three times the combined number of banks that carried a 3, 4, or 5 rating. And, the number of banks that carried a management rating of 1 approached or exceeded 80% of all 1 rated state-chartered institutions.

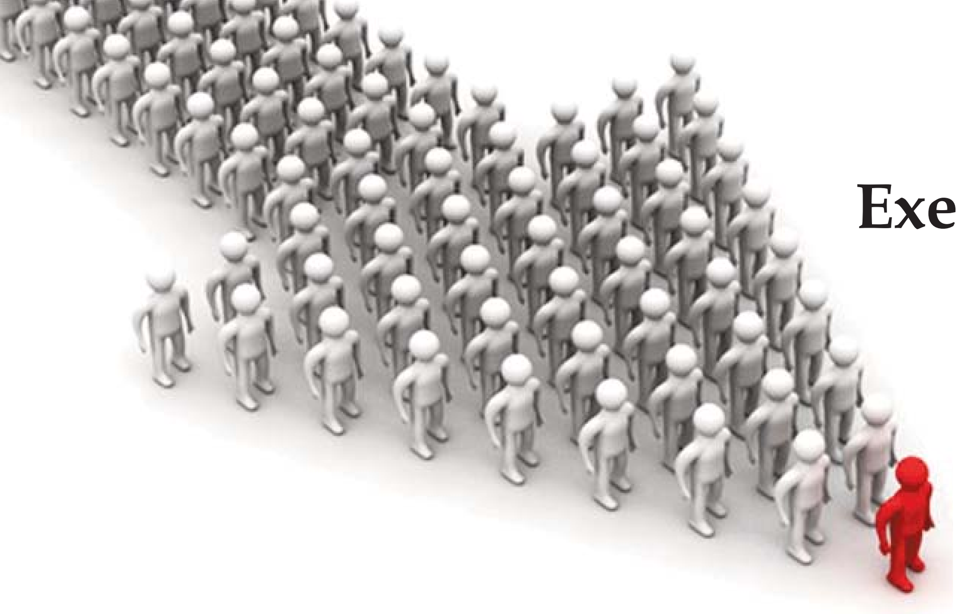


Dates represent year-ends except for 2013, which is through September.
Problem banks are defined as those with CAMELS ratings of 3, 4, or 5.

During the recent economic slump, many banks weathered the storm and maintained a satisfactory risk profile. So the question is, "what are these 1 rated banks doing right?" The answer is revealed, somewhat, in the criteria used to assess management and determine the rating. Evaluating the adequacy of board oversight has always been a major focus of the examination process and is featured predominately in the rating criteria, which lists eleven bullet points to consider when assessing management. The first two of these points are:

- The level and quality of oversight and support of all institution activities by the board of directors and management.
- The ability of the board of directors and management, in their respective roles, to plan for, and respond to, risks that may arise from changing business conditions or the initiation of new activities or products.

Both of these rating factors mention the board of directors, and relate to the existing processes in place regarding risk management and board oversight. Additionally, the definition of each of the five composite ratings includes an assessment of the ability of the board and management to address weaknesses. The difference between a 1 and a 2 is subtle. A 2 rated institution has management with the ability to address weaknesses, while a 1 rated bank has risk management systems already in place and addressing any identified weaknesses.



Executive Leadership of Cybersecurity (ELOC)

Phillip Hinkle

Commissioner Cooper began talking to the banking industry back in 2012 about the serious threat that cybercrimes pose to all banks, including rural community banks. The dialogue has not been limited to IT staff awareness, as it is equally important that executive management becomes more involved. As the volume of cyber fraud thefts reported to the Department and other regulators has increased, the Commissioner has amplified his message to the industry.

The Commissioner's warnings are not isolated. The heads of the CIA, NSA, FBI and DHS, as well as many other federal officials are also sounding warning bells.

The message came closer to home on September 16th of this year, when the CEOs of the Independent Bankers Association of Texas, Texas Bankers Association, SWACHA, as well as the CEOs of several Texas banks, met with the United States Secret Service and the Texas Department of Banking. They formed a joint initiative on Executive Leadership of Cybersecurity (ELOC, pronounced E-Lock) to bring awareness to the entire banking industry. Their message - cyber threats pose a significant risk to the banking industry and that executive leadership is needed to better address this problem.

The fact that a group of CEOs agreed to form a joint initiative is an important milestone and can only mean there is a serious issue that needs every banker's upmost attention. The ELOC concluded that cyber fraud places all banks at risk, not just large urban banks, and that executive focus on cybersecurity is required for the safety of the entire industry.

The final conclusions of the meeting are being drafted,

however this much is known, fraud is occurring through the payment systems of banks of all sizes. The initiative is more than addressing best practices related to core functions such as controlling wire and ACH payments. ELOC is executive level CEOs recognizing that cyber risk will continue to persist, morph and evolve, thus requiring the development of a counter culture of security, rather than a concentrated focus on design. Otherwise, the focus of a bank's staff will be complying with procedures rather than evaluating and analyzing potential risks.

The financial services world of delivery has changed, and bankers, regulators, and consumers need to lock arms and cultivate a new culture to manage cyber risk security.

Cybersecurity is more than a compliance matter and cannot be addressed with a simple checklist. Cybersecurity protects a bank's reputation, its customers, the community, and its stockholders. It is essential that a bank's board have confidence and the reassurance in senior management's skills to manage the risks that exist within the banking industry today. Expect to hear more about ELOC.

For questions regarding this and other IT security issues, contact Phillip Hinkle, Director - IT Security Examinations, (817) 640-4050.

Looking Back Five Years

Kurt Purdom

This fall marked the fifth anniversary of some of the most significant, and in retrospect, devastating economic events in U.S. history. Events that occurred five years ago signaled the beginning of an economic downturn, the worst recession since the Great Depression, the loss of an estimated 6 million jobs and response measures by the federal government that were unprecedented in their scope to limit the impact of these adverse events on the broader economy. Though the Texas economy fared better than most states, we were not completely immune from these disastrous economic circumstances.

Although somewhat painful, we thought a look back at some of these experiences to recall where we have been is appropriate. This exercise certainly sheds a better light on where we are now. Below is a refresher of some of the events that occurred in a four month span in the fall of 2008. By no means is the list all-inclusive, but it presents a good representation of the changing economic environment of that time.

September 2008

Fannie Mae and Freddie Mac are placed into conservatorship.

Bank of America announces agreement to buy Merrill Lynch.

Lehman Brothers files Chapter 11 bankruptcy.

FRB agrees to lend AIG up to $85 billion.

Treasury announces plan to guarantee money market mutual funds.

WAMU fails.

Dow Jones drops 777 points.

Citibank agrees to acquire Wachovia.

October 2008

U.S. House passes and President Bush signs a $700 billion bailout bill.

FRB agrees to buy an unlimited amount of commercial paper.

FDIC announces an increase in deposit insurance coverage to $250,000 per depositor.

FOMC twice reduces targeted fed funds rate by 50 basis points.

FRB approves Wells Fargo's application to purchase Wachovia.

FDIC provides details of their Temporary Liquidity Guarantee Program.

November 2008

Treasury announces a new streamlined home loan modification program.

GM, Chrysler and three large U.S. life insurance companies seek access to TARP funding.

Fannie Mae and Freddie Mac announce they will suspend mortgage foreclosures until January 2009.

Dow closes at its lowest level for the year at 7,552. Since the beginning of the year, it has lost 43% of its value.

December 2008

FRB announces three liquidity facilities: Primary Dealer Credit; Asset-Backed Commercial Paper Money Market and Term Securities Lending.

SEC announces measures to increase transparency and accountability at credit rating agencies.

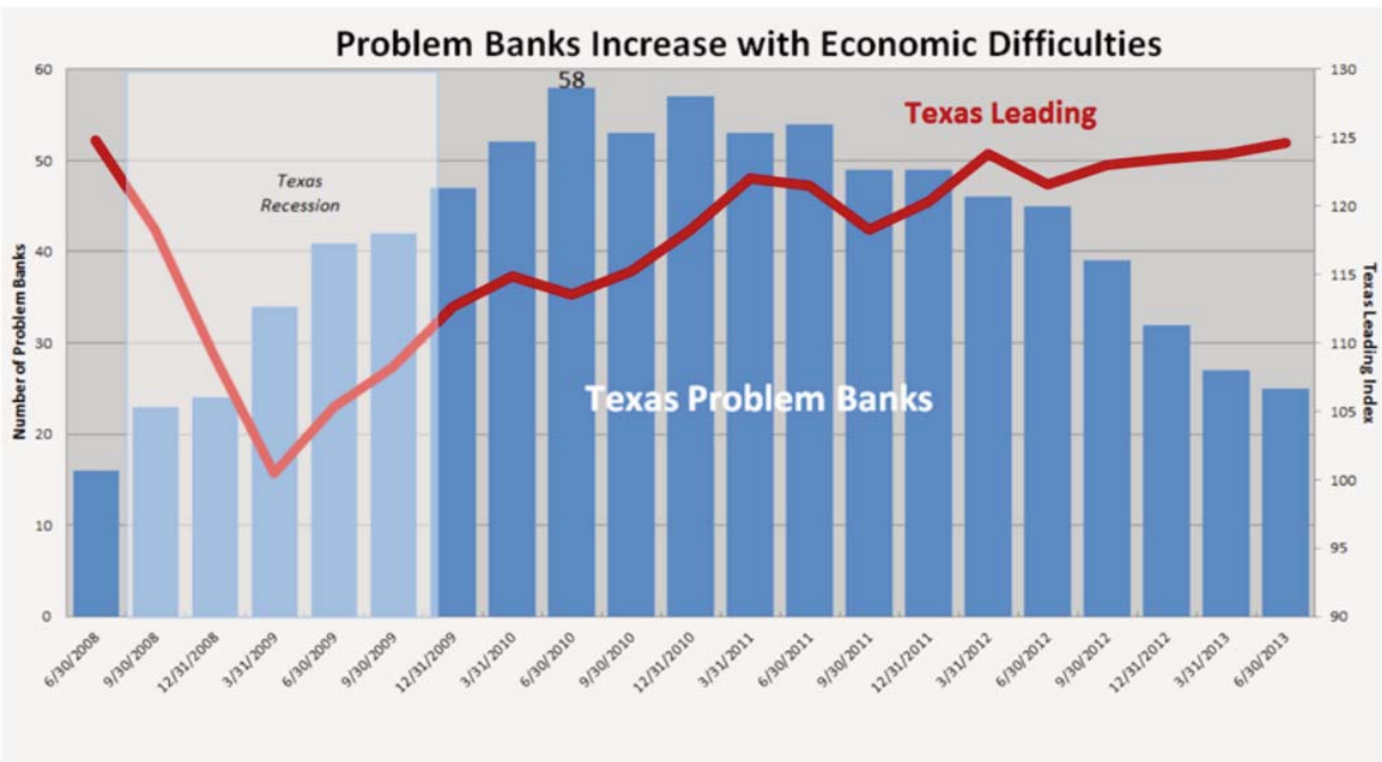
The 6-month Treasury rate ends the year at 0.27%. Twelve months before it was 3.32%.

In total, 25 banks are closed in 2008, a figure that will increase in the years to come.

The effects of these adverse events were almost immediately apparent on the Texas economy. Though Texas did not contribute significantly to the housing bubble or the widespread availability of toxic mortgages, which were partly blamed for the onset of the recession, the consequences of a nationwide recession were laid at our door just the same. The purpose of this article is not to go into a lengthy economic analysis, but instead, to highlight a few select economic measures and related problem bank statistics.

The Federal Reserve Bank of Dallas produces an index, called the Texas Leading Index, which attempts to forecast the future health of the Texas economy. The index is a composite of eight leading indicators that tend to change direction before the overall economy. They include the Texas value of the dollar, U.S. leading index, real oil price, well permits, initial claims for unemployment insurance, Texas stock index, help-wanted index and average weekly hours worked in manufacturing.

If the index falls dramatically, as it did back in 2008, then the future of the Texas economy is not very promising. As indicated by the red line in the chart below, the Texas Leading Index began a very pronounced downward trend beginning in August of 2008 with an index value of 123.1 and bottomed out in March of 2009 with an index value of 100.5. Therefore, assuming the index is a reasonable representation of the outlook for the Texas economy, the prognosis at that time certainly indicated that trouble lay ahead moving into 2009 and 2010.



Problem Banks: The Department considers any Texas state-chartered bank with a composite CAMELS rating of 3, 4, or 5 to be a problem bank. This chart includes banks examinations that are in progress, or examinations that have been completed, but the report of examination has not yet been reviewed or finalized.

Texas Recession Dates: Recession timeframe is based upon the month-over-month percent change, annualized, in the Texas Business Cycle Index. This Texas Business Cycle Index is produced by the Federal Reserve Bank of Dallas.

As bank regulators, we are well aware of the relationship between the economy and bank performance, especially after having a front row seat to the devastating banking conditions that unfolded in Texas in the 1980s. During this most recent recession, economic factors had an almost immediate impact on real estate values, small business profitability and job growth in our state, which quickly affected our supervised financial institutions.

The chart on the previous page indicates only sixteen banks reflected a composite CAMELS rating of 3, 4, or 5 in June of 2008. This represented less than 4% of the total number of Texas state-chartered banks at the time. By November of 2009, this number climbed to 47, which was a 292% increase in just 19 months. Problem banks peaked at 58 in June of 2010, which represented 18% of the total number Texas state-chartered banks. Though problem bank numbers dipped slightly in the coming months, their numbers continued at elevated levels over the next eleven months and totaled 57 in May of 2011. Interestingly, only five Texas state-chartered banks failed between 2008 and the fall of 2013.

Fortunately, the economy and banking environment in Texas have greatly improved since 2008. As illustrated in the chart, the Texas Leading Index gradually increased and as of July 2013 was at 126.1, which is very close to the level reported in April of 2008. The number of banks rated 3, 4, or 5 also improved dramatically. The chart further reflects that beginning in mid-2012, problem bank numbers exhibited a significant downward or improving trend. As of August 31, 2013, the number of problem banks was 21, or 7.4% of the total number of state-chartered institutions and represents a 64% decrease since the high of 58. Since June of 2010, when we reached the peak in the number of problem banks, 38 months have elapsed and we still have not recovered to a normalized level.

Some of the lessons both bankers and regulators can take from the past five years are clear. Adverse economic events can quickly affect banking conditions; banks should be managed and strategically positioned such that an economic downturn will neither severely harm the bank nor cause its failure. On the other hand, problem assets in the form of troubled loans and other real estate can take years to resolve. Over three years have elapsed since the recession officially ended, and many problem banks that developed asset quality, earnings and capital deficiencies are still working through those issues. Bank managers and directors should actively manage their institutions to limit credit risk and implement a credit culture that values sound underwriting at origination and excellent credit administration during repayment. Following the competition can be risky and asset concentrations should either be avoided or at the very least well controlled and understood. Regulators should foster best practices in banking and take appropriate action to address weak or unsafe practices that can become masked during economic prosperity but ultimately lead to problems during an economic downturn.

If you have any questions about this subject, contact Kurt Purdom, Director of Bank and Trust Supervision at 512-475-1333.

Benefits of CSBS Membership

The Conference of State Bank Supervisors (CSBS) is a professional regulatory association. One of the organization's overriding goals is to maintain the state system as the charter of choice for community, multi-state, international and de novo financial institutions.

CSBS has voting members and a 20-member Board of Directors that are exclusively state financial regulators. Like federal financial agencies, CSBS invites bankers and other financial service industry professionals to participate in the organization in an advisory capacity. These advisory groups share information, promote communication between state regulators and their supervised industries, and identify best practices within the state banking system.

The organization has several membership levels, including regulatory, bank, and associate memberships. Bank members of CSBS benefit from their work to keep the state banking system strong. Through a Bankers Advisory Board, they bring the industry perspective to CSBS and regulatory members with an eye towards improving the quality of supervision. Bank members also have access to CSBS compliance and management training, and CSBS publications and website keep bank members fully up-to-date on news affecting state banks and the state banking system. The CSBS weekly Examiner newsletter is supplemented by web postings and other resources. As an added bonus, CSBS bank membership dues are 100% tax deductible.

A goal of bank supervision and examination is to assure the safety and soundness of individual financial institutions and the overall banking system.

A goal of bank supervision and examination is to assure the safety and soundness of individual financial institutions and the overall banking system. One of these assurances is obtained through CSBS as it provides State Banking Commissioners with a combined voice in working with legislators and federal regulators on issues that impact state banking and financial regulation.

As a member banker stated, "I have served on the Bankers Advisory Board of CSBS since 2003 and have observed firsthand the excellent work that CSBS has accomplished. As an example, last year during the regulatory reform debate, CSBS led the charge in retaining the rights of the states to set the legal loan limit rather than imposing a national loan limit. In addition, CSBS, along with State Banking Commissioners, were instrumental in providing information to the decision makers that resulted in maintaining the Federal Reserve's role in bank supervision, which could have impacted the dual banking system."

Our own Texas Banking Commissioner, Charles G. Cooper is an active member. He is on the CSBS Board, where he serves as Treasurer. He is also on the Education Foundation Board of Trustees, the Board of Managers of the State Regulatory Registry, LLC (SRR) that oversees the Nationwide Mortgage Licensing System (NMLS) and several committees. Through CSBS, state banking regulators meet regularly with the leadership of the FDIC, Federal Reserve, CFPB, and members of Congress to discuss various issues. Without the combined voice through CSBS, these opportunities would not be available.

Corporate Application Filing Entry System

Dan Frasier

On October 1, 2013, the Department launched the Corporate Application Filing Entry System or CAFE. CAFE is a web-based application that allows entities supervised by the Department to submit applications or notices ("filings") electronically. The new system eliminates the time and expense of printing, copying, and mailing the documents. Users will no longer be required to send paper copies to the Department to submit a filing. Registered users can access the system at any time to create new filings or upload additional documents. CAFE may be utilized to submit any type of filing except Money Services Business Applications. There are no additional fees for using CAFE.

Any fees due for filings submitted via CAFE will have to be mailed to the Department. The Department anticipates adding a payment feature to CAFE to allow applicants to submit all fees due to the Department electronically in the future.

Initial registration is required before a user may begin to submit filings through CAFE. A separate registration/account is required for each individual that will utilize CAFE. The Department will verify the registration prior to activating the account. Corporate registrations or shared accounts (i.e. law firms, banks, etc.) are not allowed. However, each entity is required to designate a coordinator who will be responsible for notifying the Department of any new users that will require access to CAFE or if user access should be revoked at any time. There is no limit on the number of users an institution may register.

Applicants will continue to receive correspondence from the Department via mail, fax or email. CAFE is not intended as a communication portal between the applicant and the Department. Users cannot track the progress of the filings through CAFE. However, CAFE provides applicants with a filing history to track any filings that have been submitted and accepted.

CAFE has been designed to ensure the confidentiality of the data and the identity of individual filers. Entities ready to start using CAFE can find instructions on how to register on the Department's website.

If your institution needs assistance with CAFE, contact the Corporate Activities Division at (512) 475-1342.

Statutory Changes Related to S.B. 804 and H.B. 1664

Dan Frasier

Acts passed by the 83rd Texas Legislature included S.B. 804 relating to revising provisions in certain laws governing banks and trust companies in this state to conform to changes in terminology made by the Texas Business Organizations Code (TBOC). This bill was effective June 14, 2013, and it revises terms in Title 3, Subtitles A, F, and G of the Finance Code to be consistent with the Texas Business Organizations Code.

The Department also amended certain rules to conform to the new terms. The rules amended by this change and which impact our regulated entities are 7 Texas Administrative Code (TAC) §3.111, concerning Confidential Information; 7 TAC §§15.2, 15.9, 15.41, 15.104, 15.108 and 15.122, concerning Corporate Activities; 7 TAC §17.21, concerning Physical Location of Books and Records; and 7 TAC §§21.2, 21.9, 21.24, 21.41, 21.64 and 21.92, concerning Trust Company Corporate Activities. These rule changes were adopted at the October 18, 2013, meeting of the Finance Commission.

The new terminology includes changing "Business Corporation" to "filing entity", "articles of merger" to "certificate of merger" and "articles of association or incorporation" to "certificate of formation." Texas

CHANGES TO VARIOUS APPLICATIONS AND FORMS

Over the past several months, the Department has been working on updating corporate forms and instructions for several types of filings. The forms have been updated for clarity and to elicit the minimum information required by the Department for the purpose of making a decision. We encourage you to review the form section of our website before submitting your next corporate filing to the Department.

Finance Code, §32.008(d) makes these now outdated terms synonymous with the new terms taken from the TBOC by reference to §1.006 of the TBOC. All documents now submitted to the Department by our regulated entities must bear the new terms.

A full list of acts passed by the 83rd Texas Legislature which were effective on September 1, 2013, and impact the Finance Commission, the Department, and our regulated entities can be viewed on the Law and Guidance Manual page of the Department's website under the New Actions table. Links to House and Senate Bills are provided which show the changes to the statutes.

Effective June 14, 2013, among other matters, H.B. 1664 amended Texas Finance Code, §31.002(a)(8) and §32.204, to conform Texas law regarding state bank Loan Production Offices (LPOs) and Deposit Production Offices (DPOs) to current federal law applicable to national banks. As amended, Texas Finance Code, §32.204(a), authorizes a state bank to establish one or more LPOs or DPOs for the purpose of soliciting deposit accounts, applications for loans, or equivalent transactions, performing ministerial duties related to such solicitations, and conducting other activities permitted by rule. Under Texas Finance Code, §31.002(a)(8), such an office is not a branch, and any combination of permissible non-branch functions or facilities at one location does not create a branch.

To implement the changes, proposed amendments to 7 TAC §§3.91 and 3.93 were adopted at the October 18, 2013, meeting of the Finance Commission.

Searching for a New Headquarters

The Department of Banking is seeking to relocate its headquarters from the building it has occupied for several decades into a larger facility.

Our headquarters resides currently in a 36,499-square foot, three-story, office building located at 2601 N. Lamar Boulevard in Austin, Texas. The Department was the sole occupant of this space from December 1974 to April 1984 at which time we starting sharing the space with our sister agencies, the Office of Consumer Credit Commissioner and the Texas Department of Savings and Mortgage Lending. The original two-story building, which is situated on a 2.1-acre site, was constructed in 1968 and a third floor was added in 1984 to accommodate our growth. While the property includes a combination of surface and below building parking, the parking ratio is well below normal standards of 4.0 per 1,000 SF.

Over the years, each agency has seen their staffing grow along with the needs of their respective regulated industries. The agencies have utilized as much space as possible to accommodate the increased staffing, but additional expansion is not possible. We are also receiving feedback from regulated entities about inconveniences related to limited parking challenges.

Pros of current location:
The current headquarters building is located in one of the premier suburban office markets in one of the most desirable locations within the Austin MSA that lends itself to redevelopment. Also, the University of Texas with over 50,000 undergraduates is nearby, driving the high demand for housing projects within walking distance to the campus. This should allow the Department to achieve a respectable sales price when the time comes.

Cons of current location:
If you have had to travel to the headquarters office for a meeting with the Department, you know that parking is limited. Street parking adjacent to our building is very sparse and the City of Austin has now placed parking meters in this area. In addition, parking is not available along Lamar Boulevard. While our building is considered to be in fair overall condition, it currently is in need of renovation and repair of deferred maintenance items.

The Journey to Becoming a Commissioned Examiner

Phil Lena

Any banker knows that a bank examination can be complex and rigorous, consequently the need for highly trained examiners is paramount. Examiners serve to ensure the stability and strength of the financial system of our state and country. The success of the Department in meeting its statutory responsibilities is directly tied to its ability to develop and maintain a well trained and experienced staff.

A career for a Bank and Trust Commissioned Financial Examiner usually begins at the position of Assistant Examiner. The entry level bank examiner is heavily involved in learning examination work procedures predominantly through on-the-job training under direct supervision of a senior examiner. Their journey toward commissioned status entails a five to seven year specialized training process, one that is unlikely to be attained outside of another bank regulatory agency. The Department estimates that the direct and indirect costs of this development and training exceed $100,000 in the first two years of employment for each trainee. Training and retention of qualified examiners has historically been one of the most challenging tasks faced by the Department of Banking. The resources needed to nurture an entry-level assistant into a fully-trained examiner extend beyond time and money; sometimes bankers also find themselves included in the development process. In addition, assistant examiners also attend approximately 440 hours of formal, core school training in their formative years.

A commissioned examiner has mastered a variety of skills that are necessary to fulfill the regulatory responsibilities of the Department, and only commissioned examiners can manage examinations and sign examination reports.

To determine if an examiner has successfully mastered these vital skills and assume the increased responsibility of an Examiner-In-Charge (EIC), the Department uses a testing process known as the Commissioning Process, or Bank Examination Testing System (BETS). There are four distinctive phases of the test: General Knowledge, Credit Analysis, CAMELS Knowledge Panel, and a Test Bank.

Financial Examiners begin to prepare for the BETS process virtually on their first day of employment. The testing process is a self-referral process in which the assistant examiner notifies their Regional Director when they are prepared to be tested. Candidates regularly seek advice, recommendations for improvement and/or counseling from their colleagues and supervisors concerning their preparedness.

Once a candidate passes all four phases of the process, they are promoted to a Financial Examiner IV, or Commissioned Examiner. In fiscal year 2013, nine assistant examiners successfully completed the process and were promoted to Commissioned Examiners. Achieving this milestone is quite a feat, as staff members spend years preparing for this test that is considered more rigorous when compared to other states and federal standards. As of August 31, 2013, the Department proudly employs 75 Commissioned Examiners.

The Department has successfully improved its retention of Commissioned Examiners since being awarded the Self-Directed, Semi-Independent status in September 2010. The Department works diligently to ensure that our examination team is of the finest quality and can be relied upon to provide "tough but fair" supervision of our banking system now and well into the future.

In Memoriam

The Department's Bank and Trust Supervision Division lost two dedicated employees this year. We are grateful for their many contributions to the agency and remember them fondly as colleagues and friends.

Mary Jaco
Administrative Technician
Houston Regional Office
Passed Away on April 26, 2013

Lloyd Baker
IT Examiner
San Antonio Regional Office
Passed Away on October 5, 2013

TABLE I

Quarterly Balance Sheet and Operating Performance Ratios

for Texas State-Chartered Banks 6/30/13 Through 6/30/12

ACCOUNT DESCRIPTIONS (IN MILLIONS OF $)	6/30/13	3/31/13	12/31/12	9/30/12	6/30/12
Number of State-Chartered Banks	288	288	293	296	300
Total Assets of State-Chartered Banks	203,295	203,846	205,610	198,470	196,322
Number of Out-of-State, State-Chartered Banks Operating in Texas	29	29	27	27	26
Total Texas Assets of Out-of-State, State-Chartered Banks Operating in Texas	40,210	40,210	38,370	38,370	36,061
Subtotal	243,505	244,056	243,980	236,840	232,383
Less: Out-of-State Branch Assets/Deposits	-42,210	-42,210	-42,210	-42,210	-37,987
**Total State Banks Operating in Texas	201,295	201,846	201,770	194,630	194,396
BALANCE SHEET (Tx. State-Chartered Banks)					
Interest-Bearing Balances	12,526	16,109	15,138	13,319	12,942
Federal Funds Sold	1,174	1,174	1,404	1,172	1,229
Trading Accounts	375	455	667	651	707
Securities Held-To-Maturity	14,381	13,836	13,152	9,943	9,531
Securities Available-for-Sale	41,338	42,613	42,634	45,210	44,798
Total Securities	56,094	56,904	56,453	55,804	55,036
Total Loans	116,921	113,863	115,114	111,010	111,193
Total Earning Assets	186,715	188,050	188,109	181,305	180,400
Premises and Fixed Assets	3,344	3,321	3,338	3,234	3,274
Total Assets	203,295	203,834	205,782	198,470	196,322
Demand Deposits	21,355	22,520	24,298	20,589	20,255
MMDAs	88,429	87,477	86,538	83,285	81,164
Other Savings Deposits	14,325	14,183	13,806	13,027	12,762
Total Time Deposits	34,821	35,226	35,396	36,168	37,390
Brokered Deposits	1,710	1,662	1,581	1,673	1,526
Total Deposits	167,411	168,068	169,156	161,153	159,793
Federal Funds Purchased	3,338	3,267	3,486	3,489	3,841
Other Borrowed Funds	5,796	5,420	5,767	5,785	5,535
Total Liabilities	180,710	181,143	183,170	175,802	174,043
Total Equity Capital	22,585	22,691	22,612	22,664	22,279
Loan Valuation Reserves	1,575	1,566	1,579	1,664	1,725
Total Primary Capital	24,160	24,257	24,191	24,328	24,004
Past Due Loans > 90 Days	356	380	385	464	436
Total Nonaccrual Loans	1,249	1,319	1,380	1,661	1,731
Total Other Real Estate	564	640	659	756	827
Total Charge-Offs	190	101	503	387	265
Total Recoveries	68	32	145	108	72
Net Charge-Offs	122	69	358	279	193
INCOME STATEMENT					
Total Interest Income	3,315	1,646	6,444	4,982	3,401
Total Interest Expense	302	155	686	544	384
Net Interest Income	3,013	1,491	5,758	4,438	3,017
Total Noninterest Income	1,458	703	2,159	2,080	1,370
Loan Provisions	120	58	255	193	124
Salary and Employee Benefits	1,684	833	2,854	2,423	1,632
Premises and Fixed Assets Expenses (Net)	368	182	679	546	378
All Other Noninterest Expenses	920	462	1,759	1,413	950
Total Overhead Expenses	2,972	1,477	5,292	4,382	2,960
Securities Gains (Losses)	42	27	139	103	101
Net Extraordinary Items	0	0	-2	-2	0
Net Income	1,085	525	1,930	1,561	1,068
Cash Dividends	605	283	1,457	1,022	557
RATIO ANALYSIS					
Loan/Deposit	69.84%	67.75%	68.05%	68.88%	69.59%
Securities/Total Assets	27.59%	27.92%	27.43%	28.12%	28.03%
Total Loans/Total Assets	57.51%	55.86%	55.94%	55.93%	56.64%
Loan Provisions/Total Loans	0.21%	0.20%	0.22%	0.23%	0.22%
LVR/Total Loans	1.35%	1.38%	1.37%	1.50%	1.55%
Net Charge-Offs/Total Loans	0.10%	0.06%	0.31%	0.25%	0.17%
Nonperforming+ORE/Total Assets	1.07%	1.15%	1.18%	1.45%	1.53%
Nonperforming+ORE/Primary Capital	8.98%	9.64%	10.02%	11.84%	12.47%
Net Interest Margin	3.23%	3.17%	3.06%	3.26%	3.34%
Gross Yield	4.70%	4.61%	4.18%	4.73%	4.86%
Return on Assets	1.07%	1.03%	0.94%	1.05%	1.09%
Return on Equity	9.61%	9.25%	8.54%	9.16%	9.59%
Overhead Exp/TA	2.92%	2.90%	2.57%	2.94%	3.02%
Equity/Total Assets	11.11%	11.13%	10.99%	11.42%	11.35%
Primary Capital/Total Assets+LVR	11.79%	11.81%	11.67%	12.16%	12.12%

*Unrealized gains/losses are already included in equity capital figures.

**Total State Banks Operating in Texas includes branches of out-of-state, state-chartered banks.

Data was derived from the FDIC website.

TABLE II

Comparative Statement of Condition

Commerical Banks Domiciled in Texas

June 30, 2013 and June 30, 2012

ACCOUNT DESCRIPTIONS (In Millions of $)	6/30/2013 STATE CHARTERED		6/30/2013 NATIONAL CHARTERED		6/30/2013 ALL BANKS		6/30/2012 ALL BANKS	
Number of banks	288	% TA	224	% TA	512	% TA	544	% TA
BALANCE SHEET								
Interest-Bearing Balances	12,526	6.2%	8,645	5.7%	21,171	5.9%	22,341	6.6%
Federal Funds Sold	1,174	0.6%	15,784	10.3%	16,958	4.8%	7,009	2.1%
Trading Accounts	375	0.2%	35	0.0%	410	0.1%	751	0.2%
Securities Held-To-Maturity	14,381	7.1%	2,753	1.8%	17,134	4.8%	12,188	3.6%
Securities Available-For-Sale	41,338	20.3%	22,896	15.0%	64,234	18.0%	66,053	19.5%
Total Securities	56,094	27.6%	25,684	16.8%	81,778	23.0%	78,992	23.3%
Total Loans	116,921	57.5%	94,495	61.8%	211,416	59.3%	205,971	60.9%
Total Earning Assets	186,715	91.8%	144,608	94.5%	331,323	93.0%	314,313	92.9%
Premises & Equipment	3,344	1.6%	1,994	1.3%	5,338	1.5%	5,245	1.5%
TOTAL ASSETS	203,295	100.0%	153,002	100.0%	356,297	100.0%	338,458	100.0%
Demand Deposits	21,355	10.5%	14,734	9.6%	36,089	10.1%	33,561	9.9%
MMDAs	88,429	43.5%	49,225	32.2%	137,654	38.6%	124,001	36.6%
Other Savings Deposits	14,325	7.0%	36,769	24.0%	51,094	14.3%	44,968	13.3%
Total Time Deposits	34,821	17.1%	22,137	14.5%	56,958	16.0%	61,182	18.1%
Brokered Deposits	1,710	0.8%	2,479	1.6%	4,189	1.2%	4,041	1.2%
Total Deposits	167,411	82.3%	129,227	84.5%	296,638	83.3%	277,334	81.9%
Fed Funds Purchased	3,338	1.6%	1,425	0.9%	4,763	1.3%	5,467	1.6%
Other Borrowed Funds	5,796	2.9%	5,344	3.5%	11,140	3.1%	10,889	3.2%
TOTAL LIABILITIES	180,710	88.9%	137,101	89.6%	317,811	89.2%	300,492	88.8%
Equity Capital	22,585	11.1%	15,901	10.4%	38,486	10.8%	37,965	11.2%
Allowance for Loan/Lease Losses	1,575	0.8%	1,585	1.0%	3,160	0.9%	6,552	1.9%
Total Primary Capital	24,160	11.9%	17,486	11.4%	41,646	11.7%	41,517	12.3%
Past due >90 Days	356		361		717		855	
Nonaccrual	1,249		1,377		2,626		3,409	
Total Other Real Estate	564		484		1,048		1,541	
Total Charge-Offs	190		160		350		560	
Total Recoveries	68		46		114		116	
INCOME STATEMENT	Y-T-D		Y-T-D		Y-T-D		Y-T-D	
Total Interest Income	3,315	100.0%	2,527	100.0%	5,842	100.0%	7,324	100.0%
Total Interest Expense	302	9.1%	208	8.2%	510	8.7%	945	12.9%
Net Interest Income	3,013	90.9%	2,319	91.8%	5,332	91.3%	6,379	87.1%
Total Noninterest Income	1,458	44.0%	816	32.3%	2,274	38.9%	2,379	32.5%
Loan Provisions	120	3.6%	17	0.7%	137	2.3%	514	7.0%
Salary & Employee Benefits	1,684	50.8%	978	38.7%	2,662	45.6%	2,929	40.0%
Premises & Fixed Assets (Net)	368	11.1%	235	9.3%	603	10.3%	737	10.1%
All Other Noninterest Expenses	920	27.8%	632	25.0%	1,552	26.6%	3,036	41.5%
Total Overhead Expenses	2,972	89.7%	1,845	73.0%	4,817	82.5%	6,702	91.5%
Securities Gains(losses)	42	1.3%	19	0.8%	61	1.0%	99	1.4%
Net Extraordinary Items	0	0.0%	1	0.0%	1	0.0%	4	0.1%
NET INCOME	1,085	32.7%	955	37.8%	2,040	34.9%	2,116	28.9%
Cash Dividends	605		457		1,062		1,009	
Average ROA	1.07%		1.25%		1.15%		1.25%	
Average ROE	9.61%		12.01%		10.60%		11.15%	
Average TA ($ Millions)	706		683		696		622	
Average Leverage	11.11%		10.39%		10.80%		11.22%	
Dividends/Net Income	55.76%		47.85%		52.06%		47.68%	

***Unrealized gains/losses are already included in equity capital figures.**

Table includes only banks domiciled in Texas. Branches of out-of-state banks are not included.

Data was derived from the FDIC website.