Texas Bank Report

Texas Department of Banking, Charles G. Cooper, Commissioner November 2022

Commissioner's Comments

"Despite the economic and regulatory woes that come and go, many of you have conveyed to me over the years that banking is a fulfilling career choice ..."

Nine months have passed since the Department last issued an edition of Texas Bank Report, and yet it seems like a lifetime ago. Much has changed in the interim.

Just ten days after the issue was posted, Russia invaded Ukraine, heightening tensions between the U.S. and Russia, and disrupting the world's economy. Russia is a major supplier of oil and Ukraine provides much of the world's supply of grain and fertilizer. The war substantially reduced the flow of these vital commodities to Europe and the U.S. disrupting the world economy. Concern increased over potential cyber attacks here in the U.S.

Closer to home and prior to the invasion, the primary concerns among most bankers surveyed by the Department ranged from the long-term impact of the pandemic, the political climate and the impact on banks, and the impact of the low-rate environment on margins.

Today, the major concerns are the rapid increases in interest rates, inflation, and the possibility of a recession. While the economy remains resilient, the continued fear of rising inflation and the impact from increased wages and fuel costs to companies and consumers are greatly impacting everyone.

The cost of consumer goods increased this summer at the fastest clip in nearly 40 years. Rising gas prices, especially for diesel fuel, affected nearly every corner of the nation's economy, although the pace of price increases has slowed of late. Food prices also climbed sharply, as have mortgage rates.

Millions of Americans too young to remember the 1980s have never known inflation rates this high. Many more may have forgotten the double-digit interest rates of those days.

Against this backdrop, this edition of Texas Bank Report examines current events impacting the state's banking system, specifically the effect of a severe drought, combined with higher input costs such as fuel and fertilizer, on ag lenders.

Approximately 43% of Texas is in "severe drought," with 13% "extreme" and 1.4% in the worst category of "exceptional." Currently, 245 counties have disaster

designations, making this the eighth-driest year on record. Many crops were expected to be a total loss by early spring, with cotton experiencing the greatest damage. Livestock also experienced dramatic losses as the result of the drought, bringing with it scorched pastures, devastated feed harvests, and an endangered way of life.

Regardless of all the change we have experienced in the past six months, one area of constant concern remains: the need to remain vigilant regarding cyber security. Money laundering, the financing of terrorism, human trafficking, fraud, or other illicit financial activities can occur through any number of different methods or channels. Beyond these unlawful actions, your bank's computer security can be compromised through destructive malware, ransomware attacks, and other means.

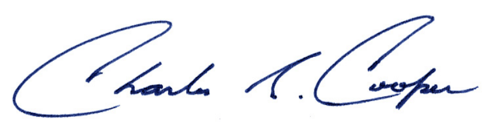
By now, banks should have an established program and procedures reasonably designed to assure and monitor compliance with regulatory requirements regarding cybersecurity. The integrity of your institution, its reputation, and the security of your customers' accounts depend on it. The Department has certainly worked tirelessly to make cybersecurity a priority, as so many of you have too. If there is one thing we have learned, is that written policies and procedures are meaningless unless the bank's leadership makes it a priority.

Despite the economic and regulatory woes that come and go, many of you have conveyed to me over the years that banking is a fulfilling career choice, giving individuals a unique opportunity to fulfill their civic desires to help their community. Bankers often play a direct role in helping customers make some of the most important decisions of their lives, such as saving for college, purchasing homes and planning for their business and retirement needs. Periodically, the Department tries to highlight the dedication to excellence so many of our state-chartered banks demonstrate each day, including helping their customers – and their customers' children – learn to make informed financial decisions through financial education.

This edition turns the spotlight on two South Texas banks heavily involved in the communities they serve by increasing financial literacy among the residents of Cameron and Hidalgo counties. Whether in the classroom, bank lobby, local chamber of commerce, or small business, the staff of these two institutions go the extra mile to serve and improve the lives of their customers.

It truly is inspiring to read about their efforts, which touch so many. It is also an excellent example of how community banks improve the quality of life in the cities and towns they call home. They do not always receive the recognition they deserve, and we hope to reverse this in some small way.

I hope you enjoy and benefit from this edition of Texas Bank Report. It is a pleasure to make it available to you. In the meantime, stay safe and we wish you all the best.



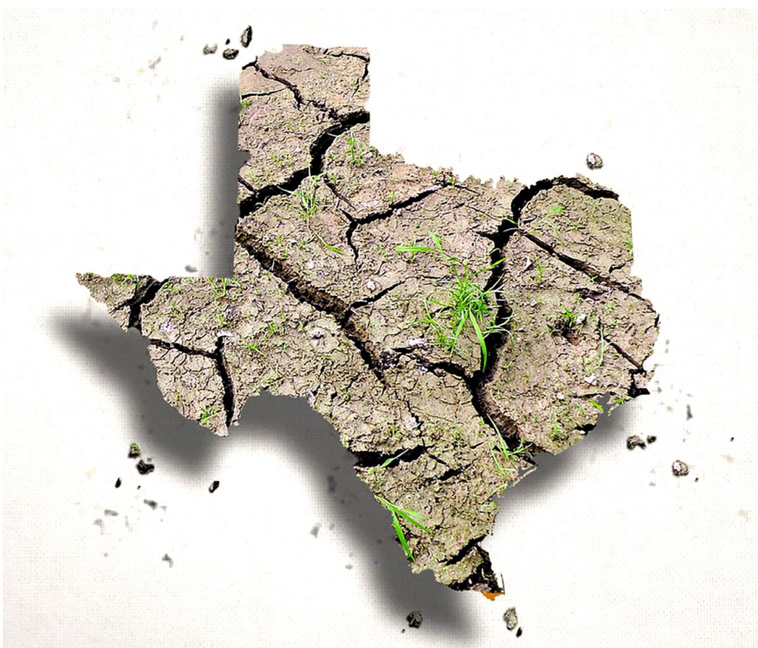
Charles G. Cooper
Banking Commissioner

Drought and Agriculture Lending: West Texas Perspective

By: David Reed

Drought is nothing new to Texas and banks involved with agriculture lending have learned to manage the risks accordingly. Each drought has a varied impact on bank lending levels, loan quality, and a borrower's financial condition due to the high number of variables. Among others, variables include timing during the growing cycle, drought severity, previous years' weather conditions, and commodity pricing.

The current drought, however, has produced its own set of unique conditions. Exacerbating the 2022 drought was a very dry fall and winter in 2021. A sampling of banks in the western and panhandle regions of Texas report a varied impact with most bankers providing a consistent pessimistic outlook. The most severely impacted areas of west Texas are the southern and western portions. However, isolated rains have improved conditions in some areas, with the northern panhandle benefiting the most.



Bankers interviewed expected ag production lending to generally decline 50%-75% for the 2022 crop cycle. However, the bankers indicated that their borrowers are in surprisingly good financial condition. Borrowers' stable financial condition results from favorable yields and conditions in 2021, (primarily for cotton producers on the south plains) resulting in good returns.

Todd Pope, with Wellington State Bank's Lubbock branch, said, "Asset quality continues to improve. 2021 was an excellent year for several of our producers. They not only paid 2021 operating lines in full, but several of our producers were able to make annual term payments for 2021 and 2022." Additionally, government aid programs and insurance claims are providing a buffer in 2022 to what otherwise could be disastrous conditions.

With the 2022 drought carrying over from fall 2021, many crops were already determined to be a loss in the early spring and summer of 2022. Thus, input costs were reduced, which in turn lead to early insurance payments that were used to pay for early season expenses.

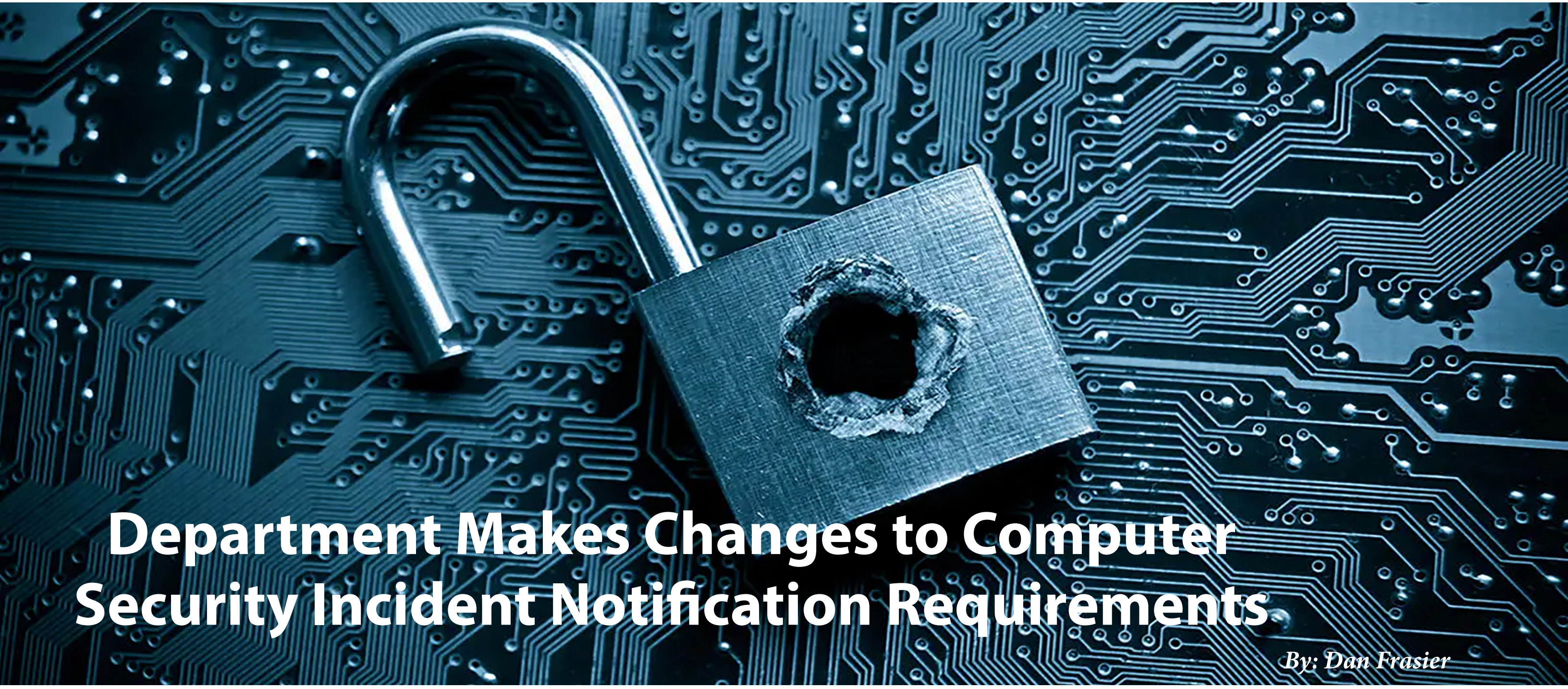
Nevertheless, Texas' current cotton crop is taking a major hit. The U.S. Department of Agriculture predicts a record low ratio of harvested-to-planted acres and the state's lowest output since 1986. Panhandle farmers interviewed in a recent *Wall Street Journal* article estimate that 90% of the region's cotton fields have been abandoned, as the rain some portions of the region received in August was insufficient for many producers.

Texas is the country's top cotton-producing state, and the commodity is an important, billion-dollar component of the state's economy.

Livestock production, another important component of the Texas economy, is also experiencing a dramatic exposure to the drought. Many banks reported seeing reductions in herd size early in the year due to lack of forage. The lack of forage is a carryover from poor conditions in the fall and winter of 2021 rolling into 2022. The prolonged drought has left many pastures dry and burnt.

Steve McSpadden, First Capital Bank, Quanah, indicated that partial liquidation of herds occurred due to the lack of drinking water for cattle from earthen tanks. Hay stock that would have been used for the winter months was used to sustain herds during the summer.

Compounding the difficulty is the lack of new hay being stored. Hay currently being produced is also sustaining herds and is not being stored for use in the fall and winter of 2022. Late summer rains may be too little too late to assist in livestock lending for 2022. The total impact on livestock lending is yet to be determined. Historically it takes several years to replenish livestock herds as seen during the drought of 2011.



Department Makes Changes to Computer Security Incident Notification Requirements

By: Dan Frasier

The Department is acutely aware of the challenges financial institutions face from continuous and evolving attacks on computer systems by cybercriminals. Computer security incidents can result from attacks through destructive malware or ransomware attacks, as well as hardware and software failures or even clerical errors.

The rapid pace of these attacks and the potential of an attack being part of a broad campaign against the industry, make it imperative supervised institutions bring material computer security incidents to the Department's attention shortly after they occur.

By ensuring the Department is promptly notified of material computer security incidents, agency staff can provide needed assistance to affected banks and warn other institutions to be on alert for threats. Incident reports assist in increasing the awareness of emerging threats that pose a broad risk to the banking system. Furthermore, the Department can use information gleaned from incident reports to provide guidance or make changes to examination programs.

Effective September 8, 2022, the Department amended its security notification rule that first went into effect on January 2, 2020. The primary purpose of the amendment is to reduce regulatory burden and allow Texas state banks to notify the Banking Commissioner using the same computer security incident notification provided to a bank's federal regulator required under federal law.

Upon the effective date, the amended rule (***7 TAC §3.24*** – ***Notice of Computer-Security Incident***) will read as follows:

> A state bank shall notify the banking commissioner and submit the information required by 12 C.F.R. part 225, subpart N, or part 304, subpart C, as applicable, or any successor regulation, regarding a computer-security incident that qualifies under such regulations as a notification incident, no later than the time the information is required to be submitted to the applicable federal regulatory agency.

Additional details regarding the specifics of the Department's cybersecurity incident reporting requirements are available on the agency's website.

Texas state member banks should refer to 12 C.F.R 225 subpart N and non-member banks to part 304 subpart C for the definition of a "notification incident" that would require notice to a bank's federal regulator and therefore the Department. Notices to regulators are required within 36 hours after the institution determines a notification incident has occurred.

The bank should send the notification to the Department by either email to bats@dob.texas.gov or phone to (877) 893-6246. Be sure to include the entity's name and city, a basic description of the incident, and contact information should follow-up be necessary. Any confidential personal identifiable information or other confidential information should be uploaded via the Data Exchange (DEX) portal to the correspondence folder.

Additional information on submitting computer security event notifications and additional Information on Technology Resources can be found on the Department's website under Cybersecurity Incident Report.

Upcoming Changes That May Affect You:

A Closer Look at the AML Act and Corporate Transparency Act

By: Kevin Wu

There are significant legislative amendments to the USA PATRIOT Act in the 2021 National Defense Authorization Act (NDAA) that are designed to enhance law enforcement tools, improve collaborative efforts, and expand jurisdiction and penalties.

Why is this important?

These changes will impact your processes and procedures and we encourage you to work with your Bank Secrecy Act (BSA) staff and audit/consulting firms to incorporate these areas into your operations. Further, it should be noted that once the rules are finalized and any initial grace period allotted ends, the Department in coordination with its federal counterparts will work together to incorporate these items into the examination process.

Overview

Since the BSA was passed in 1970, Congress has implemented various enhancements and amendments to improve the effectiveness of money laundering laws, strengthen the reporting requirements, and expand available resources. Most notably, significant changes to the law were enacted following the terrorist attacks on September 11, 2001.

First among these was the USA PATRIOT Act, Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, which was enacted in October of that year specifically to deter and punish terrorist acts and to enhance law enforcement investigatory tools.

Given the evolution of criminal activities and law enforcement's investigative limitations, legislative enhancements have been implemented or are being finalized for implementation through the Anti-Money Laundering Act of 2020 (AML Act). The Act became effective January 1, 2021, and is contained in Division F of the NDAA. These amendments to the USA PATRIOT Act seek to improve current processes and establish new systems.

The AML Act strengthens the Financial Crimes Enforcement Network (FinCEN) by expanding its authority, jurisdiction, enforcement capabilities, and available resources to carry out its mission of safeguarding the nation's financial system. The AML Act focuses on protecting national security interests and introduces enhancements that previously were wish list items for improving law enforcement capabilities and regulatory effectiveness. Furthermore, it enhances collaboration among government agencies, regulators, and industry members, and establishes public priorities for purposes of AML and Countering the Financing of Terrorism (AML/CFT).

National Priorities

FinCEN published the first set of AML/CFT National Priorities and a related Interagency Statement on June 30, 2021. Although the AML Act requires FinCEN to develop and circulate regulations regarding the National Priorities within 180 days of the establishment of the AML/CFT Priorities, the final regulations have been delayed and are yet to be finalized.

The National Priorities are not required to be incorporated until 180 days after the effective date of the final revised regulations, however, banks and non-bank financial institutions should be preparing and considering how they will incorporate these critical elements into their risk-based AML/CFT program.

Assessing the potential risks associated with each institution's products and services, customers served, and geographic areas in which they operate will need to address the following National Priorities:

A. **Corruption** – FinCEN has issued advisories regarding the Treasury Department's Office of Foreign Assets Control (OFAC) sanctions related to human rights abuses, and political and public corruption in Nicaragua (October 4, 2018), South Sudan (September 6, 2017), and Venezuela (September 20, 2017) that may help identify red flags and trends regarding gold smuggling, the laundering of embezzled proceeds, and illicit real estate investments. These advisories also contain relevant guidance related to Russia and ongoing sanctions.

B. **Cybercrime, including relevant Cybersecurity and Virtual Currency considerations** – The U.S. Department of Treasury is focused on cyber-enabled financial crime, ransomware attacks, and the misuse of virtual assets (virtual currency) that exploits and undermines their innovative potential, including through the laundering of illicit proceeds. FinCEN has published numerous advisories in recent years regarding ransomware and COVID-19 related cybercrime to alert financial institutions to predominant trends, typologies, and potential indicators. For example, FIN-2020-A006 Ransomware and the Use of the Financial System to Facilitate Ransom Payments and FIN-2020-A005 Cybercrime and Cyber-Enabled Crime Exploiting the Coronavirus Disease 2019.

   The ransomware advisory also provides information on the movement of virtual currency that may provide training benefits as well as specific recommendations on reporting information to FinCEN. Given the recent successful recoveries by the Federal Bureau of Investigation (FBI) of cybercriminals' virtual currency wallets, it is important to provide as much detailed information as possible such as the types of exchanges and digital wallets the ransomware scheme is utilizing when submitting reports regarding customers who have been victimized by these cyber-crimes.

C. **Foreign and Domestic Terrorist Financing** – While the goals of the USA PATRIOT Act historically focused on foreign terrorist financing, recent federal legislative changes have expanded efforts to address domestic terrorism as well. As the methods of these criminal organizations evolve, it is important that legislative amendments and enhancements adjust accordingly. The overall goals in preventing, disrupting, and deterring acts of domestic terrorism are embedded within the strategic goals and detailed in the National Strategy for Countering Domestic Terrorism issued by the White House in June 2021. In addition to enhanced information sharing, federal law enforcement will be updating resources and providing training to financial institutions and their state, local, tribal, and territorial partners. Financial institutions that face multiple threats and are at risk of being compromised by malicious actors should take advantage of all available training and resources to mitigate potential risks and incorporate best practices shared by industry partners.

D. **Fraud** – Fraud is ubiquitous and continues to evolve. FinCEN, in response, has been issuing related advisories with respect to various schemes. In recent years, FinCEN has issued numerous advisories targeting COVID-19 economic impact payments, health insurance and health care, unemployment payments/insurance, counterfeit COVID-19 vaccine, market manipulation, and other cyber-enabled fraud schemes that should be reviewed for potential impacts to the customers of a financial institution. Many financial institutions are taking a proactive approach by partnering with regulatory agencies and law enforcement to educate senior citizen customers and other potentially vulnerable groups to protect them from becoming victims of these schemes.

E. **Transnational Criminal Organization (TCO) Activity** – The U.S. Department of Treasury has identified TCO activity as a high priority threat to national security. Given the significance and types of illicit activities in which TCOs engage, it is important to identify the variety of money laundering methods employed by these criminal organizations. Trade-based money laundering schemes often utilize professional money laundering networks that have shifted away from cash-intensive activities to avoid unnecessary attention.

F. **Drug Trafficking Organization (DTO) Activity** – As illicit drugs generate significant proceeds for DTOs, they have increasingly utilized money laundering networks in Asia (primarily China). These networks increasingly utilize trade-based money laundering schemes by using multiple front companies and couriers to deposit cash derived from the sale of narcotics to repatriate proceeds back to DTOs. FinCEN continues to issue advisories, guidance, and other directives, updated as needed, and these documents should be reviewed and disseminated as part of financial institutions' internal training efforts.

G. **Human Trafficking and Human Smuggling** – These illicit activities require housing and transportation to facilitate this crime. Criminal organizations have established shell companies to hide the true nature of their business and they receive payments in a variety of methods, such as funnel accounts and trade-based schemes. Cash transactions, virtual currency, and other digital transactions are all being utilized to channel illegal proceeds back to the criminal organizations. DTOs often supplement their drug smuggling business with ancillary activities such as human trafficking and smuggling. FinCEN Guidance for financial institutions initially published an advisory on Financial Schemes and Trafficking of Fentanyl on August 21, 2019, to describe transactions involving bank transfers or money service businesses such as money transmitters and online payment systems to evade BSA/AML requirements for reporting and recordkeeping. The initial guidance on Human Smuggling and Trafficking was published on September 11, 2014, and updated with a supplemental advisory on Identifying and Reporting Human Trafficking on October 15, 2020. These advisories contain useful case studies involving prepaid cards, mobile payments, and virtual currency as well as other information on reporting and submitting information to FinCEN.

H. Weapons Proliferation Financing – While these criminal activities may be difficult to detect, they require significant financial support and utilize global correspondent banking services. Vulnerabilities with correspondent banking, global supply chains, and transportation methods have been exploited by malicious actors in isolated countries such as Iran, North Korea, and Syria. In response, FinCEN continues to identify concerns and issue various advisories or guidance to support this national priority, and financial institutions with international customers should review these publications for applicability.

Risk-based AML/CFT Compliance Program

The AML Act requires a risk-based approach to each institution's compliance program. The risk-based approach must be determined through an effective risk assessment process that identifies and addresses the AML/CFT priorities. These national AML/CFT priorities need to be addressed and updated in the financial institution's policies, procedures, and risk assessment. Risk assessment methodologies must be revised as needed so they can be dynamic and reflect changes to national priorities as they are updated. The AML/CFT risk assessment must address each of these national public priorities specifically, and the overall compliance program posture needs to incorporate the bank's risk management strategies appropriately. The U.S. Department of Treasury is required to make changes to public priorities on a periodic basis and needs input and feedback from financial institutions to determine how to best modify or expand the priorities.

Risk assessments are now considered a mandatory pillar of each institution's compliance program. The risk assessment process must ensure an appropriate risk-based approach for the compliance program elements such as determining the scope of independent audit reviews, establishing appropriate internal controls, and specializing training efforts for different departments and employees. A grace period will be established after the system and processes are finalized by FinCEN; however, all financial institutions are encouraged to begin addressing these national priorities and requirements in the risk assessment process by year-end 2022. Future AML/CFT examinations review the effectiveness of risk assessments and the bank's overall risk-based processes.

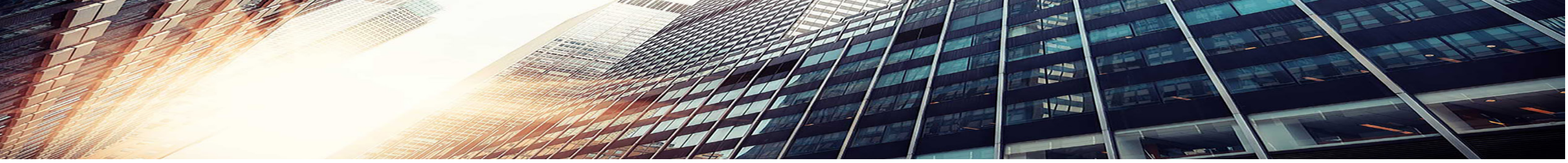
Corporate Transparency Act (CTA)

The Corporate Transparency Act of 2019 was originally passed by the U.S. Congress in October 2019 but did not take effect until January 1, 2021, as part of the NDAA of 2021. The CTA amends previous beneficial ownership recordkeeping requirements and introduces a new centralized FinCEN Exchange registry database system for beneficial ownership recordkeeping purposes. Once established, the FinCEN Exchange will facilitate a voluntary public-private information sharing partnership among law enforcement, federal financial regulatory agencies, and financial institutions. This registry will only be available to (1) law enforcement under specified conditions, (2) a federal functional regulatory, or (3) financial institutions with the customer's permission. Financial institutions will need to receive permission from the entity owner prior to accessing the national registry and validating the customer information.

Previously, banks and other non-bank financial institutions were responsible for ensuring beneficial ownership information was being captured and retained. Any corporation, limited liability company, or limited partnership required to file a certificate of formation with the Texas Secretary of State (SOS) will be subject to these new changes. If a trust is a partner (greater than or equal to 25%) in a legal entity that requires SOS formation, the appropriate ultimate beneficial ownership information will need to be filed with FinCEN once the final rules are implemented. The ultimate beneficial owners must provide personal identification information that a customer of a bank provides at account opening. For specific questions regarding related documentation for the Customer Identification Program (CIP), Know Your Customer (KYC), and Customer Due Diligence (CDD) requirements please refer to FinCEN resources or submit inquiries directly to FinCEN.

The new beneficial ownership registry and database system being developed will require coordination between FinCEN and the office of the Texas SOS. When an applicant is forming a new entity that will be registered with the SOS, the required FinCEN forms and information must also be filed to finalize the process. Once the first wave of regulations takes effect, existing reporting entities have one year to file their initial report to FinCEN, and annual updates will be required for any changes from the prior report on record. Affected entities, which could potentially cover regulated entities and applicants required to file with SOS/Treasury, should develop a new process and begin reviewing how this customer information will be updated.

Any entity that must be registered with the Texas SOS will also be required to file the applicant's personal identification information and documents (i.e., driver's license, passport, or other government-issued ID) with FinCEN once the final rules are implemented. Prior to January 1, 2010, a registered agent in Texas was not required to file a signed attestation providing evidence of consent to serve as an applicant for the entity and affirm they are the applicant on record. In the past, registered agents were not required to submit any personal identifying information and sometimes were unaware they were listed as the applicant or reg-



istered agent. There are 23 exemptions that exclude certain companies from reporting this information, which are generally for larger entities or entities already regulated by a state and/or federal agency. Maintaining awareness of these upcoming changes will improve the transition and required changes to internal policies, procedures, and processes.

Virtual Currency

The AML Act expands and reinforces FinCEN's authority to regulate virtual currency and businesses engaged in the trade of antiquities and art. Two provisions of the AML Act applicable to all financial institutions have been amended. The first amendment applies to the transmission of virtual currency. The definition of a financial institution includes a person or business that "*engages in the transmission of currency or funds*" and was modified to include the transmission of "*value that substitutes for currency,*" making clear that AML monitoring systems must cast a wider net to capture all relevant transactions. Any person "*engaged in the trade of antiquities, including any adviser, consultant or any other person who deals in the sale of antiquities*" was also added to the definition for a financial institution, therefore trade-based, anti-money laundering monitoring systems and training must be updated accordingly to include these types of businesses.

Virtual currency has the potential to evade Russian-related sanctions issued by OFAC. Recent FinCEN and Treasury guidance was issued regarding red flags, various tactics employed by Russian entities, and various resources such as an extensive section for frequently asked questions. The following resources were provided by the Treasury and can provide extensive insight into the various OFAC sanctions that have been issued and continue to be expanded:

- Ukraine-/Russia-related Sanctions | U.S. Department of the Treasury
- Russian Harmful Foreign Activities Sanctions | U.S. Department of the Treasury
- FinCEN Alert, FIN-2022-Alert001, March 7, 2022

The AML Act extends the extraterritorial jurisdiction of the United States, which may now issue subpoenas for any record related to a correspondent account *or any account of a foreign bank*, including records maintained outside of the U.S. if the records are the subject of an investigation involving a violation of a U.S. criminal law or violation of the BSA. Therefore, a foreign bank may be issued a subpoena for information related to one of its customers' account(s) even if no activity for that customer has been cleared through the bank's correspondent USD account. Failure to comply may result in sanctions, financial penalties, and in extreme cases, the Treasury may direct U.S. financial institutions to terminate their correspondent relationships with a foreign bank in noncompliance. This issue will continue to evolve as national interests must be balanced with international cooperation requirements, such that maintaining awareness of these changes is necessary to mitigate risk exposure.

BSA Advisory Group (BSAAG) on Technology, Innovation, and Communications

The AML Act encourages innovation in AML compliance efforts by requiring an innovation officer at each federal agency, establishing innovation labs at each federal functional regulator, and requiring a Federal Innovation Council to meet at least semi-annually. The Innovation Council will include participation by public and private entities, as well as law enforcement agencies to improve efficiency and collaboration. Texas banks and non-bank financial institutions are encouraged to participate and provide feedback. Additionally, given the elevated risk inherent in border locations, it is important to share "best practices" and improve collaboration efforts in higher risk locations.

Improving communications, oversight, and transparency is also a key component of the AML Act. The BSAAG is a subcommittee created by the AML Act focusing on advancing innovation and technology to enhance law enforcement's capabilities to combat financial crimes. A subcommittee of the BSAAG will work on

security, confidentiality implications, and information sharing issues which require as much industry input as possible. Financial institutions in Texas should monitor FinCEN developments and take advantage of opportunities to submit comments and influence the future direction of AML/CFT compliance.

The AML Act requires that every federal regulator appoint an Innovation Officer to promote technology for enhancing efficiency and collaboration efforts. Although it is not a formal requirement, all financial institutions could benefit from identifying an individual (or assigning a committee) to serve as an innovation officer for incorporating modern technology and services, and participating in national BSAAG meetings, committees, conferences, and councils. Texas banks and non-bank financial institutions have always been required to incorporate elevated AML/CFT standards and processes given the inherent geographical location risks, and any best practices/technologies that can be shared are encouraged because they may also have the potential for meaningful impact in enhancing national security interests.

For questions regarding any of the information above, please contact our BSA specialists at AML@dob.texas.gov.

Putting the "Community" in Community Banking

By: Gordon Anderson

First in a Two-Part Series

In this edition, we are highlighting Cameron and Hidalgo counties and the financial education efforts of community banks in these areas. Both counties have a comparatively young population with a historically limited exposure to financial education.

According to estimates from the U.S. Census Bureau, 29.3% and 31.6% of the counties' respective populations are under age 18. Both are heavily Hispanic, as 90% and 92.6% of residents are non-white Hispanic, respectively; 22.6% and 26.3% of residents are recent immigrants to the U.S.

Unfortunately, income levels in both counties lag that of the rest of the state. Cameron County residents earn, on average, a yearly income 64% of that of their fellow Texans, while the annual income of the average Hidalgo County resident is about 65% of that of the rest of the state.

The good news is that, as is so often the case, Texas community banks are jumping in to make a difference. This two-part series looks at four banks putting in the hard work to make the future much brighter for their customers – and customers to be. This first installment focuses on First Community Bank, San Benito and Texas Regional Bank, Harlingen.

FIRST COMMUNITY BANK

Headquartered in San Benito, First Community Bank maintains nine facilities, eight of which are in either Cameron or Hidalgo County. Besides its hometown, these communities include Brownsville, Harlingen, Los Fresnos, McAllen, and South Padre Island.

And for more than 10 years, the bank has been actively involved in each, with a special emphasis on financial education, according to Ricky Leal, Senior Vice President, Lending and CRA Officer.

"Our opportunities come to us in a variety of ways, but we are extremely active throughout our service area," Leal explains. He notes this includes not only elementary and high school presentations, but also more complex discussions with technical colleges, "lunch and learn" sessions for local chambers of commerce, book reading events at local parks, partnering with local United Way chapters for community activities, and much more.

"We have approached this in multiple ways," Leal says. "For non-recurring events, we have a 20- to 30-minute 'Financial Fitness' presentation that briefly touches on up to 20 topics and encourages students to learn more.

Ricky Leal covering the Fundamentals of Good Credit with an audience at a San Benito Chamber of Commerce meeting.

"For in depth financial education," he continues, "we've utilized a curriculum called 'Fundamentals of Good Credit.'" We do this in six sessions, about 30 to 45 minutes each, and usually taught one week at a time. For

Sandra Langley reading to students at Smarty Pants Day Care in Brownsville.

younger ages we have several financial themed books that we read to the kids and encourage discussion."

Leal says these include "The Go-Around Dollar", "If You Made A Million", and "Alexander, Who Used to Be Rich Last Sunday," most of which were distributed by the Texas Bankers Association and tailored to local needs, with the Independent Bankers Association of Texas contributing other resources.

The beauty of all this is that there is material for every age group.

"The Financial Fitness presentation can be used with adults and older kids," he says, "while the 'Fundamentals of Good Credit' sessions are best used with grades 9-12 and college age individuals. We've even made this presentation to teachers, coaches, and other school employees, 50 or 60 at a time. The books, of course, are best used with elementary aged kids."

He explains material designed for younger students focus on the basics, usually with a lot of pictures, customized for grades 1 through 5. But as basic as they may be, Leal feels the books accomplish one important thing.

"The books we read to the kids encourage a lot of discussion," he says. "I think this helps teachers meet the need to increase their student's critical thinking skills, which is so important. And I think it helps teachers reach and hold their attention just by having someone 'new' in the classroom. It breaks the routine."

Despite the focus on teachers and their importance as a link between the bank and students, Leal says there is another, equally important player often overlooked: the school principals.

"They really are the key, as they know exactly what – and who – they want on their campus and to serve what goal," he says. "They are very involved in all of this."

Like most businesses, COVID slowed down the bank's in-person efforts, but staff still managed to make a few Zoom presentations for a Texas State Technical College virtual event. "I'd much rather do these in person, but we are looking at opportunities to get back into classrooms starting this fall," Leal admits.

To Leal, it is obvious how local communities benefit from First Community Bank's efforts. But what does the bank receive?

"We'd like every person that participates in our programs to make healthy financial decisions or know where to find the information they need that would lead to that outcome," Leal says in summation.

Ricky Leal teaching financial literacy at Rodriguez Elementary in Harlingen.

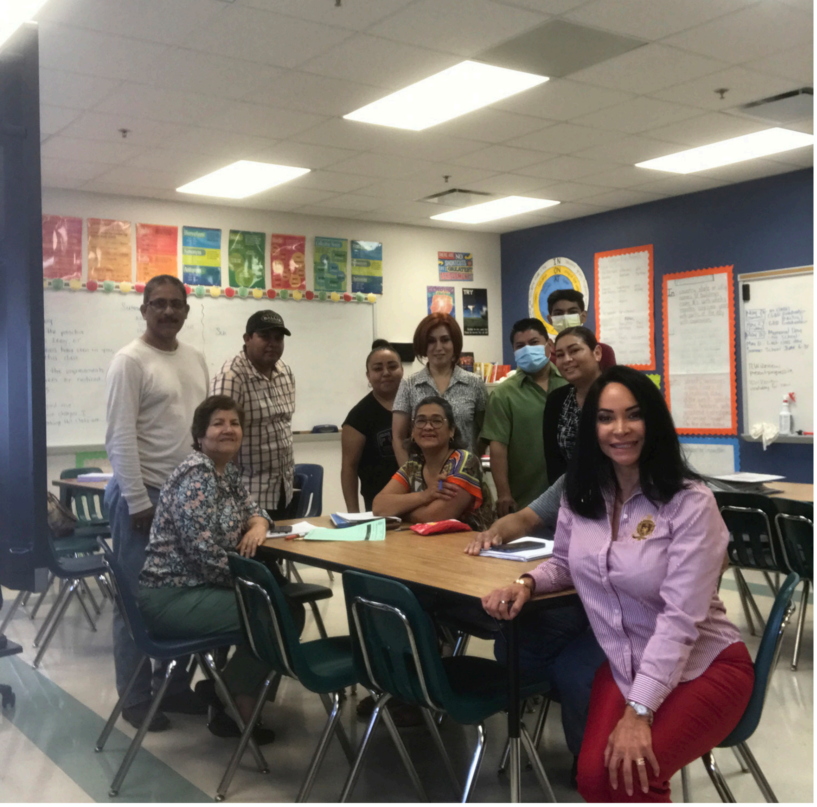
"Our employees spend a lot of time volunteering in our local communities, and financial literacy is one of the ways we give back," he says. "I feel like participants really appreciate receiving information from bankers who have seen how decisions affect outcomes, mostly good ones. The more we learn, the more likely we'll have a good outcome."

Texas Regional Bank

In addition to two loan production offices, Harlingen headquartered Texas Regional Bank operates 27 banking centers throughout South Texas, the Texas Hill Country, Houston, and the Dallas-Fort Worth area. Twelve of these facilities are located either in Cameron or Hidalgo County, with branches in Brownsville, Edinburg, McAllen, Mission, San Benito, Weslaco, and its hometown of Harlingen.

While many employees of Texas Regional Bank donate time to financial literacy, *Texas Bank Report* this month focuses on two: Diana Delaunay, First Vice President and Senior Branch Sales Officer; and Jamie L. Brown-Rosas, Assistant Vice President, Business Development Officer.

Talk about a dynamic duo: Both bring years of experience and an infectious energy to the cause. Delaunay, working in the



Diana Delaunay, FVP/Senior Branch Sales Officer, BISD Adult Continuing Education, we have a long-lasting partnership with Brownsville Independent School District's GED/ESL adult education programs. Twice a month we connect with hundreds of students ages 17 and older. These presentations may be a 45-minute bilingual class.

Brownsville branch, first received training to be a financial education provider 20 years ago while working for a series of large, national banks. Brown-Rosas, working out of the McAllen branch, leans on 16 years of financial education experience, 12 in a higher education setting and four at financial institutions.

Both remain focused on the bank's objective.

"Our overall goal is to educate, empower, inspire, and increase financial awareness," Delaunay explains. "We believe that having a powerful financial education is the first step towards true independence. Additionally, over the long term, it benefits the broader economy outlook for our community and helps creates new opportunities for businesses."

Texas Regional Bank takes a multi-prong approach to increasing financial literacy, according to Brown-Rosas. "Our 'menu' includes banking basics, such as how to create a budget; the difference between wants and needs; how to establish good credit and why it's important. Plus, we address more complex subjects such as elder financial abuse, financial planning, and how to save for retirement."

"We could put on an entire conference with our programs," she says.

From Delaunay's perspective, her efforts began years ago when the bank partnered with Brownsville Affordable Housing Corp. on a homebuyer workshop.

"We weren't there to sell anything, we simply wanted to target renters and provide guidance to first time homebuyers," she says. "We touched on what lenders look at when underwriting a mortgage, what responsibilities come with homeownership, and the importance of establishing a relationship with a bank. But these workshops really took off when our marketing staff got involved and set up a full curriculum."

"There is such a need for homebuyer education out there," she continues. "It is incredibly rewarding to see families, especially those with children, reach the stability that comes from owning your home."

In the time since, Delaunay says Texas Regional Bank has greatly expanded its reach. Besides the Brownsville ISD, she is actively involved with the district's GED/ESL adult education programs, elder day care facilities, local Boys and Girls Clubs, and many businesses throughout the Upper Valley through "lunch and Learn" sessions.

"These presentations may be a 45-minute bilingual class on budgeting, banking, and credit; how older individuals can protect their identity and assets; or a Saturday morning session in the office explain-

Rick Garcia, AVP/Wealth Management Advisor, Big Valley Auto Auction in Donna Texas, is conducting a "Lunch & Learn" financial literacy presentation for retirement planning. Many business clients with a large employee base, request these presentations.

ing digital banking," she explains, noting the bank uses the many resources provided by FDIC's "Money Smart" program, among other sources.

Delaunay goes on to say that once she receives a request for a presentation, the first task is to determine if there is a volunteer on staff with expertise in the specific topic. And when it comes to elementary schools, the fit becomes even better if the bank employee has a child the same age as his or her audience, or perhaps even has a child attending the same school.

"When our staff personally knows the school, and maybe even the classroom teacher, it really makes the logistics much easier," she says.

Like Delaunay, Brown-Rosas is a huge proponent of financial education.

"I feel Texas Regional Bank is a prime example of how the community rallies behind good causes," she states. "Customers want to know their bank is actively participating in outreach and community improvement. You don't realize how much the knowledge we impart is needed."

She, too, presents before a varied audience, which can range from UT-Rio Grande Valley, South Texas College, and the College of Health Care Professionals, and from retirees to local elementary schools.

"The word is really getting out there," she notes, "whether it's through word-of-mouth, social media, or on the broadcast news. We almost always invite the local news team when we make a presentation to the public. The more we're out there, the more people request a presentation."

For older residents of the lower valley, she says she emphasizes the importance of identity theft, good cybersecurity habits, and other concepts that may be new to her audience.

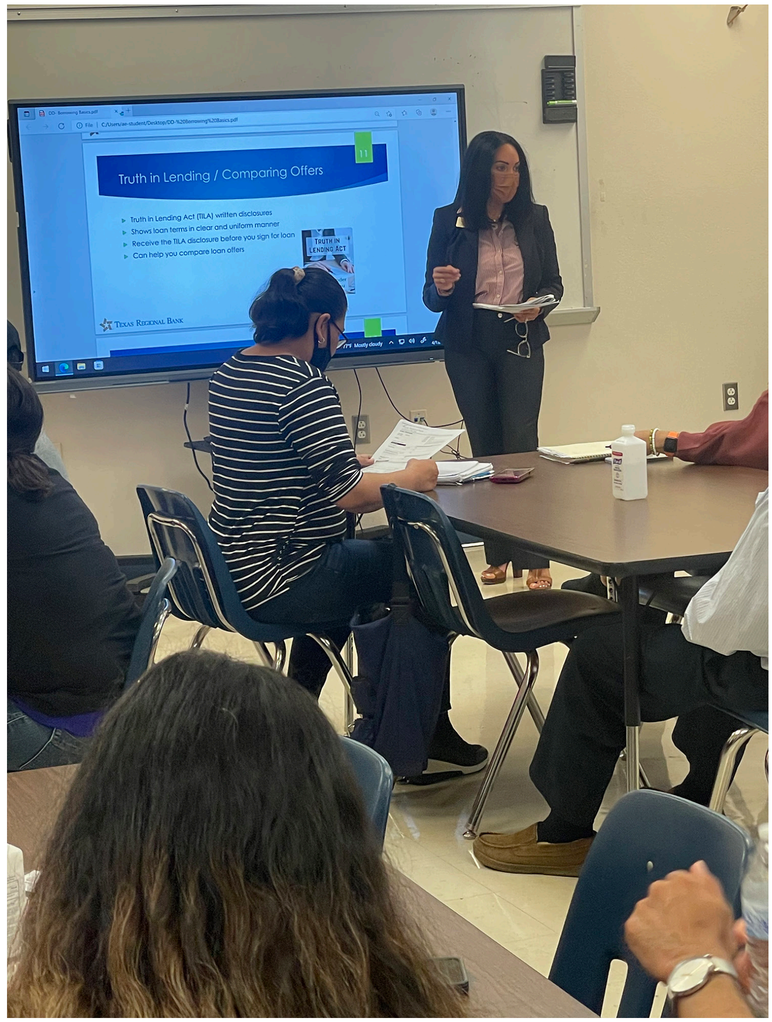
For the younger children, Brown-Rosas says Texas Regional Bank's classroom efforts complement teachers' goals to prepare students for the Texas Essential Knowledge and Skills tests, exams that include a personal financial education component for students in grades 5-8.

"We try to include in each presentation a set of math problems, adding in a little competition among the children, to generate discussion," she explains "For example, we will sometimes bring plastic piggy banks and offer them as prizes for the younger kids who interact the most, or correctly solve a problem. Teachers really appreciate this approach, as it is right up their alley in terms of improving math comprehension."

Texas Regional Bank's efforts are clearly hitting all the targets. The Independent Bankers Association of Texas in August awarded it a Gold Medal in the organization's *2022 Best of Community Banking Awards* competition for Financial Literacy. That is kind of a big deal!

As should be obvious, Leal, Delaunay, and Brown-Rosas all have one important thing in common, however: Each takes financial education very seriously, as well as the need for their respective banks to be invested in the communities they serve.

You might say both banks are putting the "community" in community banking.



Diana Delaunay, FVP/Senior Branch Sales Officer, BISD Adult Continuing Education – Teaching Borrowing Basics – many low-income individuals and economically impacted communities commonly don't participate in traditional banking or maintain accounts with mainstream lenders. We teach about credit, why good credit is important, types of loans and APRs.

Financial Highlights

TABLE I Quarterly Balance Sheet and Operating Performance Ratios for Texas State-Chartered Commercial Banks 6/30/2022 Through 6/30/2021					
ACCOUNT DESCRIPTIONS (IN MILLIONS OF $)	6/30/2022	3/31/2022	12/31/2021	9/30/2021	6/30/2021
Number of State-Chartered Banks	213	214	214	215	217
Total Assets of State-Chartered Banks	418,289	422,822	423,528	412,751	365,132
Number of Out-of-State, State-Chartered Banks Operating in Texas	48	48	48	48	48
Total Texas Assets of Out-of-State, State-Chartered Banks Operating in Texas	85,338	85,338	85,338	85,338	85,338
Subtotal	503,627	508,160	508,866	498,089	450,470
Less: Out-of-State Branch Assets/Deposits	(72,689)	(72,689)	(72,689)	(72,689)	(72,689)
**Total State Banks Operating in Texas	430,938	435,471	436,177	425,400	377,781
BALANCE SHEET (Tx. State-Chartered Banks)					
Interest-Bearing Balances	39,163	55,507	72,727	71,432	52,631
Federal Funds Sold	2,470	2,401	1,470	895	692
Trading Accounts	1,699	1,960	1,028	1,477	1,222
Securities Held-To-Maturity	23,464	22,269	17,707	17,232	16,091
Securities Available-for-Sale	86,121	84,948	79,379	73,868	65,594
Total Securities	109,585	107,217	97,086	91,100	81,685
Total Loans	236,714	226,620	224,316	221,489	203,121
Total Earning Assets	387,932	391,745	395,599	384,916	338,129
Premises and Fixed Assets	5,377	5,463	5,307	5,244	5,168
Total Assets	419,289	422,822	423,528	412,751	365,132
Demand Deposits	78,673	82,664	70,473	66,746	51,592
MMDAs	194,692	196,863	211,600	205,003	179,590
Other Savings Deposits	32,735	31,669	30,740	29,349	30,477
Total Time Deposits	35,745	35,601	33,833	35,063	34,006
Brokered Deposits	10,368	9,773	8,920	7,971	4,959
Total Deposits	357,609	363,127	360,992	349,668	308,524
Federal Funds Purchased	3,359	3,304	4,073	3,403	3,446
Other Borrowed Funds	11,807	7,651	7,556	7,634	5,479
Total Liabilities	378,669	379,652	377,664	366,828	322,564
Total Equity Capital	40,620	43,170	45,865	45,922	42,568
Loan Valuation Reserves	2,746	2,725	2,739	2,793	2,653
Total Primary Capital	43,366	45,895	48,604	48,715	45,221
Past Due Loans > 90 Days	189	220	225	315	404
Total Nonaccrual Loans	829	992	950	1,076	1,039
Total Other Real Estate	105	94	99	159	165
Total Charge-Offs	107	58	241	174	90
Total Recoveries	57	27	150	102	61
Net Charge-Offs	50	31	91	72	29
INCOME STATEMENT					
Total Interest Income	5,907	2,815	11,243	8,431	5,175
Total Interest Expense	376	158	715	556	340
Net Interest Income	5,531	2,657	10,528	7,875	4,835
Total Noninterest Income	1,938	948	4,124	3,126	2,030
Loan Provisions	104	14	(448)	(407)	(354)
Salary and Employee Benefits	2,587	1,303	5,111	3,822	2,390
Premises and Fixed Assets Expenses (Net)	466	235	935	697	446
All Other Noninterest Expenses	1,315	663	2,549	1,870	1,154
Total Overhead Expenses	4,368	2,201	8,595	6,389	3,990
Securities Gains (Losses)	(45)	(11)	43	45	22
Net Extraordinary Items	0	0	0	0	0
Net Income	2,433	1,157	5,374	4,151	2,670
Cash Dividends	1,364	633	2,719	1,568	791
RATIO ANALYSIS					
Loan/Deposit	66.19%	62.41%	62.14%	63.34%	65.84%
Securities/Total Assets	26.14%	25.36%	22.92%	22.07%	22.37%
Total Loans/Total Assets	56.46%	53.60%	52.96%	53.66%	55.63%
Loan Provisions/Total Loans	0.09%	0.02%	-0.20%	-0.24%	-0.35%
LVR/Total Loans	1.16%	1.20%	1.22%	1.26%	1.31%
Net Charge-Offs/Total Loans	0.02%	0.01%	0.04%	0.03%	0.01%
Nonperforming+ORE/Total Assets	0.27%	0.31%	0.30%	0.38%	0.44%
Nonperforming+ORE/Primary Capital	2.59%	2.85%	2.62%	3.18%	3.56%
Net Interest Margin	2.85%	2.71%	2.66%	2.72%	2.86%
Gross Yield	3.74%	3.56%	3.63%	3.72%	3.95%
Return on Assets	1.16%	1.09%	1.27%	1.34%	1.46%
Return on Equity	11.98%	10.72%	11.72%	12.02%	12.54%
Overhead Exp/TA	2.08%	2.08%	2.03%	2.06%	2.19%
Equity/Total Assets	9.69%	10.21%	10.83%	11.13%	11.66%
Primary Capital/Total Assets+LVR	10.28%	10.78%	11.40%	11.72%	12.30%

*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.

Financial Highlights

TABLE II
Comparative Statement of Condition
Commercial Banks Domiciled in Texas
June 30, 2021 and June 30, 2022

ACCOUNT DESCRIPTIONS (In Millions of $)	6/30/2022 STATE CHARTERED		6/30/2022 NATIONAL CHARTERED		6/30/2022 ALL BANKS		6/30/2021 ALL BANKS	
Number of Banks	213	% TA	157	% TA	370	% TA	376	% TA
BALANCE SHEET								
Interest-Bearing Balances	39,163	9.3%	17,631	11.9%	56,794	10.0%	76,938	14.3%
Federal Funds Sold	2,470	0.6%	608	0.4%	3,078	0.5%	2,384	0.4%
Trading Accounts	1,699	0.4%	16	0.0%	1,715	0.3%	1,300	0.2%
Securities Held-To-Maturity	23,464	5.6%	6,640	4.5%	30,104	5.3%	19,085	3.5%
Securities Available-For-Sale	86,121	20.5%	33,072	22.3%	119,193	21.0%	100,316	18.6%
Total Securities	109,585	26.1%	39,712	26.8%	149,297	26.3%	119,401	22.2%
Total Loans	236,714	56.5%	82,064	55.4%	318,778	56.2%	304,341	56.5%
Total Earning Assets	387,932	92.5%	140,015	94.5%	527,947	93.0%	503,064	93.4%
Premises & Equipment	5,377	1.3%	1,863	1.3%	7,240	1.3%	6,980	1.3%
TOTAL ASSETS	419,289	100.0%	148,167	100.0%	567,456	100.0%	538,773	100.0%
Demand Deposits	78,673	18.8%	37,669	25.4%	116,342	20.5%	88,938	16.5%
MMDAs	194,692	46.4%	40,768	27.5%	235,460	41.5%	239,949	44.5%
Other Savings Deposits	32,735	7.8%	22,501	15.2%	55,236	9.7%	52,333	9.7%
Total Time Deposits	35,745	8.5%	15,510	10.5%	51,255	9.0%	52,402	9.7%
Brokered Deposits	10,368	2.5%	683	0.5%	11,051	1.9%	8,406	1.6%
Total Deposits	357,609	85.3%	131,804	89.0%	489,413	86.2%	457,571	84.9%
Fed Funds Purchased	3,359	0.8%	1,665	1.1%	5,024	0.9%	4,870	0.9%
Other Borrowed Funds	11,807	2.8%	1,062	0.7%	12,869	2.3%	9,189	1.7%
TOTAL LIABILITIES	378,669	90.3%	135,440	91.4%	514,109	90.6%	478,518	88.8%
Equity Capital	40,620	9.7%	12,727	8.6%	53,347	9.4%	60,255	11.2%
Allowance for Loan/Lease Losses	2,746	0.7%	1,102	0.7%	3,848	0.7%	3,945	0.7%
Total Primary Capital	43,366	10.3%	13,829	9.3%	57,195	10.1%	64,200	11.9%
Past Due >90 Days	189		250		439		460	
Nonaccrual	829		467		1,296		1,649	
Total Other Real Estate	105		34		139		223	
Total Charge-Offs	107		47		154		157	
Total Recoveries	57		25		82		97	
INCOME STATEMENT	Y-T-D		Y-T-D		Y-T-D		Y-T-D	
Total Interest Income	5,907	100.0%	2,269	100.0%	8,176	100.0%	7,732	100.0%
Total Interest Expense	376	6.4%	131	5.8%	507	6.2%	538	7.0%
Net Interest Income	5,531	93.6%	2,138	94.2%	7,669	93.8%	7,194	93.0%
Total Noninterest Income	1,938	32.8%	889	39.2%	2,827	34.6%	3,027	39.1%
Loan Provisions	104	1.8%	67	3.0%	171	2.1%	(325)	-4.2%
Salary & Employee Benefits	2,587	43.8%	1,040	45.8%	3,627	44.4%	3,588	46.4%
Premises & Fixed Assets (Net)	466	7.9%	194	8.6%	660	8.1%	657	8.5%
All Other Noninterest Expenses	1,315	22.3%	647	28.5%	1,962	24.0%	1,828	23.6%
Total Overhead Expenses	4,368	73.9%	1,881	82.9%	6,249	76.4%	6,073	78.5%
Securities Gains(Losses)	(45)	-0.8%	1	0.0%	(44)	-0.5%	36	0.5%
Net Extraordinary Items	0	0.0%	0	0.0%	0	0.0%	0	0.0%
NET INCOME	2,433	41.2%	972	42.8%	3,405	41.6%	3,765	48.7%
Cash Dividends	1,364		345		1,709		1,096	
Average ROA	1.16%		1.31%		1.20%		1.40%	
Average ROE	11.98%		15.27%		12.77%		12.50%	
Average TA ($ Millions)	1,968		944		1,534		1,433	
Average Leverage	9.69%		8.59%		9.40%		11.18%	
Dividends/Net Income	56.06%		35.49%		50.19%		29.11%	

***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.