TEXANA BANK

To Whom It May Concern:

We as owners, directors, and managers of Texana Bank appreciate and understand far too well the importance of maintaining and appropriately managing a healthy level of capital. We also recognize the need for appropriate levels of capital for a safe and sound banking system. After all, is it not the entire industry that shoulders the heavy burden of costly regulatory guidance and increased FDIC premiums to cover failed institutions? We all have a vested interest in maintaining a healthy banking system. Our concern is not the need for healthy levels of capital, an operating principle we as managers fully embrace. However, it is the introduction of yet another set of complicated rules, misguided processes and standards, and more importantly, the unintended consequences of Basel III that brings us to writing this letter.

It is quite apparent that this will be nothing more than another set of convoluted "one size fits all" rule making from the top down. Community banks have been, throughout the worst economic crises since the 80's, the defibrillator, providing much needed capital to a flat lined economy. Basel III, perhaps inadvertently by design, was created to apply to the largest, internationally active banks. Community banks did not engage in the highly levered activities that brought us to the economic. These rules will not only impair any community bank's ability to operate profitably, but threaten their very existence.

Concerns:

Incorporating AOCI as Part of Regulatory Capital

The first detrimental flaw in the set of proposed rules in the introduction of Common Equity Tier 1 Capital (CET1), and more specifically, the inclusion of Accumulated Other Comprehensive Income (AOCI) in the calculation. This inclusion will cause significant volatility in regulatory capital balances and could rapidly deplete capital levels under certain economic conditions. AOCI for community banks, like ours, is made up of predominantly unrealized gains and losses. Moreover, we are currently in an interest rate environment too low to be sustained long term. As rates begin to rise, AOCI will fall due to the mark downs in the fair value of our securities. Therefore, through zero change in management practices and zero risk added to the balance sheet, capital will be significantly depleted. Under the new CET1 calculation, an increase in rates as much as 300 basis points will deplete our capital by over $2 million or 15%. As low as rates are today, this could be a very likely scenario for many community banks, including this one.

Moreover, with the regulatory consequences of undercapitalization, it will become necessary for community banks to allocate even more costly resources to managing this volatility. This will only punish otherwise healthy returns and reduce capital even more. Again, Basel III was created with only large banks in mind. These large financial institutions have the ability and the resources to mitigate these volatility risks; community banks do not.

Capital Conservation Buffer

Implementation of the capital conservation buffer will be difficult and needless. Many community banks will have to raise additional capital from outside sources to meet the new capital standards, let alone the addition of the conservation buffer. These banks will have a significant challenge in raising that capital,

Hwy. 80	Linden	Loan Operations	Spring Hill
910 E. Marshall Ave.	P.O. Box 546	P.O. Box 546	3814 Gilmer Rd.
Longview, TX 75601	Linden, TX 75563	Linden, TX 75563	Longview, TX 75604
(903) 553-9128	**(903) 756-5573**	**(903) 756-5573**	**(903) 295-0896**
Fax (903) 553-9616	**Fax (903) 756-5790**	**Fax (903) 756-5790**	**Fax (903) 295-0897**

as we know firsthand. Texana Bank has been on a large growth trajectory since 2005, and our single largest restraining factor has been capital. Without access to large, liquid sources of capital that large banks have, community banks are forced to raise capital through private placement; investor by investor. This method has proved very difficult, time consuming, and results take years. The other source of capital community banks realize is internal, through retention of earnings. In our current low rate environment, community bank's profitability has been diminished therefore the addition to capital has been extremely reduced.

This proposed rule would be particularly detrimental to any Subchapter S community banks. Imposing distribution prohibitions conflicts with the requirement that shareholders personally pay income taxes on earned income. Banks electing to be Subchapter S would especially need to be exempt from this proposed rule to allow distributions of earned income, regardless of capital levels, to shareholders in order for them to make timely payments on income tax.

New Risk Weights

The proposed risk weight framework under Basel III will be a heavy regulatory burden, penalizing community banks and jeopardizing the housing recovery. Increasing risk weights unnecessarily, as Basel III proposes, penalizes banks for providing consumers with balloon loans, interest only loans, and second liens. Not only will these banks be punished for loans already on the books, but due to the regulatory burden, banks will no longer be lending using these products robbing customers of many options for financing. Not only does this reduce bank income, but reduces the amount of capital in consumers' hands significantly slowing economic recovery even more. Because of the effect this will have on banks' liquidity, management costs, software upgrades to track these loans and loan to value ratios, not to mention the burden on capital ratios, many banks may choose to exit the residential loan market entirely. Second liens may also become extinct as they become too expensive for borrowers or as banks choose not to allocate additional capital to these balance sheet exposures. Again, this unnecessary proposed rule will only add a heavy burden to community banks and should be removed from Basel III.

Proposed Phase Out of Trust Preferred Securities

We also object to the proposed ten year phase out of instruments like trust preferred securities as a part of capital. TRUPS are a reliable source of capital for community banks that would be extremely difficult to replace. As discussed above, community banks have a very limited source of outside capital, and this would only add to that burden. It was the intent of the Collins amendment of the Dodd-Frank Act to permanently grandfather tier one treatment of TRUPS issued by bank holding companies between $500 million and $15 billion. Due to the fact that our bank, as well as many other community banks are under $500 million, our balance sheets would not be affected initially, which we applaud. However, just like us, many banks are on a growth trajectory and very soon could break through the $500 million mark. At that point any TRUPS held on the balance sheet would immediately be removed from tier 1 capital, bringing growth to a screeching halt, and possibly making an otherwise healthy bank undercapitalized because of a change in a simple calculation.

Conclusion

These proposed rules pose a threat to the livelihood and very existence of community banks. Basel III was developed with only large banks in mind, banks who have the resources and capabilities to manage these regulations and quick sources of capital should they become undercapitalized. With the proposed rules and new capital calculations, perfectly healthy and profitable community banks could soon be classified as undercapitalized. Without readily available sources of outside capital that large banks enjoy, these banks will have no other option but to suffer the regulatory consequences or submit to consolidation with a larger institution. Because of these reasons, we plead that common sense prevail and Basel III be either significantly changed or revoked.

Pat Rountree