# ANNUAL REPORT
## 2010

International Bancshares Corporation

*We do more*

# INTERNATIONAL BANCSHARES CORPORATION

ALL BANKS MEMBER FDIC
MEMBER BANKS:

**International Bank Of Commerce**
**1200 San Bernardo Avenue**
**(956) 722-7611**

**Laredo**
7002 San Bernardo Ave.
(956) 728-0060
1002 Matamoros
(956) 726-6622
1300 Guadalupe
(956) 726-6601
2418 Jacaman Rd.
(956) 764-6161
5300 San Dario Ste. 440D
(956) 728-0063
5300 San Dario Ste. 202
(956) 790-6500
9710 Mines Road
(956) 728-0092
4501 San Bernardo
(956) 722-0485
7909 McPherson Ave.
(956) 728-0064
2442 San Isidro Pkwy
(956) 726-6611
2415 S. Zapata Hwy.
(956) 728-0061
1320 San Dario Ave.
(956) 790-6511
5610 San Bernardo
(956) 726-6688
2320 Bob Bullock Lp 20
(956) 728-0062
4401 Highway 83 South
(956) 794-8140
1911 N.E. Bob Bullock
(956) 764-6171
4801 San Dario
(956) 794-8130
210 West Del Mar Blvd.
(956) 794-8145
2310 Saunders
(956) 794-8155

**Administration Center**
2418 Jacaman Rd. (Rear)
(956) 722-7611

**San Antonio**
130 East Travis
(210) 518-2500
5029 Broadway
(210) 518-2523
6630 Callaghan
(210) 369-2960
6301 NW Lp. 410 Ste. Q14
(210) 369-2911
2201 NW Military Dr.
(210) 366-0617
12400 Hwy. 281 North
(210) 369-2900
16339 Huebner Rd.
(210) 369-2974
7400 San Pedro, Ste. 608
(210) 369-2940
1500 NE Lp. 410
(210) 281-2430
10200 San Pedro Ave.
(210) 366-5400
18750 Stone Oak Pkwy Ste. 100
(210) 496-6111
5300 Walzem Rd.
(210) 564-2300
11831 Bandera Rd.
(210) 369-2980
15900 La Cantera Parkway Ste 10005
(210)354-6984
6909 N. Loop 1604 E Ste. E-01
(210) 369-2922
3119 SE Military Drive
(210) 354-6980
327 SW Loop 410
(210) 930-9825
2310 SW Military Dr. Ste #216
(210) 518-2558
6818 South Zarzamora
(210) 354-6988
999 E. Basse Rd. Ste. 150
(210) 369-2920
24165 IH 10 W. Ste. 300
(210) 369-2912
12018 Perrin Beitel Rd.
(210) 369-2917
6580 FM 78
(210) 930-9810
10718 Potranco Rd.
(210) 930-9820
2130 Culebra
(210) 930-9830
938 SW Military Dr.
(210) 930-9815
735 SE Military
(210) 930-9835
11002 Culebra
(210) 930-9850
6030 Montgomery Rd
(210) 930-9845
9900 Wurzbach Rd.
(210) 883-1410
1150 NW Loop 1604
(210) 930-9865
8503 NW Military Hwy
(210) 369-2918
9255 FM 471 West
(210) 883-1430
18140 San Pedro
(210) 883-1425
20935 Hwy 281 N., Ste 121
(210) 369-2914
4100 S. New Braunfels Ave.
(210) 883-1415
10660 FM 471
(210) 883-1420

**Service Center**
2416 Cee Gee
(210) 821-4700
8770 Tesoro
(210) 821-4700

**Luling**
200 S. Pecan St.
(830) 875-2445

**Marble Falls**
2401 Hwy. 281 North
(830) 693-4301

**San Marcos**
1081 Wonder World
(512) 353-1011

**New Braunfels**
955 N. Walnut Ave.
(830) 608-9665

**Shertz**
3800 Hwy 3009
(210) 354-6982
17460 IH 35 North
(210) 930-9855

**Boerne**
420 Bandera
(210) 249-1589

**Kyle**
5401 South FM 1626
(512) 397-4567

**McAllen**
One S. Broadway
(956) 686-0263
7124 N. 23rd.
(956) 630-9310
301 S. 10th St.
(956) 688-3610
3600 N.10th. St.
(956) 688-3690
2200 S. 10th St. (La Plaza East)
(956) 688-3670
2200 S. 10th St. (La Plaza West)
(956) 688-3660
2225 Nolana
(956) 688-3600
1200 E. Jackson
(956) 688-3685
2800 Nolana
(956) 688-3620
2900 W. Exp 83
(956) 630-9350
3601 Pecan Blvd.
(956) 630-9325

**Alamo**
1421 West Frontage Rd.
(956) 688-3645

**Edinburg**
400 S. Closner
(956) 688-3640
4101 S. McColl
(956) 630-9335
1724 W. University Dr. Ste. B
(956) 688-3680
2205 W. University Dr.
(956) 630-9340

**Mission**
900 N. Bryan Rd.
(956) 688-3630
200 E. Griffin Pkwy
(956) 632-3512
2410 E. Expressway 83
(956) 688-3625
1840 Palma Vista Dr.
(956) 630-9355
2409 E. Expressway 83
(956) 630-9315

**Pharr**
401 South Cage
(956) 688-3636
1007 North I Rd.
(956) 688-3655

**Weslaco**
606 S. Texas Blvd.
(956) 688-3605
1310 N. Texas
(956) 968-5551
1004 N. TX Blvd
(956) 968-5551
301 N. Westgate Drive
(956) 968-5551

**Hidalgo**
1023 S. Bridge
(956) 688-3665

**San Juan**
108 E. FM 495
(956) 630-9320

**Palmhurst**
215 E. Mile 3 Rd.
(956) 688-3675

**Penitas**
1705 Expressway 83
(956) 583-9964

**Corpus Christi**
221 S. Shoreline
(361) 888-4000
6130 S. Staples
(361) 991-4000
4622 Everhart
(361) 903-7265
14066 Northwest Blvd.
(361) 903-7285

**Flour Bluff**
1317 Waldron Road
(361) 886-9950

**Sinton**
301 West Sinton
(361) 364-1230

**Rockport**
2701 Hwy. 35 N.
(361) 729-0500
2431 Hwy. 35
(361) 729-0500

**Aransas Pass**
2501 W. Wheeler
(361) 729-0500

**Portland**
1800 US Hwy 181
(361) 886-9910

**Port Lavaca**
311 N. Virginia St.
(361) 552-9771
101 Calhoun Plaza
(361) 553-4211

**Bay City**
1916 7th Street
(979) 245-5781
2700 7th St.
(979) 244-7410

**Victoria**
6411 N. Navarro
(361) 575-8394
6106 N. Navarro
(361) 573-8035
1505 E. Rio Grande St.
(361) 573-8011

**Houston**
5615 Kirby Dr.
(713) 526-1211
1630 Spencer Highway
(713) 535-8344
8203 S. Kirkwood
(713) 285-2163
1001 McKinney Ste. 150
(713) 285-2139
5250 FM 1640
(713) 285-2177
1777 Sage Rd.
(713) 285-2133
3200 Woodridge, Ste. 1350
(713) 285-2255
3939 Montrose Ste. W
(713) 285-2195
5085 Westheimer Ste. 4640
(713) 285-2294
1545 Eldridge Parkway
(713) 285-2042
12400 FM 1960 W.
(713) 285-2212
7747 Kirby Dr.
(713) 285-2118
10251 Kempwood
(713) 535-8330
10100 Beechnut
(713) 535-8311
1630 Spencer Highway
(713) 535-8344
3111 Woodridge #500
(713) 535-8350
9710 Katy Freeway
(713) 535-8335
4955 Hwy 6 N.
(713) 535-8320
1550 Fry Rd
(713) 535-8410

**Sugarland**
11565 State Hwy 6
(713) 285-2203
10570 State Hwy 6
(713) 285-2285

**League City**
2955 S. Gulf Freeway
(713) 285-2086

**Friendswood**
3135 FM 528
(713) 285-2235

**Kingwood**
4303 Kingwood Dr.
(713) 525-8301

**The Woodlands**
9595 Six Pines Rd.
(713) 535-8340

**College Station**
1900 Texas Avenue
(979) 764-7264

**Bryan**
725 E. Villa Maria
(979) 764-9264

**Galveston**
2931 Central City Blvd.
(409) 741-9573
500 Seawall Blvd., Ste. 200
(409) 763-2254

**Cypress**
24224 NW Freeway
(713) 535-8370

**Spring**
7310 Louetta
(713) 535-8420
10019 Louetta
(713) 535-8390

**Humble**
7405 FM 1960 East
(713) 535-8360

**Wharton**
1616 North Alabama
(979) 282-2233

**Pearland**
2805 Business Center Drive
(713) 535-8380

**El Campo**
306 N. Mechanic
(979) 543-1039

**Katy**
6711 Cinco Ranch
(713) 285-2090
544 West Grand Parkway
(713) 285-2034

**Lake Jackson**
212 That Way
(979) 297-2466

**Angleton**
200 East Mulberry
(979) 849-7711

**Freeport**
1208 N. Brazosport Blvd.
(979) 233-2677

**Dickinson**
2301 West FM 646
(713) 285-2015

## International Bank Of Commerce
**1200 San Bernardo Avenue**
**(956) 722-7611**

**Pasadena**
6210 Fairmont Parkway
(713) 535-8358

**Missouri City**
8900 Hwy 6
(713) 535-8425

**Eagle Pass**
2395 E. Main Street
(830) 773-2313

2538 E. Main Street
(830) 773-2313

439 Main Street
(830) 773-2313

2305 Del Rio Blvd.
(830) 773-2313

455 S. Bibb Ave. Ste. 502
(830) 773-4930

2135 East Main Street
(830) 773-4823

**Del Rio**
2410 Dodson St.
(830) 775-4265

1507 Veteran's Blvd
(830) 775-4265

2205 Veterans Blvd, Suite E9
(830) 775-4265

**Uvalde**
3100 E. Hwy. 90
(830) 278-8045

2065 E. Main St.
(830) 278-8045

227 E. Main St.
(830) 773-2313

**Austin**
816 Congress Ave., Ste. 100
(512) 397-4506

10405 FM 2222
(512) 397-4584

2817 E. Cesar Chavez
(512) 320-9650

6001 Airport Blvd. Ste. 2390
(512) 397-4542

12625 North IH 35 Bldg. D
(512) 397-4570

11400 Burnett Road Bldg. 46
(512) 397-4595

7112 Ed Bluestein #125
(512) 397-4545

9900 South IH 35 Southbound Svc Rd
(512) 397-4530

12407 N Mopac Expressway
(512) 320-9535

**Bastrop**
701 W. Hwy 71
(512) 308-9412

**Buda**
15300 IH 35 South
(512) 295-6368

**Georgetown**
1101 South IH 35
(512) 863-9300

**Cedar Park**
301 W. Whitestone Blvd
(512) 397-4552

11200 Lakeline Mall Dr.
(512) 397-4590

170 E. Whitestone Blvd
(512) 320-9510

**Round Rock**
1850 Gattis School Rd.
(512) 397-4521

**Leander**
651 N. US Highway 183
(512) 397-4560

1695 US Hwy 183
(512) 320-9089

**Taylor**
100 NW Carlos Parker Blvd.
(512) 397-4576

**Oklahoma**

**Ardmore**
313 W. Broadway
(580) 223-0345

2302 12th Ave.
(580) 223-0345

**Broken Arrow**
6412 S. Elm Pl.
(918) 497-2488

8112 Garnett Rd.
(918) 497-2840

**Chickasha**
628 Grand Ave.
(405) 841-2282

**Claremore**
1050 N. Lynn Riggs Blvd.
(918) 497-2464

**Clinton**
1002 W. Frisco Ave.
(580) 323-0730

**Duncan**
1006 Main
(580) 255-8187

2311 N. Hwy 81
(580) 255-9055

**Edmond**
1812 SE 15th St.
(405) 775-8061

421 S. Santa Fe Ave.
(405) 841-2130

**Grove**
100 E. 3rd St.
(918)786-4438

**Guthrie**
120 N. Division St.
(405) 841-2304

**Tulsa**
2808 E. 101st St.
(918) 497-2821

1951 S. Yale Ave.
(918) 497-2452

4202 S. Garnett
(918) 497-2883

2250 E. 73rd St
(918) 497-2405

11 E. 5th St.
(918) 497-2462

8202 E. 71st St
(918) 497-2476

5302 E. Skelly Dr.
(918) 497-2472

14002 E. 21st, Suite 1170
(918) 497-2850

**Chandler**
3108 E. First St.
(405) 258-2351

**Oklahoma City**
3817 NW Expressway
(405) 775-8051

100 W. Park Ave.
(405) 841-2288

5701 N. May Ave.
(405) 841-2241

10500 S. Pennsylvania Ave
(405) 841-2266

2301 N. Portland Ave.
(405) 841-2116

12241 N. May Ave.
(405) 841-2341

6233 NW Expressway
(405) 841-2294

2501 W. Memorial Rd. Ste. 105
(405) 775-1730

4902 N. Western Ave.
(405) 841-2286

14001 N. McArthur Blvd
(405) 775-1710

**Lawton**
2101 W. Gore
(520) 250-4322

6425 NW Cache Rd.
(520) 520-4322

200 SW C. Ave., Ste 10
(520) 250-2265

**Miami**
2520 N. Main
(918) 542-4411

**Midwest City**
414 N. Air Depot Blvd.
(405) 841-2345

2200 S. Douglas Blvd.
(405) 775-8057

**Moore**
513 NE 12th
(405) 841-2308

901 SW 19th
(405) 775-1720

**Pauls Valley**
700 W. Grant Ave.
(405) 238-7318

**Purcell**
430 Lincoln St.
(405) 775-8094

2015 S. Green
(405) 775-1782

**Sand Springs**
800 E. Charles Page Blvd.
(918) 497-2468

3402 State Hwy. 97
(918) 497-2466

**Sapulpa**
911 E. Taft St.
(918) 497-2465

**Shawnee**
2512 N. Harrison Ave.
(405) 775-8067

**Sulphur**
2009 W. Broadway Ave.
(580) 622-3172

**Weatherford**
109 E. Franklin Ave.
(580) 772-7441

**Yukon**
1203 Cornwell Dr.
(405) 775-1713

**Stillwater**
1900 N. Perkins
(405) 372-0889

**Owasso**
9350 N. Garnett
(918) 497-2833

**Elk City**
1504 W. 3rd St.
(580) 225-7200

**Norman**
2403 W. Main St.
(405) 841-4744

**Lindsey**
211 E. Cherokee
(405) 756-4494

**Muskogee**
3143 Azalea Park Drive
(918) 497-2492

**Bixby**
11886 S. Memorial
(918) 497-2855

**Bethany**
7723 NW 23rd St.
(405) 841-2367

## Commerce Bank
**5800 San Dario**
**Laredo, Texas 78041**
**(956) 724-1616**

2120 Saunders
(956) 724-1616

2302 Blaine St.
(956) 724-1616

1200 Welby Court
(956) 724-1616

## International Bank of Commerce, Brownsville
**1600 Ruben Torres Blvd.**
**Brownsville, TX 78522-1831**
**(956) 547-1000**

1623 Central Blvd.
(956) 547-1000

4520 E. 14th St.
(956) 547-1000

630 E. Elizabeth St.
(956) 547-1000

2370 N. Expressway
(956) 547-1000

3600 W. Alton Gloor Blvd.
(956) 547-1000

79 E. Alton Gloor Blvd
(956) 547-1000

7480 S. HWY 48
(956) 547-1000

2721 Boca Chica Blvd
(956) 547-1000

2250 Boca Chica Blvd
(956) 547-1000

**Harlingen**
501 S. Dixieland Rd.
(956) 428-6902

902 N. 77th Sunshine Strip
(956) 428-6454

1801 W. Lincoln
(956)428-4559

**South Padre Island**
911 Padre Blvd.
(956) 761-6156

**Port Isabel**
1401 W. Hwy. 100
(956) 943-2108

## International Bank of Commerce, Zapata
**U.S Hwy. 83 @ 10th Ave.**
**Zapata, TX 78076**
**(956) 765-8361**

**Roma**
1702 Grant St.
(956) 849-1047

**Alice**
2001 E. Main St.
(361) 661-1211

**Rio Grande City**
4015 E. Hwy. 83
(956) 487-5531

4534 E. Hwy. 83
(956) 487-4434

4031 E. Hwy 83
(956) 487-5535

**Hebbronville**
401 N. Smith Ave.
(361) 527-2645

**Kingsville**
1320 General Cavazos Blvd
(361) 516-1040

715 W. Santa Gertrudis
(361) 516-1040

**Freer**
405 S. Norton
(361) 661-1211

**Beeville**
802 E. Houston St.
(361) 358-8700

302 N. St. Mary's Street
(361) 358-8700

100 E. Houston
(361) 358-8700

**INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES**
**(Consolidated)**

The following consolidated selected financial data is derived from the Corporation's audited financial statements as of and for the five years ended December 31, 2010. The following consolidated financial data should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the Consolidated Financial Statements and related notes in this report.

## SELECTED FINANCIAL DATA

| | AS OF OR FOR THE YEARS ENDED DECEMBER 31, | | | | |
|---|---|---|---|---|---|
| | 2010 | 2009 | 2008 | 2007 | 2006 |
| | (Dollars in Thousands, Except Per Share Data) | | | | |
| **STATEMENT OF CONDITION** | | | | | |
| Assets | $11,943,469 | $11,762,543 | $12,439,341 | $11,167,161 | $10,911,454 |
| Net loans | 5,325,521 | 5,571,869 | 5,799,372 | 5,474,902 | 4,970,273 |
| Deposits | 7,599,558 | 7,178,007 | 6,858,784 | 7,157,606 | 6,989,918 |
| Other borrowed funds | 1,026,780 | 1,347,625 | 2,522,986 | 1,456,936 | 2,095,576 |
| Junior subordinated deferrable interest debentures | 201,117 | 201,082 | 201,048 | 200,929 | 210,908 |
| Shareholders' equity | 1,459,217 | 1,407,470 | 1,257,297 | 935,905 | 842,056 |
| **INCOME STATEMENT** | | | | | |
| Interest income | $ 458,769 | $ 527,377 | $ 564,603 | $ 643,573 | $ 609,073 |
| Interest expense | 114,036 | 139,796 | 231,731 | 333,340 | 319,588 |
| Net interest income | 344,733 | 387,581 | 332,872 | 310,233 | 289,485 |
| Provision (credit) for probable loan losses | 22,812 | 58,833 | 19,813 | (1,762) | 3,849 |
| Non-interest income | 218,784 | 201,013 | 189,809 | 165,363 | 176,971 |
| Non-interest expense | 339,725 | 309,031 | 301,226 | 300,282 | 288,717 |
| Income before income taxes | 200,980 | 220,730 | 201,642 | 177,076 | 173,890 |
| Income taxes | 70,957 | 77,988 | 69,530 | 55,764 | 56,889 |
| Net income | 130,023 | 142,742 | 132,112 | 121,312 | 117,001 |
| Preferred stock dividends and discount accretion | 13,126 | 12,984 | — | — | — |
| Net income available to common shareholders | $ 116,897 | $ 129,758 | $ 132,112 | $ 121,312 | $ 117,001 |
| Per common share (Note 1): | | | | | |
| Basic | $ 1.72 | $ 1.90 | $ 1.93 | $ 1.76 | $ 1.68 |
| Diluted | $ 1.72 | $ 1.90 | $ 1.92 | $ 1.75 | $ 1.67 |

Note 1: Per share information has been re-stated giving retroactive effect to stock dividends distributed.

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Management's discussion and analysis represents an explanation of significant changes in the financial position and results of operations of International Bancshares Corporation and subsidiaries (the "Company" or the "Corporation") on a consolidated basis for the three-year period ended December 31, 2010. The following discussion should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2010, and the Selected Financial Data and Consolidated Financial Statements included elsewhere herein.

### Special Cautionary Notice Regarding Forward Looking Information

Certain matters discussed in this report, excluding historical information, include forward-looking statements, within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and are subject to the safe harbor created by these sections. Although International Bancshares Corporation (the "Company") believes such forward-looking statements are based on reasonable assumptions, no assurance can be given that every objective will be reached. The words "estimate," "expect," "intend," "believe" and "project," as well as other words or expressions of a similar meaning are intended to identify forward-looking statements. Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date of this report. Such statements are based on current expectations, are inherently uncertain, are subject to risks and should be viewed with caution. Actual results and experience may differ materially from the forward-looking statements as a result of many factors.

Risk factors that could cause actual results to differ materially from any results that are projected, forecasted, estimated or budgeted by the Company in forward-looking statements include, among others, the following possibilities:

- Local, regional, national and international economic business conditions and the impact they may have on the Company, the Company's customers, and such customers' ability to transact profitable business with the Company, including the ability of its borrowers to repay their loans according to their terms or a change in the value of the related collateral.
- Volatility and disruption in national and international financial markets.
- Government intervention in the U.S. financial system.
- The Company relies, in part, on external financing to fund the Company's operations and the unavailability of such funds in the future could adversely impact the Company's growth strategy and prospects.
- Changes in consumer spending, borrowings and savings habits.
- Changes in interest rates and market prices, which could reduce the Company's net interest margins, asset valuations and expense expectations, including, without limitation, the repeal of federal prohibitions on the payment of interest on demand deposits.
- Changes in the capital markets utilized by the Company and its subsidiaries, including changes in the interest rate environment that may reduce margins.
- Changes in state and/or federal laws and regulations to which the Company and its subsidiaries, as well as their customers, competitors and potential competitors, are subject, including, without limitation, changes in the accounting, tax and regulatory treatment of trust preferred securities, as well as changes in banking, tax, securities, insurance and employment, environmental and immigration laws and regulations and the risk of litigation that may follow.

- Changes in U.S.—Mexico trade, including, without limitation, reductions in border crossings and commerce resulting from the Homeland Security Programs called "US-VISIT," which is derived from Section 110 of the Illegal Immigration Reform and Immigrant Responsibility Act of 1996.
- The loss of senior management or operating personnel.
- Increased competition from both within and outside the banking industry.
- The timing, impact and other uncertainties of the Company's potential future acquisitions including regulatory restrictions, the Company's ability to identify suitable potential future acquisition candidates, the success or failure in the integration of their operations and the Company's ability to maintain its current branch network and to enter new markets successfully and capitalize on growth opportunities.
- Changes in the Company's ability to pay dividends on its Preferred Stock or Common Stock.
- Additions to the Company's loan loss allowance as a result of changes in local, national or international conditions which adversely affect the Company's customers, including, without limitation, lower real estate values or environmental liability risks associated with foreclosed properties.
- Greater than expected costs or difficulties related to the development and integration of new products and lines of business.
- Impairment of carrying value of our goodwill could negatively impact our earnings and capital.
- Changes in the soundness of other financial institutions with which the Company interacts.
- Political instability in the United States or Mexico.
- Technological changes or system failure or breaches of our network security could subject us to increased operating costs as well as litigation and other liabilities.
- Acts of war or terrorism.
- Natural disasters.
- Reduced earnings resulting from the write down of the carrying value of securities held in our securities available-for-sale portfolio following a determination that the securities are other-than-temporarily impaired.
- The effect of changes in accounting policies and practices as may be adopted by the regulatory agencies, as well as the Public Company Accounting Oversight Board, the Financial Accounting Standards Board and other accounting standards setters.
- The costs and effects of regulatory developments, including the resolution of regulatory or other governmental inquiries and the results of regulatory examinations or reviews.
- The effect of final rules amending Regulation E that prohibit financial institutions from charging the consumer fees for paying overdrafts on ATM and one-time debit card transactions, unless the consumer consents or opts-in to the overdraft service for those types of transactions, as well as, the effect of the FDIC Overdraft Payment Supervisory Guidance and any other regulatory or legal developments that limit overdraft services.
- The reduction of income and possible increase in required capital levels related to the adoption of new legislation, including without limitation the Dodd-Frank Regulatory Reform Act and the implementing rules and regulations that will be adopted in the future, including the Federal Reserve's proposed rule that would establish debit card interchange fee standards and prohibit network exclusivity arrangements and routing restrictions that may negatively affect interchange

revenue from debit card transactions as well as revenue from consumer services and may required increased levels of capital.

- The Company may be adversely affected by its continued participation in the Capital Purchase Program (“CPP”).
- The Company’s success at managing the risks involved in the foregoing items, or a failure or circumvention of the Company’s internal controls and risk management, policies and procedures.

Forward-looking statements speak only as of the date on which such statements are made. It is not possible to foresee or identify all such factors. The Company makes no commitment to update any forward-looking statement, or to disclose any facts, events or circumstances after the date hereof that may affect the accuracy of any forward-looking statement, unless required by law.

**Summary of Recent Legislation**

On July 21 2010, sweeping financial regulatory reform legislation entitled the “Dodd-Frank Wall Street Reform and Consumer Protection Act” (the “Dodd-Frank Regulatory Reform Act”) was signed into law. The Dodd-Frank Regulatory Reform Act implements far-reaching changes across the financial regulatory landscape, including provisions that, among other things, will:

- Centralize responsibility for consumer financial protection by creating a new agency, the Consumer Financial Protection Bureau, responsible for implementing, examining and enforcing compliance with federal consumer financial laws.
- Restrict the preemption of state law by federal law and disallow subsidiaries and affiliates of banks from availing themselves of such preemption.
- Apply the same leverage and risk-based capital requirements that apply to insured depository institutions to most bank holding companies.
- Require each federal bank regulatory agency to seek to make its capital requirements for banks countercyclical so that capital requirements increase in times of economic expansion and decrease in times of economic contraction.
- Require financial holding companies, such as the Company, to be well-capitalized and well-managed. Bank holding companies and banks must also be both well-capitalized and well-managed in order to acquire banks located outside their home state.
- Change the assessment base for federal deposit insurance from the amount of insured deposits to consolidated assets less tangible capital, eliminate the ceiling on the size of the Deposit Insurance Fund (“DIF”) and increase the floor of the size of the DIF.
- Impose comprehensive regulation of the over-the-counter derivatives market, which would include certain provisions that would effectively prohibit insured depository institutions from conducting certain derivatives businesses in the institution itself.
- Implement corporate governance revisions, including executive compensation and proxy access by shareholders, provisions that apply to all public companies, not just financial institutions.
- Make permanent the $250,000 limit for federal deposit insurance and increase the cash limit of Securities Investor Protection Corporation protection from $100,000 to $250,000 and provide unlimited federal deposit insurance until January 1, 2013 for non-interest bearing demand transaction accounts at all insured depository institutions.
- Repeal the federal prohibitions on the payment of interest on demand deposits, thereby permitting depository institutions to pay interest on business transaction and other accounts.

- Amend the Electronic Fund Transfer Act ("EFTA") to, among other things, give the Federal Reserve the authority to establish rules regarding interchange fees charged for electronic debit transactions by payment card issuers having assets over $10 billion and to enforce a new statutory requirement that such fees be reasonable and proportional to the actual cost of a transaction to the issuer.
- Increase the authority of the Federal Reserve to examine the Company and its non-bank subsidiaries.

Many aspects of the Dodd-Frank Regulatory Reform Act are subject to rulemaking and will take effect over several years, making it difficult to anticipate the overall financial impact on the Company, its customers or the financial industry more generally. Provisions in the legislation that affect deposit insurance assessments, payment of interest on demand deposits and interchange fees could increase the costs associated with deposits as well as place limitations on certain revenues those deposits may generate. Provisions in the legislation that may require revisions to the capital requirements of the Company could require the Company to seek other sources of capital in the future.

**Overview**

The Company, which is headquartered in Laredo, Texas, with 278 facilities and 440 ATMs, provides banking services for commercial, consumer and international customers of South, Central and Southeast Texas and the State of Oklahoma. The Company is one of the largest independent commercial bank holding companies headquartered in Texas. The Company, through its bank subsidiaries, is in the business of gathering funds from various sources and investing those funds in order to earn a return. The Company either directly or through a bank subsidiary owns two insurance agencies, a liquidating subsidiary, a broker/dealer and a fifty percent interest in an investment banking unit that owns a broker/dealer. The Company's primary earnings come from the spread between the interest earned on interest-bearing assets and the interest paid on interest-bearing liabilities. In addition, the Company generates income from fees on products offered to commercial, consumer and international customers.

A primary goal of the Company is to grow net interest income and non-interest income while adequately managing credit risk, interest rate risk and expenses. Effective management of capital is a critical objective of the Company. A key measure of the performance of a banking institution is the return on average common equity ("ROE"). The Company's ROE for the year ended December 31, 2010 was 9.43% as compared to 11.10% for the year ended December 31, 2009.

The Company is very active in facilitating trade along the United States border with Mexico. The Company does a large amount of business with customers domiciled in Mexico. Deposits from persons and entities domiciled in Mexico comprise a large and stable portion of the deposit base of the Company's bank subsidiaries. The Company also serves the growing Hispanic population through the Company's facilities located throughout South, Central and Southeast Texas and the State of Oklahoma.

Expense control is an essential element in the Company's long-term profitability. As a result, the Company monitors the efficiency ratio, which is a measure of non-interest expense to net interest income plus non-interest income closely. The Company's efficiency ratio has been negatively impacted over the last few years because of the Company's branch expansion which has added a total of 18 branches during 2009 and 2010. During expansion periods, the Company's efficiency ratio will suffer but the long-term benefits of the expansion should be realized in future periods and the benefits should positively impact the efficiency ratio in future periods. The Company monitors this ratio over time to assess the Company's efficiency relative to its peers taking into account the Company's branch expansion. The Company uses this measure as one factor in determining if the Company is accomplishing its long-term goals of providing superior returns to the Company's shareholders.

## Results of Operations

### Summary

### Consolidated Statements of Condition Information

| | December 31, 2010 | December 31, 2009 | Percent Increase (Decrease) |
|---|---|---|---|
| | (Dollars in Thousands) | | |
| Assets | $11,943,469 | $11,762,543 | 1.5% |
| Net loans | 5,325,521 | 5,571,869 | (4.4) |
| Deposits | 7,599,558 | 7,178,007 | 5.9 |
| Other borrowed funds | 1,026,780 | 1,347,625 | (23.8) |
| Junior subordinated deferrable interest debentures | 201,117 | 201,082 | — |
| Shareholders' equity | 1,459,217 | 1,407,470 | 3.7 |

### Consolidated Statements of Income Information

| | Year Ended December 31, 2010 | Year Ended December 31, 2009 | Percent Increase (Decrease) 2010 vs. 2009 | Year Ended December 31, 2008 | Percent Increase (Decrease) 2009 vs. 2008 |
|---|---|---|---|---|---|
| | (Dollars in Thousands) | | | | |
| Interest income | $458,769 | $527,377 | (13.0)% | $564,603 | (6.6)% |
| Interest expense | 114,036 | 139,796 | (18.4) | 231,731 | (39.7) |
| Net interest income | 344,733 | 387,581 | (11.1) | 332,872 | 16.4 |
| Provision for probable loan losses | 22,812 | 58,833 | (61.2) | 19,813 | 196.9 |
| Non-interest income | 218,784 | 201,013 | 8.8 | 189,809 | 5.9 |
| Non-interest expense | 339,725 | 309,031 | 9.9 | 301,226 | 2.6 |
| Net income | 130,023 | 142,742 | (8.9) | 132,112 | 8.0 |
| Net income available to common shareholders | 116,897 | 129,758 | (9.9) | 132,112 | (1.8) |
| Per common share: | | | | | |
| Basic | $ 1.72 | $ 1.90 | (9.5)% | $ 1.93 | (1.6)% |
| Diluted | 1.72 | 1.90 | (9.5) | 1.92 | (1.0) |

### Net Income

Net income available to common shareholders for the year ended December 31, 2010 decreased by 9.9% as compared to the same period in 2009. Net income for the year ended December 31, 2010 was positively affected by gains on investment securities sales totaling $21.6 million, net of tax. The sales of the securities were to facilitate a re-positioning of the Company's investment portfolio. Net income was negatively affected by an additional reserve of $21.8 million that the Company recorded during the first quarter of 2010 in connection with a dispute related to certain tax matters that were inherited by the Company in its 2004 acquisition of LFIN. See Note 17 to the Consolidated Financial Statements. The provision for probable loan losses charged to expense decreased $23.4 million, after tax to $14.8 million, after tax for the year ended December 31, 2010 from $38.2 million, after tax for the same period of 2009. The decrease is mainly due to a decrease in required reserves for impaired loans analyzed on an individual basis. The impaired loans have been measured based on the fair value of collateral. The majority of these loans show a fair value greater than carrying value.

Net income for the year ended December 31, 2009 increased by 8.0% compared to the same period in 2008 despite the $25.4 million, after tax, increase in the provision for probable loan losses charged to expense during 2009. Additionally, an industry-wide FDIC special assessment negatively impacted the

Company's earnings by $3.3 million, after tax in the second quarter. The increase in the provision was prompted by management's analysis of the general weakness in the economy and the impact of that weakness on the Company's loan portfolio and the related allowance for probable loan losses. Additionally, net income for 2009 was positively affected by the increasing net interest margin of the Company. While the Texas and Oklahoma economies are performing better than other parts of the country, Texas and Oklahoma are not immune to the problems associated with the U.S. economy. The substantial increase in the provision for probable loan losses is not necessarily an indicator that more credits will worsen to the point that the Company will have to continue to record provisions for probable loan losses at these levels in future periods.

**Net Interest Income**

Net interest income is the spread between income on interest-earning assets, such as loans and securities, and the interest expense on liabilities used to fund those assets, such as deposits, repurchase agreements and funds borrowed. Net interest income is the Company's largest source of revenue. Net interest income is affected by both changes in the level of interest rates and changes in the amount and composition of interest-earning assets and interest-bearing liabilities.

| | For the years ended December 31, | | |
|---|---|---|---|
| | 2010 Average Rate/Cost | 2009 Average Rate/Cost | 2008 Average Rate/Cost |
| *Assets* | | | |
| Interest earning assets: | | | |
| Loan, net of unearned discounts: | | | |
| Domestic | 5.72% | 5.88% | 6.60% |
| Foreign | 4.62 | 4.96 | 6.03 |
| Investment securities: | | | |
| Taxable | 3.30 | 4.34 | 4.59 |
| Tax-exempt | 5.02 | 4.87 | 4.87 |
| Federal funds sold | — | — | 1.75 |
| Other | 2.23 | .87 | 5.23 |
| Total interest-earning assets | 4.64% | 5.17% | 5.70% |
| *Liabilities* | | | |
| Interest bearing liabilities: | | | |
| Savings and interest bearing demand deposits | .39% | .51% | 1.17% |
| Time deposits: | | | |
| Domestic | 1.46 | 1.96 | 3.25 |
| Foreign | 1.24 | 1.78 | 3.11 |
| Securities sold under repurchase agreements | 2.99 | 3.06 | 3.51 |
| Other borrowings | .19 | .57 | 2.44 |
| Junior subordinated deferrable interest debentures | 6.07 | 6.23 | 7.03 |
| Total interest bearing liabilities | 1.39% | 1.59% | 2.67% |

For the three years ended December 31, 2010, as short term interest rates have fluctuated, the Company has monitored and adjusted interest rates on loans and deposits accordingly. The level of interest rates and the volume and mix of earning assets and interest-bearing liabilities impact net income and net interest margin. The yield on average interest-earning assets decreased 11.4% from 5.17% in 2009 to 4.64% in 2010, and the rates paid on average interest-bearing liabilities decreased 14.4% from 1.59% in 2009 to 1.39% in 2010. The yield on average interest-earning assets decreased 9.3% from 5.70% in 2008 to 5.17% in 2009, and the rates paid on average interest-bearing liabilities decreased 40.4% from 2.67% in 2008 to 1.59% in 2009. The majority of the Company's taxable investment securities are invested in mortgage backed securities and during rapid increases or reduction in interest rates, the yield on these securities do not re-price as quickly as the loans.

The following table analyzes the changes in net interest income during 2010 and 2009 and the relative effect of changes in interest rates and volumes for each major classification of interest-earning assets and interest-bearing liabilities. Non-accrual loans have been included in assets for the purpose of this analysis, which reduces the resulting yields:

| | 2010 compared to 2009 Net increase (decrease) due to | | | 2009 compared to 2008 Net increase (decrease) due to | | |
|---|---|---|---|---|---|---|
| | Volume(1) | Rate(1) | Total | Volume(1) | Rate(1) | Total |
| | (Dollars in Thousands) | | | (Dollars in Thousands) | | |
| Interest earned on: | | | | | | |
| Loans, net of unearned discounts: | | | | | | |
| Domestic | $(10,557) | $ (8,807) | $(19,364) | $ 7,524 | $(39,016) | $(31,492) |
| Foreign | (1,347) | (856) | (2,203) | (531) | (2,926) | (3,457) |
| Investment securities: | | | | | | |
| Taxable | (8,061) | (42,764) | (50,825) | 7,389 | (10,386) | (2,997) |
| Tax-exempt | 1,950 | 220 | 2,170 | 1,560 | (4) | 1,556 |
| Other | 260 | 1,354 | 1,614 | 2,205 | (3,041) | (836) |
| Total interest income | $(17,755) | $(50,853) | $(68,608) | $18,147 | $(55,373) | $(37,226) |
| Interest incurred on: | | | | | | |
| Savings and interest bearing demand deposits | $ 1,291 | $ (2,740) | $ (1,449) | $(1,759) | $(14,060) | $(15,819) |
| Time deposits: | | | | | | |
| Domestic | 1,673 | (9,109) | (7,436) | 526 | (22,122) | (21,596) |
| Foreign | 1,173 | (9,025) | (7,852) | (1,169) | (21,459) | (22,628) |
| Securities sold under repurchase agreements | 543 | (1,050) | (507) | 900 | (6,577) | (5,677) |
| Other borrowings | (5,719) | (2,463) | (8,182) | 6,508 | (31,033) | (24,525) |
| Junior subordinated deferrable interest debentures | 2 | (336) | (334) | 2 | (1,604) | (1,602) |
| Other | — | — | — | (88) | — | (88) |
| Total interest expense | $ (1,037) | $(24,723) | $(25,760) | $ 4,920 | $(96,855) | $(91,935) |
| Net interest income | $(16,718) | $(26,130) | $(42,848) | $13,227 | $ 41,482 | $ 54,709 |

(Note 1) The change in interest due to both rate and volume has been allocated to volume and rate changes in proportion to the relationship of the absolute dollar amounts of the change in each.

As part of the strategy to manage interest rate risk, the Company strives to manage both assets and liabilities so that interest sensitivities match. One method of calculating interest rate sensitivity is through gap analysis. A gap is the difference between the amount of interest rate sensitive assets and interest rate sensitive liabilities that re-price or mature in a given time period. Positive gaps occur when interest rate

sensitive assets exceed interest rate sensitive liabilities, and negative gaps occur when interest rate sensitive liabilities exceed interest rate sensitive assets. A positive gap position in a period of rising interest rates should have a positive effect on net interest income as assets will re-price faster than liabilities. Conversely, net interest income should contract somewhat in a period of falling interest rates. Management can quickly change the Company's interest rate position at any given point in time as market conditions dictate. Additionally, interest rate changes do not affect all categories of assets and liabilities equally or at the same time. Analytical techniques employed by the Company to supplement gap analysis include simulation analysis to quantify interest rate risk exposure. The gap analysis prepared by management is reviewed by the Investment Committee of the Company twice a year. The Investment Committee is comprised of certain senior managers of the various Company bank subsidiaries along with consultants. Management currently believes that the Company is properly positioned for interest rate changes; however, if management determines at any time that the Company is not properly positioned, it will strive to adjust the interest rate sensitive assets and liabilities in order to manage the effect of interest rate changes.

At December 31, 2010, based on these simulations, a rate shift of 300 basis points in interest rates up will vary net interest income by 3.84%, while a rate shift of 150 basis points down will not vary net interest income by more than 4.33% of projected 2011 net interest income. The basis point shift in interest rates is a hypothetical rate scenario used to calibrate risk, and does not necessarily represent management's current view of future market developments. The Company believes that it is properly positioned for a potential interest rate increase or decrease.

**Allowance for Probable Loan Loss**

The following table presents information concerning the aggregate amount of non-accrual, past due and restructured domestic loans; certain loans may be classified in one or more categories:

| | December 31, | | | | |
|---|---|---|---|---|---|
| | 2010 | 2009 | 2008 | 2007 | 2006 |
| | (Dollars in Thousands) | | | | |
| Loans accounted for on a non-accrual basis | $108,023 | $68,314 | $163,700 | $32,900 | $13,490 |
| Accruing loans contractually past due ninety days or more as to interest or principal payments | 19,347 | 11,986 | 6,208 | 21,330 | 9,201 |
| Loans accounted for as "troubled debt restructuring" | — | — | — | — | — |

The allowance for probable loan losses decreased 11.4% to $84,482,000 at December 31, 2010 from $95,393,000 at December 31, 2009. The allowance was 1.56% of total loans, net of unearned income at December 31, 2010 and 1.68% at December 31, 2009. The provision for probable loan losses charged to expense decreased $36,021,000 to $22,812,000 for the year ended December 31, 2010 from $58,833,000 for the same period in 2009. The Company's provision for probable loan losses decreased from the December 31, 2010 to December 31, 2009 mainly due to the decrease in the required reserves for impaired loans analyzed on an individual basis. The impaired loans have been measured based on the fair value of collateral. The majority of these loans show a fair value, after considering selling costs, greater than the carrying value. The Company's provision for probable loan losses increased for the years ended December 31, 2009 and 2008, prompted by the analysis of management regarding the weakness in the overall economy and the impact of that weakness on the Company's loan portfolio and the related allowance for probable loan losses. While the Texas and Oklahoma economies are performing better and appear to be recovering faster than other parts of the country, Texas and Oklahoma are not completely immune to the problems associated with the U.S. economy.

The following table presents information concerning the aggregate amount of non-accrual and past due foreign loans extended to persons or entities in foreign countries. Certain loans may be classified in one or more category:

| | December 31, | | | | |
|---|---|---|---|---|---|
| | 2010 | 2009 | 2008 | 2007 | 2006 |
| | (Dollars in Thousands) | | | | |
| Loans accounted for on a non-accrual basis | $ 7 | $ 24 | $530 | $722 | $4,298 |
| Accruing loans contractually past due ninety days or more as to interest or principal payments | 501 | 103 | 66 | 510 | 199 |

The gross income that would have been recorded during 2010 and 2009 on non-accrual loans in accordance with their original contract terms was $3,748,000 and $4,008,000 on domestic loans and $2,000 and $3,000 on foreign loans, respectively. The amount of interest income on such loans that was recognized in 2010 and 2009 was $32,000 and $547,000 on domestic loans and $0 and $0 for foreign loans, respectively.

Generally, loans are placed on non-accrual status if principal or interest payments become 90 days past due and/or management deem the collectability of the principal and/or interest to be in question, as well as when required by applicable regulatory guidelines. Interest income on non-accrual loans is recognized only to the extent payments are received or when, in management's opinion, the creditor's financial condition warrants reestablishment of interest accruals. Under special circumstances, a loan may be more than 90 days delinquent as to interest or principal and not be placed on non-accrual status. This situation generally results when a bank subsidiary has a borrower who is experiencing financial difficulties, but not to the extent that requires a restructuring of indebtedness. The majority of this category is composed of loans that are considered to be adequately secured and/or for which there has been a recent history of payments. When a loan is placed on non-accrual status, any interest accrued, not paid is reversed and charged to operations against interest income.

Loan commitments, consisting of unused commitments to lend, letters of credit, credit card lines and other approved loans, that have not been funded, were $1,309,921,000 and $1,349,516,000 at December 31, 2010 and 2009, respectively. See Note 19 to the Consolidated Financial Statements.

The following table summarizes loan balances at the end of each year and average loans outstanding during the year; changes in the allowance for probable loan losses arising from loans charged-off and recoveries on loans previously charged-off by loan category; and additions to the allowance which have been charged to expense:

| | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| | (Dollars in Thousands) | | | | |
| Loans, net of unearned discounts, outstanding at December 31 | $5,410,003 | $5,667,262 | $5,872,833 | $5,536,628 | $5,034,810 |
| Average loans outstanding during the year (Note 1) | $5,542,230 | $5,748,789 | $5,683,130 | $5,215,435 | $4,796,489 |
| Balance of allowance at January 1 | $ 95,393 | $ 73,461 | $ 61,726 | $ 64,537 | $ 77,796 |
| Provision (credit) charged to expense | 22,812 | 58,833 | 19,813 | (1,762) | 3,849 |
| Loans charged off: | | | | | |
| Domestic: | | | | | |
| Commercial, financial and agricultural | (7,702) | (14,565) | (5,754) | (3,606) | (7,302) |
| Real estate—mortgage | (2,973) | (2,500) | (1,400) | (800) | (554) |
| Real estate—construction | (22,186) | (17,953) | (202) | (202) | (99) |
| Consumer | (2,152) | (2,690) | (1,770) | (1,741) | (2,056) |
| Foreign | (227) | (831) | (8) | (102) | (8,377) |
| Total loans charged off: | (35,240) | (38,539) | (9,134) | (6,451) | (18,388) |
| Recoveries credited to allowance: | | | | | |
| Domestic: | | | | | |
| Commercial, financial and agricultural | 626 | 519 | 576 | 810 | 625 |
| Real estate—mortgage | 517 | 128 | 94 | 58 | 130 |
| Real estate—construction | 16 | 19 | 21 | 89 | 53 |
| Consumer | 256 | 937 | 361 | 306 | 448 |
| Foreign | 102 | 35 | 4 | 3,085 | 24 |
| Total recoveries | 1,517 | 1,638 | 1,056 | 4,348 | 1,280 |
| Net loans charged off | (33,723) | (36,901) | (8,078) | (2,103) | (17,108) |
| Allowance acquired in purchase transactions | — | — | — | 1,054 | — |
| Balance of allowance at December 31 | $ 84,482 | $ 95,393 | $ 73,461 | $ 61,726 | $ 64,537 |
| Ratio of net loans charged-off during the year to average loans outstanding during the year (Note 1) | .61% | .64% | .14% | .04% | .36% |
| Ratio of allowance to loans, net of unearned discounts, outstanding at December 31 | 1.56% | 1.68% | 1.25% | 1.11% | 1.28% |

(Note 1) The average balances for purposes of the above table are calculated on the basis of daily balances.

The allowance for probable loan losses has been allocated based on the amount management has deemed to be reasonably necessary to provide for the probable losses incurred within the following categories of loans at the dates indicated and the percentage of loans to total loans in each category:

| | At December 31, | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 2010 | | 2009 | | 2008 | | 2007 | | 2006 | |
| | Allowance | Percent of total | Allowance | Percent of total | Allowance | Percent of total | Allowance | Percent of total | Allowance | Percent of total |
| | (Dollars in Thousands) | | | | | | | | | |
| Commercial, Financial and Agricultural | $38,439 | 48.5% | $47,676 | 47.8% | $33,737 | 43.8% | $28,117 | 43.9% | $28,158 | 46.5% |
| Real estate— Mortgage | 12,670 | 17.5 | 16,825 | 16.8 | 11,639 | 15.1 | 9,256 | 14.4 | 9,461 | 15.6 |
| Real estate— Construction | 26,695 | 27.2 | 27,918 | 27.9 | 25,058 | 32.6 | 21,277 | 33.2 | 16,914 | 27.9 |
| Consumer | 6,241 | 2.3 | 2,581 | 2.6 | 2,223 | 2.9 | 2,212 | 3.4 | 2,392 | 3.9 |
| Foreign | 437 | 4.5 | 393 | 4.9 | 804 | 5.6 | 864 | 5.1 | 7,612 | 6.1 |
| | $84,482 | 100.0% | $95,393 | 100.0% | $73,461 | 100.0% | $61,726 | 100.0% | $64,537 | 100.0% |

The allowance for probable loan losses consists of the aggregate loan loss allowances of the bank subsidiaries. The allowances are established through charges to operations in the form of provisions for probable loan losses.

The bank subsidiaries charge off that portion of any loan which management considers to represent a loss as well as that portion of any other loan which is classified as a "loss" by bank examiners. Commercial, financial and agricultural or real estate loans are generally considered by management to represent a loss, in whole or part, (i) when an exposure beyond any collateral coverage is apparent, (ii) when no further collection of the portion of the loan so exposed is anticipated based on actual results, (iii) when the credit enhancements, if any, are not adequate, and (iv) when the borrower's financial condition would indicate so. Generally, unsecured consumer loans are charged off when 90 days past due.

The allowance for probable loan losses is a reserve established through a provision for probable loan losses charged to expense, which represents management's best estimate of probable loan losses within the existing portfolio of loans. The Company's allowance for probable loan loss methodology is based on guidance provided in Securities and Exchange Commission Staff Accounting Bulletin No. 102, "Selected Loan Loss Allowance Methodology and Documentation Issues" and includes allowance allocations calculated in accordance with ASC 310, "Receivables" and ASC 450, "Contingencies." The reserve allocated to all categories of loans decreased approximately $10.9 million from 2009 to 2010 and increased approximately $21.9 million from 2008 to 2009. The decrease in the reserve from 2010 to 2009 is mainly due to a decrease in the required reserves for impaired loans analyzed on an individual basis. The impaired loans have been measured based on the fair value of collateral. The majority of these loans show a fair value, after considering selling costs, greater than the carrying value. The increase in the reserve from 2008 to 2009 occurred as the result of the deterioration of economic conditions in 2008 that continue in to occur in 2009. Please refer to Note 4—Allowance for Probable Loan Losses in the accompanying Notes to the consolidated Financial Statements.

While management of the Company considers that it is generally able to identify borrowers with financial problems reasonably early and to monitor credit extended to such borrowers carefully, there is no precise method of predicting loan losses. The determination that a loan is likely to be uncollectible and that it should be wholly or partially charged off as a loss is an exercise of judgment. Similarly, the determination of the adequacy of the allowance for probable loan losses can be made only on a subjective basis. It is the judgment of the Company's management that the allowance for probable loan losses at December 31, 2010 was adequate to absorb probable losses from loans in the portfolio at that date. See Critical Accounting Policies on page 25. Should any of the factors considered by management in evaluating the adequacy of the allowance for probable loan losses change, the Company's estimate of probable loan losses could also change, which could affect the level of future provisions for probable loan losses.

**Non-Interest Income**

| | Year Ended December 31, 2010 | Year Ended December 31, 2009 | Percent Increase (Decrease) 2010 vs. 2009 | Year Ended December 31, 2008 | Percent Increase (Decrease) 2009 vs. 2008 |
|---|---|---|---|---|---|
| | (Dollars in Thousands) | | | | |
| Service charges on deposit accounts | $ 99,644 | $ 99,642 | —% | $ 98,466 | 1.2% |
| Other service charges, commissions and fees | | | | | |
| Banking | 47,930 | 42,861 | 11.8 | 40,543 | 5.7 |
| Non-banking | 8,439 | 12,697 | (33.5) | 7,592 | 67.2 |
| Investment securities transactions, net | 33,209 | 11,956 | 177.8 | 6,427 | 86.0 |
| Other investments, net | 17,696 | 19,773 | (10.5) | 15,183 | 30.2 |
| Other income | 11,866 | 14,084 | (15.7) | 21,598 | (34.8) |
| Total non-interest income | $218,784 | $201,013 | 8.8% | $189,809 | 5.9% |

The increase in investment securities transactions for the year ended December 31, 2010 can be attributed to the sale of investment securities to facilitate the re-positioning of the Company's investment portfolio. The largest portion of securities sales for 2010 occurred in the first quarter. The increase in investment securities transactions for the year ended December 31, 2009 can be attributed to the sale of investment securities resulting in a gain of $12.0 million, before taxes. Non-banking service charges, commissions and fees 2009 was positively impacted by the results of a wholly owned insurance subsidiary of the Company's lead bank. During 2008, the Company sold certain equity securities resulting in a gain of $6.2 million, before taxes.

**Non-Interest Expense**

| | Year Ended December 31, 2010 | Year Ended December 31, 2009 | Percent Increase (Decrease) 2010 vs. 2009 | Year Ended December 31, 2008 | Percent Increase (Decrease) 2009 vs. 2008 |
|---|---|---|---|---|---|
| | (Dollars in Thousands) | | | | |
| Employee compensation and benefits | $127,469 | $130,849 | (2.6)% | $129,084 | 1.4% |
| Occupancy | 36,631 | 35,374 | 3.6 | 38,315 | (7.7) |
| Depreciation of bank premises and equipment | 35,395 | 35,879 | (1.3) | 36,700 | (2.2) |
| Professional fees | 15,625 | 12,640 | 23.6 | 10,051 | 25.8 |
| Deposit insurance assessments | 10,253 | 10,249 | — | 1,027 | 898.0 |
| Amortization of identified intangible assets | 5,284 | 5,286 | — | 5,195 | 1.8 |
| Advertising | 7,716 | 9,149 | (15.7) | 13,189 | (30.6) |
| Litigation expense | 21,837 | — | — | — | — |
| Impairment charges (Total other-than-temporary impairment charges, $(19,070) less loss of $10,654 included in other comprehensive income) | 8,416 | — | — | — | — |
| Other | 71,099 | 69,605 | (2.1) | 67,665 | 2.9 |
| Total non-interest expense | $339,725 | $309,031 | 9.9% | $301,226 | 2.6% |

Included in litigation expense is a reserve for a dispute related to certain tax deductions that were inherited by the Company's 2004 acquisition of LFIN. The dispute involves claims by the former controlling shareholders of LFIN related to approximately $14 million of tax refunds received by the Company based on deductions taken in 2003 by LFIN in connection with losses on loans acquired from a failed thrift and a dispute LFIN had with the FDIC regarding tax benefits related to the failed thrift acquisition, which originated in 1988. The Company recorded an other-than-temporary impairment charge of $8.4 million on non-agency mortgage-backed securities, representing the credit related impairment on the securities. Professional fee expense for the twelve months ended December 31, 2009 was negatively impacted by the FDIC special assessment. In May 2009, the FDIC issued a final rule which levied a special assessment on all insured depository institutions totaling five basis points of each institution's total assets less Tier 1 capital as of June 30, 2009 that was collected on September 30, 2009. The special assessment is part of the FDIC's efforts to re-build the Deposit Insurance Fund ("DIF"). The Company accrued $5.1 million related to the special assessment.

**Effects of Inflation**

The principal component of earnings is net interest income, which is affected by changes in the level of interest rates. Changes in rates of inflation affect interest rates. It is difficult to precisely measure the impact of inflation on net interest income because it is not possible to accurately differentiate between increases in net interest income resulting from inflation and increases resulting from increased business activity. Inflation also raises costs of operations, primarily those of employment and services.

**Financial Condition**

**Investment Securities**

The following table sets forth the carrying value of investment securities as of December 31, 2010, 2009 and 2008:

| | December 31, | | |
|---|---|---|---|
| | 2010 | 2009 | 2008 |
| | (Dollars in Thousands) | | |
| U.S. Treasury Securities | | | |
| Available for sale | $ 1,327 | $ 1,327 | $ 1,319 |
| Residential mortgage-backed securities | | | |
| Available for sale | 4,924,468 | 4,491,764 | 4,974,317 |
| Obligations of states and political subdivisions | | | |
| Available for sale | 145,997 | 136,866 | 82,214 |
| Equity securities | | | |
| Available for sale | 14,665 | 14,126 | 14,030 |
| Other securities | | | |
| Held to maturity | 2,450 | 2,450 | 2,300 |
| Total | $5,088,907 | $4,646,533 | $5,074,180 |

The following tables set forth the contractual maturities of investment securities, based on amortized cost, at December 31, 2010 and the average yields of such securities, except for the totals, which reflect the

weighted average yields. Actual maturities will differ from contractual maturities because borrowers may have the right to prepay obligations with or without prepayment penalties.

| | Available for Sale Maturing | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Within one year | | After one but within five years | | After five but within ten years | | After ten years | |
| | Adjusted | | Adjusted | | Adjusted | | Adjusted | |
| | Cost | Yield | Cost | Yield | Cost | Yield | Cost | Yield |
| | (Dollars in Thousands) | | | | | | | |
| U.S. Treasury and obligations of U.S. Government agencies | $1,327 | .17% | $ — | —% | $ — | —% | $ — | —% |
| Residential mortgage-backed securities | 912 | 5.01 | 3,231 | 5.51 | 538,147 | 4.22 | 4,334,283 | 2.98 |
| Obligations of states and political subdivisions | — | — | 234 | 4.72 | 4,642 | 4.91 | 145,246 | 5.74 |
| Equity securities | 325 | — | — | — | — | — | 13,500 | 3.43 |
| Other securities | — | — | — | — | — | — | — | — |
| Total | $2,564 | 1.87% | $3,465 | 5.45% | $542,789 | 4.23% | $4,493,029 | 3.07% |

| | Held to Maturity Maturing | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Within one year | | After one but within five years | | After five but within ten years | | After ten years | |
| | Adjusted | | Adjusted | | Adjusted | | Adjusted | |
| | Cost | Yield | Cost | Yield | Cost | Yield | Cost | Yield |
| | (Dollars in Thousands) | | | | | | | |
| Other securities | $1,825 | 1.45% | $625 | 1.41% | $— | —% | $— | % |
| Total | $1,825 | 1.45% | $625 | 1.41% | $— | —% | $— | —% |

Mortgage-backed securities are securities primarily issued by the Federal Home Loan Mortgage Corporation (“Freddie Mac”), Federal National Mortgage Association (“Fannie Mae”), and the Government National Mortgage Association (“Ginnie Mae”). Investments in mortgage-backed securities issued by Ginnie Mae are fully guaranteed by the U.S. Government. Investments in mortgage-backed securities issued by Freddie Mac and Fannie Mae are not fully guaranteed by the U.S. Government, however, the Company believes that the quality of the bonds is similar to other AAA rated bonds with limited credit risk, particularly given the placement of Fannie Mae and Freddie Mac into conservatorship by the federal government in early September 2008.

**Loans**

The amounts of loans outstanding, by classification, at December 31, 2010, 2009, 2008, 2007 and 2006 are shown in the following table:

| | December 31, | | | | |
|---|---|---|---|---|---|
| | 2010 | 2009 | 2008 | 2007 | 2006 |
| | (Dollars in Thousands) | | | | |
| Commercial, financial and agricultural | $2,615,878 | $2,703,379 | $2,574,247 | $2,426,064 | $2,337,573 |
| Real estate—mortgage | 948,982 | 954,010 | 888,095 | 798,708 | 785,401 |
| Real estate—construction | 1,473,471 | 1,583,057 | 1,911,954 | 1,835,950 | 1,404,186 |
| Consumer | 126,047 | 146,331 | 169,589 | 190,899 | 198,580 |
| Foreign | 245,625 | 280,485 | 328,948 | 285,008 | 309,144 |
| Total loans | 5,410,003 | 5,667,262 | 5,872,833 | 5,536,629 | 5,034,884 |
| Unearned discount | — | — | — | (1) | (74) |
| Loans, net of unearned discount | $5,410,003 | $5,667,262 | $5,872,833 | $5,536,628 | $5,034,810 |

The following table shows the amounts of loans (excluding real estate mortgages and consumer loans) outstanding as of December 31, 2010, which based on remaining scheduled repayments of principal are due in the years indicated. Also, the amounts due after one year are classified according to the sensitivity to changes in interest rates:

| | Maturing | | | |
|---|---|---|---|---|
| | Within one year | After one but within five years | After five years | Total |
| | (Dollars in Thousands) | | | |
| Commercial, financial and agricultural | $ 905,685 | $1,599,429 | $110,764 | $2,615,878 |
| Real estate—construction | 935,022 | 522,093 | 16,356 | 1,473,471 |
| Foreign | 161,772 | 82,571 | 1,282 | 245,625 |
| Total | $2,002,479 | $2,204,093 | $128,402 | $4,334,974 |

| | Interest sensitivity | |
|---|---|---|
| | Fixed Rate | Variable Rate |
| | (Dollars in Thousands) | |
| Due after one but within five years | $238,302 | $1,965,791 |
| Due after five years | 32,407 | 95,995 |
| Total | $270,709 | $2,061,786 |

**International Operations**

On December 31, 2010, the Company had $245,625,000 (2.1% of total assets) in loans outstanding to borrowers domiciled in foreign countries, which included primarily borrowers domiciled in Mexico. The loan policies of the Company's bank subsidiaries generally require that loans to borrowers domiciled in foreign countries be primarily secured by assets located in the United States or have credit enhancements, in the form of guarantees, from significant United States corporations. The composition of such loans and the related amounts of allocated allowance for probable loan losses as of December 31, 2010 is presented below.

| | Amount of Loans | Related Allowance for Probable Losses |
|---|---|---|
| | (Dollars in Thousands) | |
| Secured by certificates of deposit in United States banks | $139,496 | $ 70 |
| Secured by United States real estate | 32,700 | 86 |
| Secured by other United States collateral (securities, gold, silver, etc.) | 31,685 | 79 |
| Unsecured | 627 | 2 |
| Other (principally Mexico real estate) | 41,117 | 200 |
| | $245,625 | $437 |

The transactions for the year ended December 31, 2010, in that portion of the allowance for probable loan losses related to foreign debt were as follows:

| | (Dollars in Thousands) |
|---|---|
| Balance at December 31, 2009 | $ 393 |
| Charge-offs | (227) |
| Recoveries | 102 |
| Net recoveries | (125) |
| Provision charged to expense | 169 |
| Balance at December 31, 2010 | $ 437 |

**Deposits**

| | 2010 Average Balance | 2009 Average Balance |
|---|---|---|
| | (Dollars in Thousands) | |
| Deposits: | | |
| Demand—non-interest bearing | | |
| Domestic | $1,471,034 | $1,325,682 |
| Foreign | 168,085 | 155,312 |
| Total demand non-interest bearing | 1,639,119 | 1,480,994 |
| Savings and interest bearing demand | | |
| Domestic | 1,949,389 | 1,781,663 |
| Foreign | 440,310 | 353,484 |
| Total savings and interest bearing demand | 2,389,699 | 2,135,147 |
| Time certificates of deposit | | |
| $100,000 or more: | | |
| Domestic | 1,038,031 | 947,382 |
| Foreign | 1,270,513 | 1,218,579 |
| Less than $100,000: | | |
| Domestic | 766,075 | 771,362 |
| Foreign | 402,913 | 388,852 |
| Total time, certificates of deposit | 3,477,532 | 3,326,175 |
| Total deposits | $7,506,350 | $6,942,316 |

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| | (Dollars in Thousands) | | |
| Interest expense: | | | |
| Savings and interest bearing demand | | | |
| Domestic | $ 7,771 | $ 9,267 | $ 23,197 |
| Foreign | 1,612 | 1,565 | 3,454 |
| Total savings and interest bearing demand | 9,383 | 10,832 | 26,651 |
| Time, certificates of deposit | | | |
| $100,000 or more | | | |
| Domestic | 14,839 | 18,091 | 28,990 |
| Foreign | 17,084 | 23,315 | 41,383 |
| Less than $100,000 | | | |
| Domestic | 11,416 | 15,600 | 26,297 |
| Foreign | 3,628 | 5,249 | 9,809 |
| Total time, certificates of deposit | 46,967 | 62,255 | 106,479 |
| Total interest expense on deposits | $56,350 | $73,087 | $133,130 |

Scheduled maturities of time deposits in amounts of $100,000 or more at December 31, 2010, were as follows:

| | |
|---|---|
| Due within 3 months or less | $ 966,224 |
| Due after 3 months and within 6 months | 576,168 |
| Due after 6 months and within 12 months | 544,175 |
| Due after 12 months | 210,606 |
| | $2,297,173 |

The Company offers a variety of deposit accounts having a wide range of interest rates and terms. The Company relies primarily on its high quality customer service, sales programs, customer referrals and advertising to attract and retain these deposits. Deposits provide the primary source of funding for the Company's lending and investment activities, and the interest paid for deposits must be managed carefully to control the level of interest expense. Deposits at December 31, 2010 were $7,599,558,000, an increase of 5.9% from $7,178,007,000 at December 31, 2009.

**Return on Equity and Assets**

Certain key ratios for the Company for the years ended December 31, 2010, 2009 and 2008 follows (Note 1):

| | Years ended December 31, | | |
|---|---|---|---|
| | 2010 | 2009 | 2008 |
| Percentage of net income to: | | | |
| Average shareholders' equity | 9.43% | 11.10% | 13.34% |
| Average total assets | 1.15 | 1.23 | 1.17 |
| Percentage of average shareholders' equity to average total assets | 12.24 | 11.07 | 8.81 |
| Percentage of cash dividends per share to net income per share | 20.81 | 17.89 | 34.27 |

(Note 1) The average balances for purposes of the above table are calculated on the basis of daily balances.

**Liquidity and Capital Resources**

**Liquidity**

The maintenance of adequate liquidity provides the Company's bank subsidiaries with the ability to meet potential depositor withdrawals, provide for customer credit needs, maintain adequate statutory reserve levels and take full advantage of high-yield investment opportunities as they arise. Liquidity is afforded by access to financial markets and by holding appropriate amounts of liquid assets. The Company's bank subsidiaries derive their liquidity largely from deposits of individuals and business entities. Deposits from persons and entities domiciled in Mexico comprise a stable portion of the deposit base of the Company's bank subsidiaries. Historically, the Mexico based deposits of the Company's bank subsidiaries have been a stable source of funding. Such deposits comprised approximately 30%, 31%, and 30% of the Company's bank subsidiaries' total deposits at each of the years ended December 31, 2010, 2009 and 2008, respectively. Other important funding sources for the Company's bank subsidiaries have been borrowings from the Federal Home Loan Bank ("FHLB"), securities sold under repurchase agreements and large certificates of deposit, requiring management to closely monitor its asset/liability mix in terms of both rate sensitivity and maturity distribution. Primary liquidity of the Company and its subsidiaries has been maintained by means of increased investment in shorter-term securities, certificates of deposit and repurchase agreements. As in the past, the Company will continue to monitor the volatility

and cost of funds in an attempt to match maturities of rate-sensitive assets and liabilities, and respond accordingly to anticipate fluctuations in interest rates over reasonable periods of time.

**Asset/Liability Management**

The Company's fund management policy has as its primary focus the measurement and management of the banks' earnings at risk in the face of rising or falling interest rate forecasts. The earliest and most simplistic concept of earnings at risk measurement is the gap report, which is used to generate a rough estimate of the vulnerability of net interest income to changes in market rates as implied by the relative re-pricings of assets and liabilities. The gap report calculates the difference between the amounts of assets and liabilities re-pricing across a series of intervals in time, with emphasis typically placed on the one-year period. This difference, or gap, is usually expressed as a percentage of total assets.

If an excess of liabilities over assets matures or re-prices within the one-year period, the statement of condition is said to be negatively gapped. This condition is sometimes interpreted to suggest that an institution is liability-sensitive, indicating that earnings would suffer from rising rates and benefit from falling rates. If a surplus of assets over liabilities occurs in the one-year time frame, the statement of condition is said to be positively gapped, suggesting a condition of asset sensitivity in which earnings would benefit from rising rates and suffer from falling rates.

The gap report thus consists of an inventory of dollar amounts of assets and liabilities that have the potential to mature or re-price within a particular period. The flaw in drawing conclusions about interest rate risk from the gap report is that it takes no account of the probability that potential maturities or re-pricings of interest-rate-sensitive accounts will occur, or at what relative magnitudes. Because simplicity, rather than utility, is the only virtue of gap analysis, financial institutions increasingly have either abandoned gap analysis or accorded it a distinctly secondary role in managing their interest-rate risk exposure.

The net interest rate sensitivity at December 31, 2010, is illustrated in the following table. This information reflects the balances of assets and liabilities whose rates are subject to change. As indicated in the table on the following page, the Company is liability-sensitive during the early time periods and is asset-sensitive in the longer periods. The table shows the sensitivity of the statement of condition at one point in time and is not necessarily indicative of the position at future dates.

**INTEREST RATE SENSITIVITY**
(Dollars in Thousands)

| December 31, 2010 | Rate/Maturity | | | | |
|---|---|---|---|---|---|
| | 3 Months or Less | Over 3 Months to 1 Year | Over 1 Year to 5 Years | Over 5 Years | Total |
| | (Dollars in Thousands) | | | | |
| Rate sensitive assets | | | | | |
| Investment securities | $ 383,533 | $ 1,307,996 | $3,251,615 | $ 145,763 | $ 5,088,907 |
| Loans, net of non-accruals | 4,013,163 | 200,606 | 370,304 | 717,900 | 5,301,973 |
| Total earning assets | $ 4,396,696 | $ 1,508,602 | $3,621,919 | $ 863,663 | $10,390,880 |
| Cumulative earning assets | $ 4,396,696 | $ 5,905,298 | $9,527,217 | $10,390,880 | |
| Rate sensitive liabilities | | | | | |
| Time deposits | $ 1,494,497 | $ 1,589,708 | $ 352,928 | $ 507 | $ 3,437,640 |
| Other interest bearing deposits | 2,522,842 | — | — | — | 2,522,842 |
| Securities sold under repurchase agreements | 357,809 | 74,013 | 1,448 | 1,000,000 | 1,433,270 |
| Other borrowed funds | 1,020,000 | — | — | 6,780 | 1,026,780 |
| Junior subordinated deferrable interest debentures | 61,858 | 41,238 | 87,630 | 10,391 | 201,117 |
| Total interest bearing liabilities | $ 5,457,006 | $ 1,704,959 | $ 442,006 | $ 1,017,678 | $ 8,621,649 |
| Cumulative sensitive liabilities | $ 5,457,006 | $ 7,161,965 | $7,603,971 | $ 8,621,649 | |
| Repricing gap | $(1,060,310) | $ (196,357) | $3,179,913 | $ (154,015) | $ 1,769,231 |
| Cumulative repricing gap | (1,060,310) | (1,256,667) | 1,923,246 | 1,769,231 | |
| Ratio of interest-sensitive assets to liabilities | .806 | .885 | 8.194 | .849 | 1.205 |
| Ratio of cumulative, interest-sensitive assets to liabilities | .806 | .825 | 1.253 | 1.205 | |

The detailed inventory of statement of condition items contained in gap reports is the starting point of income simulation analysis. Income simulation analysis also focuses on the variability of net interest income and net income, but without the limitations of gap analysis. In particular, the fundamental, but often unstated, assumption of the gap approach that every statement of condition item that can re-price will do so to the full extent of any movement in market interest rates is taken into consideration in income simulation analysis.

Accordingly, income simulation analysis captures not only the potential of assets and liabilities to mature or re-price, but also the probability that they will do so. Moreover, income simulation analysis focuses on the relative sensitivities of these balance sheet items and projects their behavior over an extended period of time in a motion picture rather than snapshot fashion. Finally, income simulation analysis permits management to assess the probable effects on balance sheet items not only of changes in market interest rates, but also of proposed strategies for responding to such changes. The Company and many other institutions rely primarily upon income simulation analysis in measuring and managing exposure to interest rate risk.

At December 31, 2010, based on these simulations, a rate shift of 300 basis points in interest rates up will vary projected 2011 net interest income by 3.84%, while a rate shift of 150 basis points down will not vary net interest income by more than 4.33% of projected 2011 net interest income. The basis point shift in interest rates is a hypothetical rate scenario used to calibrate risk, and does not necessarily represent

management's current view of future market developments. The Company believes that it is properly positioned for a potential interest rate increase or decrease.

All the measurements of risk described above are made based upon the Company's business mix and interest rate exposures at the particular point in time. The exposure changes continuously as a result of the Company's ongoing business and its risk management initiatives. While management believes these measures provide a meaningful representation of the Company's interest rate sensitivity, they do not necessarily take into account all business developments that have an effect on net income, such as changes in credit quality or the size and composition of the statement of condition.

Principal sources of liquidity and funding for the Company are dividends from subsidiaries and borrowed funds, with such funds being used to finance the Company's cash flow requirements. The Company closely monitors the dividend restrictions and availability from the bank subsidiaries as disclosed in Note 20 to the Consolidated Financial Statements. At December 31, 2010, the aggregate amount legally available to be distributed to the Company from bank subsidiaries as dividends was approximately $465,000,000, assuming that each bank subsidiary continues to be classified as "well capitalized" under the applicable regulations. The restricted capital (capital and surplus) of the bank subsidiaries was approximately $939,685,000 as of December 31, 2010. The undivided profits of the bank subsidiaries were approximately $813,711,000 as of December 31, 2010. Additionally, as a result of the Company's participation in the TARP Capital Purchase Program, the Company is restricted in the payment of dividends and may not without the Treasury Department's consent, declare or pay any dividend on the Company Common Stock other than a regular semi-annual cash dividend of not more than $.33 per share, as adjusted for any stock dividend or stock split. The restriction ceases to exist only on the earlier to occur of December 23, 2011 or the date on which the Company has redeemed all of the Series A Preferred Stock issued as part of the Capital Purchase Program or the date on which the Treasury has transferred all of the Preferred Stock to third parties affiliated with the Treasury.

At December 31, 2010, the Company has outstanding $1,026,780,000 in other borrowed funds and $201,117,000 in junior subordinated deferrable interest debentures. In addition to borrowed funds and dividends, the Company has a number of other available alternatives to finance the growth of its existing banks as well as future growth and expansion.

**Capital**

The Company maintains an adequate level of capital as a margin of safety for its depositors and shareholders. At December 31, 2010, shareholders' equity was $1,459,217,000 compared to $1,407,470,000 at December 31, 2009, an increase of $51,747,000, or 3.7%. Shareholders' equity increased primarily due to the retention of earnings offset by the payment of cash dividends to shareholders and the repurchase of common stock under the Company's publicly announced stock purchase program. The accumulated other comprehensive income is not included in the calculation of regulatory capital ratios.

During 1990, the Federal Reserve Board ("FRB") adopted a minimum leverage ratio of 3% for the most highly rated bank holding companies and at least 4% to 5% for all other bank holding companies. The Company's leverage ratio (defined as shareholders' equity plus eligible trust preferred securities issued and outstanding less goodwill and certain other intangibles divided by average quarterly assets) was 11.58% at December 31, 2010 and 10.95% at December 31, 2009. The large increase in the Company's leverage ratio is primarily due to the Company's participation in the Treasury's CPP program. The core deposit intangibles and goodwill of $299,841,000 as of December 31, 2010, are deducted from the sum of core capital elements when determining the capital ratios of the Company.

The FRB has adopted risk-based capital guidelines which assign risk weightings to assets and off-balance sheet items. The guidelines also define and set minimum capital requirements (risk-based capital ratios). Under the final 1992 rules, all banks are required to have Tier 1 capital of at least 4.0% of risk-weighted assets and total capital of 8.0% of risk-weighted assets. Tier 1 capital consists principally of

shareholders' equity plus trust preferred securities issued and outstanding less goodwill and certain other intangibles, while total capital consists of Tier 1 capital, certain debt instruments and a portion of the reserve for loan losses. In order to be deemed well capitalized pursuant to the regulations, an institution must have a total risk-weighted capital ratio of 10%, a Tier 1 risk-weighted ratio of 6% and a Tier 1 leverage ratio of 5%. The Company had risk-weighted Tier 1 capital ratios of 19.47% and 17.74% and risk weighted total capital ratios of 20.72% and 18.99% as of December 31, 2010 and 2009, respectively, which are well above the minimum regulatory requirements and exceed the well capitalized ratios (see Note 20 to Notes to Consolidated Financial Statements).

**Junior Subordinated Deferrable Interest Debentures**

The Company currently has eight statutory business trusts under the laws of the State of Delaware, for the purpose of issuing trust preferred securities. The eight statutory business trusts formed by the Company (the "Trusts") have each issued Capital and Common Securities and invested the proceeds thereof in an equivalent amount of junior subordinated debentures (the "Debentures") issued by the Company. As of December 31, 2010 and 2009, the principal amount of debentures outstanding totaled $201,117,000 and $201,082,000, respectively. As a result of the participation in the TARP Capital Purchase Program, the Company may not, without the consent of the Treasury Department, redeem any of the Debentures until the earlier to occur of December 23, 2011, or the date on which the Company has redeemed all of the Series A Preferred Stock issued under the Capital Purchase Program or the date on which the Treasury has transferred all of the Series A Preferred Stock to third parties not affiliated with the Treasury.

The Debentures are subordinated and junior in right of payment to all present and future senior indebtedness (as defined in the respective indentures) of the Company, and are *pari passu* with one another. The interest rate payable on, and the payment terms of the Debentures are the same as the distribution rate and payment terms of the respective issues of Capital and Common Securities issued by the Trusts. The Company has fully and unconditionally guaranteed the obligations of each of the Trusts with respect to the Capital and Common Securities. The Company has the right, unless an Event of Default (as defined in the Indentures) has occurred and is continuing, to defer payment of interest on the Debentures for up to ten consecutive semi-annual periods on Trust I and for up to twenty consecutive quarterly periods on Trusts VI, VII, VIII, IX, X, XI and XII. If interest payments on any of the Debentures are deferred, distributions on both the Capital and Common Securities related to that Debenture would also be deferred. The redemption prior to maturity of any of the Debentures may require the prior approval of the Federal Reserve and/or other regulatory bodies.

For financial reporting purposes, the Trusts are treated as investments of the Company and not consolidated in the consolidated financial statements. Although the Capital Securities issued by each of the Trusts are not included as a component of shareholders' equity on the consolidated statement of condition, the Capital Securities are treated as capital for regulatory purposes. Specifically, under applicable regulatory guidelines, the Capital Securities issued by the Trusts qualify as Tier 1 capital up to a maximum of 25% of Tier 1 capital on an aggregate basis. Any amount that exceeds the 25% threshold would qualify as Tier 2 capital. At December 31, 2010 and 2009, the total $201,117,000 and $201,082,000, of the Capital Securities outstanding qualified as Tier 1 capital.

In March 2005, the Federal Reserve Board issued a final rule that would continue to allow the inclusion of trust preferred securities in Tier 1 capital, but with stricter quantitative limits. Under the final rule, after a five-year transition period ending March 31, 2009, the aggregate amount of trust preferred securities and certain other capital elements would be limited to 25% of Tier 1 capital elements, net of goodwill, less any associated deferred tax liability. The amount of trust preferred securities and certain other elements in excess of the limit could be included in Supplementary Capital or Tier 2 capital, subject to restrictions. Tier 2 capital includes among other things, perpetual preferred stock, qualifying mandatory convertible debt securities, qualifying subordinated debt, and allowances for probable loan and lease

losses, subject to limitations. Bank holding companies with significant international operations will be expected to limit trust preferred securities to 15% of Tier 1 capital elements, net of goodwill; however, they may include qualifying mandatory convertible preferred securities up to the 25% limit. On March 16, 2009, the Federal Reserve Board extended for two years the transition period. The Company believes that substantially all of the trust preferred securities issued by the Company will qualify as Tier 1 capital after the transition period ending on March 31, 2011. The Collins Amendment to the Dodd-Frank Act further restricts the use of trust preferred securities by excluding them from the regulatory capital of banking holding companies more broadly. However, for institutions with consolidated assets of less than $15 billion on December 31, 2009, such as the Company, the Collins Amendment will not apply to securities issued before May 19, 2010 and all the Company's trust preferred securities were issued before such date. Pursuant to this grandfather provision, the Company will be able to continue to treat these securities as Tier 1 capital subject to existing Federal Reserve limitations through the life of the securities.

The following table illustrates key information about each of the Debentures and their interest rates at December 31, 2010:

| | Junior Subordinated Deferrable Interest Debentures | Repricing Frequency | Interest Rate | Interest Rate Index | Maturity Date | Optional Redemption Date |
|---|---|---|---|---|---|---|
| | (in thousands) | | | | | |
| Trust I | $ 10,391 | Fixed | 10.18% | Fixed | June 2031 | June 2011 |
| Trust VI | $ 25,774 | Quarterly | 3.74% | LIBOR + 3.45 | November 2032 | May 2011 |
| Trust VII | $ 10,310 | Quarterly | 3.54% | LIBOR + 3.25 | April 2033 | April 2011 |
| Trust VIII | $ 25,774 | Quarterly | 3.34% | LIBOR + 3.05 | October 2033 | April 2011 |
| Trust IX | $ 41,238 | Fixed | 7.10% | Fixed | October 2036 | October 2011 |
| Trust X | $ 34,021 | Fixed | 6.66% | Fixed | February 2037 | February 2012 |
| Trust XI | $ 32,990 | Fixed | 6.82% | Fixed | July 2037 | July 2012 |
| Trust XII | $ 20,619 | Fixed | 6.85% | Fixed | September 2037 | September 2012 |
| | $201,117 | | | | | |

(1) Trust IX, X, XI and XII accrue interest at a fixed rate for the first five years, then floating at LIBOR + 1.62%, 1.65%, 1.62% and 1.45% thereafter, respectively.

**Contractual Obligations and Commercial Commitments**

The following table presents contractual cash obligations of the Company (other than deposit liabilities) as of December 31, 2010:

| | Payments due by Period (Dollars in Thousands) | | | | |
|---|---|---|---|---|---|
| Contractual Cash Obligations | Total | Less than One Year | One to Three Years | Three to Five Years | After Five Years |
| Securities sold under repurchase agreements | $1,433,270 | $ 431,822 | $ 1,448 | $ — | $1,000,000 |
| Federal Home Loan Bank borrowings | $1,026,780 | 1,020,000 | — | — | 6,780 |
| Junior subordinated deferrable interest debentures | $ 201,117 | — | — | — | 201,117 |
| Operating leases | $ 28,327 | 9,472 | 10,586 | 4,388 | 3,881 |
| Total Contractual Cash Obligations | $2,689,494 | $1,461,294 | $12,034 | $4,388 | $1,211,778 |

The following table presents contractual commercial commitments of the Company (other than deposit liabilities) as of December 31, 2010:

| Commercial Commitments | Amount of Commitment Expiration Per Period (Dollars in Thousands) | | | | |
|---|---|---|---|---|---|
| | Total | Less than One Year | One to Three Years | Three to Five Years | After Five Years |
| Financial and Performance Standby Letters of Credit | $ 111,295 | $107,426 | $ 3,869 | $ — | $ — |
| Commercial Letters of Credit | $ 8,906 | 8,906 | — | — | — |
| Credit Card Lines | $ 64,252 | 64,252 | — | — | — |
| Other Commercial Commitments | $1,125,468 | 681,077 | 276,632 | 102,849 | 64,910 |
| Total Commercial Commitments | $1,309,921 | $861,661 | $280,501 | $102,849 | $64,910 |

Due to the nature of the Company's commercial commitments, including unfunded loan commitments and lines of credit, the amounts presented above do not necessarily reflect the amounts the Company anticipates funding in the periods presented above.

**Critical Accounting Policies**

The Company has established various accounting policies which govern the application of accounting principles in the preparation of the Company's consolidated financial statements. The significant accounting policies are described in the Notes to the Consolidated Financial Statements. Certain accounting policies involve significant subjective judgments and assumptions by management which have a material impact on the carrying value of certain assets and liabilities; management considers such accounting policies to be critical accounting policies.

The Company considers its Allowance for Probable Loan Losses as a policy critical to the sound operations of the bank subsidiaries. The allowance for probable loan losses consists of the aggregate loan loss allowances of the bank subsidiaries. The allowances are established through charges to operations in the form of provisions for probable loan losses. Loan losses or recoveries are charged or credited directly to the allowances. The allowance for probable loan losses of each bank subsidiary is maintained at a level considered appropriate by management, based on estimated probable losses in the loan portfolio. The allowance is derived from the following elements: (i) allowances established on specific loans (ii) allowances based on quantitative historical loss experience on the Company's loan portfolio and (iii) allowances based on qualitative data, which includes general economic conditions and other risk factors both internal and external to the Company. See also discussion regarding the allowance for probable loan losses and provision for probable loan losses included in the results of operations and "Provision and Allowance for Probable Loan Losses" included in Notes 1 and 4 of the Notes to Consolidated Financial Statements.

The specific loan loss provision is determined using the following methods. On a weekly basis, loan past due reports are reviewed by the servicing loan officer to determine if a loan has any potential problem and if a loan should be placed on the Company's internal classified report. Additionally, the Company's credit department reviews the majority of the Company's loans regardless of whether they are past due and segregates any loans with potential problems for further review. The credit department will discuss the potential problem loans with the servicing loan officers to determine any relevant issues that were not discovered in the evaluation. Also, any analysis on loans that is provided through examinations by regulatory authorities is considered in the review process. After the above analysis is completed, the Company will determine if a loan should be placed on an internal classified report because of issues related to the analysis of the credit, credit documents, collateral and/or payment history.

The Company's internal classified report is segregated into the following categories: (i) "Special Review Credits," (ii) "Watch List—Pass Credits," or (iii) "Watch List—Substandard Credits." The loans placed in the "Special Review Credits" category reflect the Company's opinion that the loans reflect potential weakness which require monitoring on a more frequent basis. The "Special Review Credits" are reviewed and discussed on a regular basis with the credit department and the lending staff to determine if a change in category is warranted. The loans placed in the "Watch List—Pass Credits" category reflect the Company's opinion that the credit contains weaknesses which represent a greater degree of risk, which warrant "extra attention." The "Watch List—Pass Credits" are reviewed and discussed on a regular basis with the credit department and the lending staff to determine if a change in category is warranted. The loans placed in the "Watch List—Substandard Credits" classification are considered to be potentially inadequately protected by the current sound worth and debt service capacity of the borrower or of any pledged collateral. These credit obligations, even if apparently protected by collateral value, have shown defined weaknesses related to adverse financial, managerial, economic, market or political conditions which may jeopardize repayment of principal and interest. Furthermore, there is the possibility that some future loss could be sustained by the bank if such weaknesses are not corrected. For loans that are classified as impaired, management evaluates these credits under Statement of Financial Accounting Standards No. 114, "Accounting by Creditors for Impairment of a Loan," now included as part of ASC 310-10, "Receivables," criteria and, if deemed necessary, a specific reserve is allocated to the credit. The specific reserve allocated under ASC 310-10, is based on (1) the present value of expected future cash flows discounted at the loan's effective interest rate; (2) the loan's observable market price; or (3) the fair value of the collateral if the loan is collateral dependent. Substantially all of the Company's loans evaluated as impaired under ASC 310-10 are measured using the fair value of collateral method. In limited cases, the Company may use other methods to determine the specific reserve of a loan under SFAS ASC 310-10 if such loan is not collateral dependent.

The allowance based on historical loss experience on the Company's remaining loan portfolio, which includes the "Special Review Credits," "Watch List—Pass Credits," and "Watch List—Substandard Credits" is determined by segregating the remaining loan portfolio into certain categories such as commercial loans, installment loans, international loans, loan concentrations and overdrafts. Management determined in 2010 that the allowance should be further segmented for commercial and consumer mortgage loans by the type of loans in order to better analyze the portfolio. The further segmentation did not have a significant impact on the allowance or provision for probable loan losses.

Installment loans are then further segregated by number of days past due. A historical loss percentage, adjusted for (i) management's evaluation of changes in lending policies and procedures, (ii) current economic conditions in the market area served by the Company, (iii) other risk factors, (iv) the effectiveness of the internal loan review function, (v) changes in loan portfolios, and (vi) the composition and concentration of credit volume is applied to each category. Each category is then added together to determine the allowance allocated under ASC 450-20.

The Company's management continually reviews the allowance for loan loss of the bank subsidiaries using the amounts determined from the allowances established on specific loans, allowance established on quantitative historical percentages, allowance based on qualitative data, and the loans charged off and recoveries to establish an appropriate amount to maintain in the Company's allowance for loan loss. If the basis of the Company's assumptions change, the allowance for loan loss would either decrease or increase and the Company would increase or decrease the provision for loan loss charged to operations accordingly.

**Recent Accounting Standards Issued**

See Note 1—Summary of Significant Accounting Policies in the accompanying Notes to the Consolidated Financial Statements for details of recently issued and recently adopted accounting standards and their impact on the Company's consolidated financial statements.

**Preferred Stock, Common Stock and Dividends**

The Company had issued and outstanding 67,701,671 shares of $1.00 par value Common Stock held by approximately 2,430 holders of record at February 22, 2011. The book value of the Common Stock at December 31, 2010 was $19.61 per share compared with $18.90 per share at December 31, 2009. The Company has issued and outstanding 216,000 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A, par value $0.01 per share, having a liquidation preference of $1,000 per share, as of February 22, 2011. The book value of the Series A Preferred at December 31, 2008 was $1,000 per share.

The Common Stock is traded on the NASDAQ National Market under the symbol "IBOC." The following table sets forth the approximate high and low bid prices in the Company's Common Stock during 2010 and 2009, as quoted on the NASDAQ National Market for each of the quarters in the two year period ended December 31, 2010. Some of the quotations reflect inter-dealer prices, without retail mark-up, mark-down or commission and may not necessarily represent actual transactions. The closing sales price of the Company's Common Stock was $19.15 per share at February 22, 2011.

| | | High | Low |
|---|---|---|---|
| 2010: | First quarter | $25.14 | $18.93 |
| | Second quarter | 25.04 | 16.69 |
| | Third quarter | 18.61 | 15.11 |
| | Fourth quarter | 21.20 | 15.97 |
| | | **High** | **Low** |
| 2009: | First quarter | $21.68 | $ 7.36 |
| | Second quarter | 14.92 | 7.82 |
| | Third quarter | 16.91 | 9.18 |
| | Fourth quarter | 19.06 | 14.85 |

The Company paid cash dividends to the common shareholders of $.17 per share on April 19, 2010 to all holders of record on April 1, 2010 and $.19 per share on October 18, 2010 to all holders of record on September 30, 2010, or $24,444,000 in the aggregate during 2010. The Company paid cash dividends to the shareholders in 2009 of $.17 per share on May 11 and November 2, 2009, to all holders of record on April 27 and October 19, 2009, respectively, or $23,262,000 in the aggregate during 2009.

Additionally, as a result of the Company's participation in the TARP Capital Purchase Program, the Company is restricted in the payment of dividends and may not without the Treasury Department's consent, declare or pay any dividend on the Company Common Stock other than a regular semi-annual cash dividend of not more than $.33 per share, as adjusted for any stock dividend or stock split. The restriction ceases to exist only on the earlier to occur of December 23, 2011 or the date on which the Company has redeemed all of the Series A Preferred Stock issued as part of the Capital Purchase Program or the date on which the Treasury has transferred all of the Preferred Stock to third parties not affiliated with the Treasury. On April 7, 2009, the Company gained consent from the Treasury Department (the "Treasury Consent") to use the regular semi-annual cash dividend funds of not more than $.33 per share, as adjusted for any stock dividend or stock split, to pay quarterly dividends and to repurchase common stock. While the IBC Board is inclined to continue to declare regular semi-annual cash dividends, the Board may decide to pay quarterly cash dividends in the future and the amount of any cash dividends, combined with amounts spent in conjunction with the Company's stock repurchase program, will be limited by the restrictions set forth in the Treasury Consent. There can be no assurance as to future dividends because they are dependent upon the Company's future earnings, capital requirements, financial condition, acquisition opportunities and general business conditions at the time.

In addition, the Company has issued common stock dividends during the last five-year period as follows:

| Date | Stock Dividend |
|---|---|
| May 2006 | 0% |
| May 2007 | 10% |
| May 2008 | 0% |
| May 2009 | 0% |
| May 2010 | 0% |

The Company's principal source of funds to pay cash dividends on its Common Stock and Series A Preferred Stock is cash dividends from its bank subsidiaries. For a discussion of the limitations, please see Note 20 of Notes to Consolidated Financial Statements.

**Stock Repurchase Program**

The Company terminated its stock repurchase program on December 19, 2008, in connection with participating in the TARP Capital Purchase Program, which program prohibited stock repurchases, except for repurchases made in connection with the administration of an employee benefit plan in the ordinary course of business and consistent with past practices. On April 7, 2009, the Company obtained consent from the Treasury to repurchase shares of the Company's common stock; provided, however, that in no event will the aggregate amount of cash dividends and common stock repurchases for a given semi-annual period exceed the aggregate amount that would be used to pay the originally permitted semi-annual cash dividend of $.33 per share. The Company also received consent from the Treasury to pay quarterly dividends. The Company will determine on an ongoing basis the best use of the funds and whether a more frequent dividend program and expanded repurchase program are warranted and beneficial to its shareholders. Following receipt of the Treasury Department's consent, the Board of Directors established a formal stock repurchase program that authorized the repurchase of up to $40 million of common stock within the following twelve months and on March 9, 2010, the Board of Directors extended the repurchase program and again authorized the repurchase of up to $40 million of common stock during the twelve month period expiring on April 9, 2011, which repurchase cap the Board is inclined to increase over time, subject to the limitations imposed by the Treasury Department's consent. Stock repurchases may be made from time to time, on the open market or through private transactions. Shares repurchased in this program will be held in treasury for reissue for various corporate purposes, including employee stock option plans. As of February 22, 2011, a total of 7,322,172 shares had been repurchased under all programs at a cost of $229,384,000.

Except for repurchases in connection with the administration of an employee benefit plan in the ordinary course of business and consistent with past practices, common stock repurchases are only conducted under publicly announced repurchase programs approved by the Board of Directors. The

following table includes information about common stock share repurchases for the quarter ended December 31, 2010.

| | Total Number of Shares Purchased | Average Price Paid Per Share | Total Number of Shares Purchased as Part of a Publicly-Announced Program | Approximate Dollar Value of Shares Available for Repurchase(1) |
|---|---|---|---|---|
| October 1 - October 31, 2010 | 15,600 | $16.30 | 15,600 | $33,252,000 |
| November 1 - November 30, 2010 | 11,016 | 18.25 | 11,016 | 33,051,000 |
| December 1 - December 31, 2010 | — | — | — | 33,051,000 |
| Total | 26,616 | $17.10 | 26,616 | |

(1) The repurchase program was extended on March 9, 2010 and allows for the repurchase of up to an additional $40,000,000 of treasury stock through April 9, 2011.

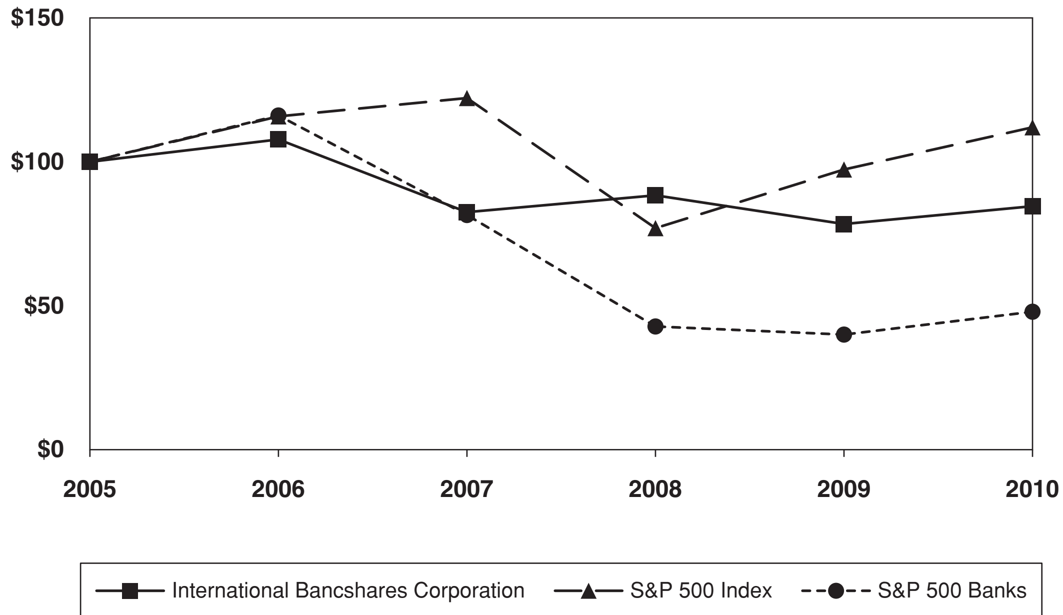
**Equity Compensation Plan Information**

The following table sets forth information as of December 31, 2010, with respect to the Company's equity compensation plans:

| Plan Category | (A) Number of securities to be issued upon exercise of outstanding options, warrants and rights | (B) Weighted average exercise price of outstanding options, warrants and rights | (C) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column A) |
|---|---|---|---|
| Equity Compensation plans approved by security holders | 764,982 | $20.65 | 193,197 |
| Total | 764,982 | $20.65 | 193,197 |

**Stock Performance**

## COMPARISON OF CUMULATIVE FIVE YEAR TOTAL RETURN




**Total Return To Shareholders**
**(Includes reinvestment of dividends)**

| Company / Index | Base Period 2005 | INDEXED RETURNS December 31, 2006 | 2007 | 2008 | 2009 | 2010 |
|---|---|---|---|---|---|---|
| **International Bancshares Corporation** | **100** | 107.78 | 82.52 | 88.36 | 78.39 | 84.58 |
| **S&P 500 Index** | **100** | 115.79 | 122.16 | 76.96 | 97.33 | 111.99 |
| **S&P 500 Banks** | **100** | 116.10 | 81.52 | 42.80 | 39.98 | 47.92 |

## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders
International Bancshares Corporation

We have audited the accompanying consolidated statements of condition of International Bancshares Corporation and subsidiaries as of December 31, 2010 and 2009, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2010. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of International Bancshares Corporation and subsidiaries as of December 31, 2010 and 2009, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2010, in conformity with U.S. generally accepted accounting principles.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), International Bancshares Corporation and subsidiaries' internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated February 28, 2011 expressed an unqualified opinion on the effectiveness of International Bancshares Corporation and subsidiaries' internal control over financial reporting.

/s/ McGladrey & Pullen, LLP

Dallas, Texas
February 28, 2011

**INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES**

**Consolidated Statements of Condition**

**December 31, 2010 and 2009**

**(Dollars in Thousands, Except Per Share Amounts)**

| | 2010 | 2009 |
|---|---|---|
| **Assets** | | |
| Cash and due from banks | $ 197,814 | $ 224,638 |
| Cash and due from banks—cash and cash equivalents | 197,814 | 224,638 |
| Investment securities: | | |
| Held to maturity (Market value of $2,450 on December 31, 2010 and $2,450 on December 31, 2009) | 2,450 | 2,450 |
| Available for sale (Amortized cost of $5,041,847 on December 31, 2010 and $4,541,851 on December 31, 2009) | 5,086,457 | 4,644,083 |
| Total investment securities | 5,088,907 | 4,646,533 |
| Loans | 5,410,003 | 5,667,262 |
| Less allowance for probable loan losses | (84,482) | (95,393) |
| Net loans | 5,325,521 | 5,571,869 |
| Bank premises and equipment, net | 468,950 | 490,375 |
| Accrued interest receivable | 35,660 | 41,731 |
| Other investments | 360,955 | 359,404 |
| Identified intangible assets, net | 17,309 | 22,358 |
| Goodwill, net | 282,532 | 282,532 |
| Other assets | 165,821 | 123,103 |
| Total assets | $11,943,469 | $11,762,543 |

**See accompanying notes to consolidated financial statements.**

**INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES**

**Consolidated Statements of Condition (Continued)**

**December 31, 2010 and 2009**

**(Dollars in Thousands, Except Per Share Amounts)**

| | 2010 | 2009 |
|---|---|---|
| **Liabilities and Shareholders' Equity** | | |
| Liabilities: | | |
| Deposits: | | |
| Demand—non-interest bearing | $ 1,639,076 | $ 1,516,799 |
| Savings and interest bearing demand | 2,522,842 | 2,262,552 |
| Time | 3,437,640 | 3,398,656 |
| Total deposits | 7,599,558 | 7,178,007 |
| Securities sold under repurchase agreements | 1,433,270 | 1,441,817 |
| Other borrowed funds | 1,026,780 | 1,347,625 |
| Junior subordinated deferrable interest debentures | 201,117 | 201,082 |
| Other liabilities | 223,527 | 186,542 |
| Total liabilities | 10,484,252 | 10,355,073 |
| Commitments, Contingent Liabilities and Other Tax Matters (Note 17) | | |
| Shareholders' equity: | | |
| Series A cumulative perpetual preferred shares, $.01 par value, $1,000 per share liquidation value. Authorized 25,000,000 shares; issued 216,000 shares on December 31, 2010, net of discount of $7,932 and 216,000 shares on December 31, 2009 net of discount of $10,258 | 208,068 | 205,742 |
| Common shares of $1.00 par value. Authorized 275,000,000 shares; issued 95,711,285 shares on December 31, 2010 and 95,711,111 shares on December 31, 2009 | 95,711 | 95,711 |
| Surplus | 162,276 | 161,258 |
| Retained earnings | 1,214,743 | 1,122,290 |
| Accumulated other comprehensive income | 28,777 | 65,878 |
| | 1,709,575 | 1,650,879 |
| Less cost of shares in treasury, 28,016,059 shares on December 31, 2010 and 27,607,171 shares on December 31, 2009 | (250,358) | (243,409) |
| Total shareholders' equity | 1,459,217 | 1,407,470 |
| Total liabilities and shareholders' equity | $11,943,469 | $11,762,543 |

**See accompanying notes to consolidated financial statements.**

## INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

**Consolidated Statements of Income**

**Years ended December 31, 2010, 2009 and 2008**

**(Dollars in Thousands, Except Per Share Amounts)**

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| Interest income: | | | |
| Loans, including fees | $314,202 | $335,769 | $370,718 |
| Federal funds sold | — | — | 927 |
| Investment securities: | | | |
| Taxable | 135,106 | 185,931 | 188,928 |
| Tax-exempt | 7,240 | 5,070 | 3,514 |
| Other interest income | 2,221 | 607 | 516 |
| Total interest income | 458,769 | 527,377 | 564,603 |
| Interest expense: | | | |
| Savings and interest bearing demand deposits | 9,383 | 10,832 | 26,651 |
| Time deposits | 46,967 | 62,255 | 106,479 |
| Securities sold under repurchase agreements | 44,216 | 44,723 | 50,400 |
| Other borrowings | 1,269 | 9,451 | 33,976 |
| Junior subordinated deferrable interest debentures | 12,201 | 12,535 | 14,137 |
| Other interest expense | — | — | 88 |
| Total interest expense | 114,036 | 139,796 | 231,731 |
| Net interest income | 344,733 | 387,581 | 332,872 |
| Provision for probable loan losses | 22,812 | 58,833 | 19,813 |
| Net interest income after provision for probable loan losses | 321,921 | 328,748 | 313,059 |
| Non-interest income: | | | |
| Service charges on deposit accounts | 99,644 | 99,642 | 98,466 |
| Other service charges, commissions and fees | | | |
| Banking | 47,930 | 42,861 | 40,543 |
| Non-banking | 8,439 | 12,697 | 7,592 |
| Investment securities transactions, net | 33,209 | 11,956 | 6,427 |
| Other investments, net | 17,696 | 19,773 | 15,183 |
| Other income | 11,866 | 14,084 | 21,598 |
| Total non-interest income | 218,784 | 201,013 | 189,809 |

**See accompanying notes to consolidated financial statements.**

## INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

**Consolidated Statements of Income (Continued)**

**Years ended December 31, 2010, 2009 and 2008**

**(Dollars in Thousands, Except Per Share Amounts)**

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| Non-interest expense: | | | |
| Employee compensation and benefits | $ 127,469 | $ 130,849 | $ 129,084 |
| Occupancy | 36,631 | 35,374 | 38,315 |
| Depreciation of bank premises and equipment | 35,395 | 35,879 | 36,700 |
| Professional fees | 15,625 | 12,640 | 10,051 |
| Deposit insurance assessments | 10,253 | 10,249 | 1,027 |
| Amortization of identified intangible assets | 5,284 | 5,286 | 5,195 |
| Advertising | 7,716 | 9,149 | 13,189 |
| Litigation expense | 21,837 | — | — |
| Impairment charges (Total other-than-temporary impairment charges, $(19,070) less loss of $10,654 included in other comprehensive income) | 8,416 | — | — |
| Other | 71,099 | 69,605 | 67,665 |
| Total non-interest expense | 339,725 | 309,031 | 301,226 |
| Income before income taxes | 200,980 | 220,730 | 201,642 |
| Provision for income taxes | 70,957 | 77,988 | 69,530 |
| Net income | $ 130,023 | $ 142,742 | $ 132,112 |
| Preferred stock dividends and discount accretion | 13,126 | 12,984 | — |
| Net income available to common shareholders | $ 116,897 | $ 129,758 | $ 132,112 |
| Basic earnings per common share: | | | |
| Weighted average number of shares outstanding | 67,921,353 | 68,373,732 | 68,576,654 |
| Net income | $ 1.72 | $ 1.90 | $ 1.93 |
| Fully diluted earnings per common share: | | | |
| Weighted average number of shares outstanding | 68,004,441 | 68,394,624 | 68,714,390 |
| Net income | $ 1.72 | $ 1.90 | $ 1.92 |

**See accompanying notes to consolidated financial statements.**

## INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

**Consolidated Statements of Comprehensive Income**

**Years ended December 31, 2010, 2009, and 2008**

**(Dollars in Thousands)**

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| Net income | $130,023 | $142,742 | $132,112 |
| Other comprehensive income, net of tax: | | | |
| Net unrealized holding (losses) gains on securities available for sale arising during period (tax effects of $(11,300), $29,863, and $11,955) | (20,985) | 55,460 | 22,202 |
| Reclassification adjustment for gains on securities available for sale included in net income (tax effects of $(11,623), $(4,185), and $(2,249)) | (21,586) | (7,771) | (4,178) |
| Reclassification adjustment for impairment charges on available for sale securities included in net income (tax effects of $2,946, $0, and $0) | 5,470 | — | — |
| Comprehensive income | $ 92,922 | $190,431 | $150,136 |

**See accompanying notes to consolidated financial statements.**

## INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

### Consolidated Statements of Shareholders' Equity

### Years ended December 31, 2010, 2009 and 2008

### (in Thousands)

| | Preferred Stock | Number of Shares | Common Stock | Surplus | Retained Earnings | Other Comprehensive Income (Loss) | Treasury Stock | Total |
|---|---|---|---|---|---|---|---|---|
| Balance at December 31, 2007 | $ — | 95,441 | $95,441 | $144,140 | $ 929,145 | $ 165 | $(232,986) | $ 935,905 |
| Net Income | — | — | — | — | 132,112 | — | — | 132,112 |
| Dividends: | | | | | | | | |
| Cash ($.66 per share) | — | — | — | — | (45,253) | — | — | (45,253) |
| Issuance of preferred stock | 203,558 | — | — | 12,442 | — | — | — | 216,000 |
| Purchase of treasury (48,339 shares) | — | — | — | — | — | — | (1,077) | (1,077) |
| Exercise of stock options | — | 58 | 58 | 836 | — | — | — | 894 |
| Stock compensation expense recognized in earnings | — | — | — | 692 | — | — | — | 692 |
| Other comprehensive income, net of tax: | | | | | | | | |
| Net change in unrealized gains and losses on available for sale securities, net of reclassification adjustment | — | — | — | — | — | 18,024 | — | 18,024 |
| Balance at December 31, 2008 | 203,558 | 95,499 | 95,499 | 158,110 | 1,016,004 | 18,189 | (234,063) | 1,257,297 |
| Net Income | — | — | — | — | 142,742 | — | — | 142,742 |
| Dividends: | | | | | | | | |
| Cash ($.34 per share) | — | — | — | — | (23,262) | — | — | (23,262) |
| Preferred stock (5%) including discount accretion | 2,184 | — | — | — | (13,194) | — | — | (11,010) |
| Purchase of treasury stock (708,952 shares) | — | — | — | — | — | — | (9,346) | (9,346) |
| Exercise of stock options | — | 212 | 212 | 2,493 | — | — | — | 2,705 |
| Stock compensation expense recognized in earnings | — | — | — | 655 | — | — | — | 655 |
| Other comprehensive income, net of tax: | | | | | | | | |
| Net change in unrealized gains and losses on available for sale securities, net of reclassification adjustment | — | — | — | — | — | 47,689 | — | 47,689 |
| Balance at December 31, 2009 | 205,742 | 95,711 | 95,711 | 161,258 | 1,122,290 | 65,878 | (243,409) | 1,407,470 |
| Net Income | — | — | — | — | 130,023 | — | — | 130,023 |
| Dividends: | | | | | | | | |
| Cash ($.36 per share) | — | — | — | — | (24,444) | — | — | (24,444) |
| Preferred stock (5%) including discount accretion | 2,326 | — | — | — | (13,126) | — | — | (10,800) |
| Purchase of treasury stock (408,888 shares) | — | — | — | — | — | — | (6,949) | (6,949) |
| Exercise of stock options | — | — | — | 484 | — | — | — | 484 |
| Stock compensation expense recognized in earnings | — | — | — | 534 | — | — | — | 534 |
| Other comprehensive loss, net of tax: | | | | | | | | |
| Net change in unrealized gains and losses on available for sale securities, net of reclassification adjustments | — | — | — | — | — | (37,101) | — | (37,101) |
| Balance at December 31, 2010 | $208,068 | 95,711 | $95,711 | $162,276 | $1,214,743 | $ 28,777 | $(250,358) | $1,459,217 |

**See accompanying notes to consolidated financial statements.**

**INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES**

**Consolidated Statements of Cash Flows**

**Years ended December 31, 2010, 2009 and 2008**

**(Dollars in Thousands)**

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| Operating activities: | | | |
| Net income | $ 130,023 | $ 142,742 | $ 132,112 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Provision for probable loan losses | 22,812 | 58,833 | 19,813 |
| Amortization of loan premiums | — | — | 134 |
| Accretion of discounts on time deposits with banks | — | — | 1 |
| Accretion of time deposit discounts | (14) | (14) | (36) |
| Depreciation of bank premises and equipment | 35,395 | 35,879 | 36,700 |
| (Gain) loss on sale of bank premises and equipment | (22) | 80 | 282 |
| Depreciation and amortization of leased assets | — | 300 | 880 |
| Accretion of investment securities discounts | (1,693) | (1,940) | (1,405) |
| Amortization of investment securities premiums | 13,211 | 6,911 | 6,017 |
| Investment securities transactions, net | (33,209) | (11,956) | (6,427) |
| Impairment charges on available for sale securities | 8,416 | — | — |
| Accretion of junior subordinated debenture discounts | 35 | 34 | 119 |
| Amortization of identified intangible assets | 5,284 | 5,286 | 5,195 |
| Stock based compensation expense | 534 | 655 | 692 |
| Earnings from affiliates and other investments | (15,023) | (16,891) | (11,324) |
| Deferred tax benefit | (3,532) | (3,035) | (4,683) |
| Decrease in accrued interest receivable | 6,071 | 6,981 | 5,589 |
| Increase in other assets | (42,718) | (69,845) | (10,677) |
| Increase (decrease) in other liabilities | 1,652 | (12,253) | (18,878) |
| Net cash provided by operating activities | 127,222 | 141,767 | 154,104 |
| Investing activities: | | | |
| Proceeds from maturities of securities | 4,423 | 1,637 | 18,124 |
| Proceeds from sales and calls of available for sale securities | 1,149,021 | 579,099 | 8,376 |
| Purchases of available for sale securities | (2,666,596) | (1,280,925) | (2,002,446) |
| Principal collected on mortgage backed securities | 1,085,817 | 1,224,938 | 1,186,450 |
| Proceeds from matured time deposits with banks | — | 396 | 4,457 |
| Net decrease (increase) in loans | 223,536 | 168,671 | (344,418) |
| Purchases of other investments | (7,438) | (11,430) | (60,567) |
| Distributions from other investments | 20,910 | 56,988 | 7,385 |
| Purchases of bank premises and equipment | (15,953) | (61,015) | (68,537) |
| Proceeds from sales of bank premises and equipment | 2,005 | 1,052 | 838 |
| Purchase, adjustment of identified intangible asset | (235) | (259) | (1,074) |
| Net cash (used in) provided by investing activities | (204,510) | 679,152 | (1,251,412) |

**See accompanying notes to consolidated financial statements.**

**INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES**

**Consolidated Statements of Cash Flows (Continued)**

**Years ended December 31, 2010, 2009 and 2008**

**(Dollars in Thousands)**

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| Financing activities: | | | |
| Net increase (decrease) in non-interest bearing demand deposits | $ 122,277 | $ 57,129 | $ (52,957) |
| Net increase (decrease) in savings and interest bearing demand deposits | 260,290 | 180,950 | (210,987) |
| Net increase (decrease) in time deposits | 38,998 | 81,158 | (34,842) |
| Net (decrease)increase in securities sold under repurchase agreements | (8,547) | 686 | 112,148 |
| Other borrowed funds, net | (320,845) | (1,175,361) | 1,066,050 |
| Purchase of treasury stock | (6,949) | (9,346) | (1,077) |
| Proceeds from stock transactions | 484 | 2,705 | 216,894 |
| Payments of cash dividends—common | (24,444) | (23,262) | (45,253) |
| Payments of cash dividends—preferred | (10,800) | (9,660) | — |
| Net cash provided by (used in) financing activities | 50,464 | (895,001) | 1,049,976 |
| Decrease in cash and cash equivalents | (26,824) | (74,082) | (47,332) |
| Cash and cash equivalents at beginning of year | 224,638 | 298,720 | 346,052 |
| Cash and cash equivalents at end of year | $ 197,814 | $ 224,638 | $ 298,720 |
| Supplemental cash flow information: | | | |
| Interest paid | $ 116,037 | $ 146,778 | $ 245,509 |
| Income taxes paid | 78,435 | 83,830 | 69,646 |
| Purchases of available-for-sale securities not yet settled | 160,216 | 100,829 | 84,768 |
| Net transfers from loans to other real estate owned | 59,429 | 22,487 | 28,776 |
| Accrued dividends, preferred shares | 1,350 | 1,350 | — |

**See accompanying notes to consolidated financial statements.**

## (1) Summary of Significant Accounting Policies

The accounting and reporting policies of International Bancshares Corporation ("Corporation") and Subsidiaries (the Corporation and Subsidiaries collectively referred to herein as the "Company") conform to accounting principles generally accepted in the United States of America and to general practices within the banking industry. The following is a description of the more significant of those policies.

*Consolidation and Basis of Presentation*

The consolidated financial statements include the accounts of the Corporation and its wholly-owned bank subsidiaries, International Bank of Commerce, Laredo ("IBC"), Commerce Bank, International Bank of Commerce, Zapata, International Bank of Commerce, Brownsville, and the Corporation's wholly-owned non-bank subsidiaries, IBC Subsidiary Corporation, IBC Life Insurance Company, IBC Trading Company, Premier Tierra Holdings, Inc. and IBC Capital Corporation. All significant inter-company balances and transactions have been eliminated in consolidation.

The Company, through its subsidiaries, is primarily engaged in the business of banking, including the acceptance of checking and savings deposits and the making of commercial, real estate, personal, home improvement, automobile and other installment and term loans. The primary markets of the Company are South, Central, and Southeast Texas and the state of Oklahoma. Each bank subsidiary is very active in facilitating international trade along the United States border with Mexico and elsewhere. Although the Company's loan portfolio is diversified, the ability of the Company's debtors to honor their contracts is primarily dependent upon the economic conditions in the Company's trade area. In addition, the investment portfolio is directly impacted by fluctuations in market interest rates. The Company and its bank subsidiaries are subject to the regulations of certain Federal agencies as well as the Texas Department of Banking and undergo periodic examinations by those regulatory authorities. Such agencies may require certain standards or impose certain limitations based on their judgments or changes in law and regulations.

The Company owns two insurance-related subsidiaries, IBC Life Insurance Company and IBC Insurance Agency, Inc., a wholly owned subsidiary of IBC, the bank subsidiary. Neither of the insurance-related subsidiaries conducts underwriting activities. The IBC Life Insurance Company is in the business of reinsuring credit life and credit accident and health insurance. The business is assumed from an unaffiliated insurer and the only business written is generated by the bank subsidiaries of the Company. The risk assumed on each of the policies is not significant to the consolidated financial statements.

The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the dates of the statement of condition and income and expenses for the periods. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to significant changes in the near-term relate to the determination of the allowance for probable loan losses.

On July 1, 2009, the Financial Accounting Standards Board officially launched the "FASB Accounting Standards Codification," ("Codification"), which is now the single official source of authoritative, non-governmental U.S. GAAP, in addition to guidance issued by the Securities and Exchange Commission ("SEC"). The Codification supersedes all prior accounting literature. With the launch of the Codification, U.S. GAAP now consists of two levels—authoritative (Codification) and non-authoritative (anything not in the Codification). The Codification is effective for interim and annual periods ending after September 15, 2009, and is organized into approximately 90 accounting topics. The FASB will no longer be issuing accounting standards in the form of Statements, Staff Positions or Emerging Issues Task Force Abstracts.

**(1) Summary of Significant Accounting Policies (Continued)**

The FASB will instead amend the Codification by issuing "Accounting Standards Updates." The adoption of the Codification did not have a significant impact to the Company's consolidated financial statements.

*Subsequent Events*

Effective June 30, 2009, the Company adopted Statement of Financial Accounting Standards No. 165 ("SFAS No. 165"), "Subsequent Events." SFAS No. 165 is currently included in the Codification under ASC Topic 855, "Subsequent Events" ("ASC 855"). ASC 855 establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or available to be issued. ASC 855 defines (i) the period after the balance sheet date during which a reporting entity's management should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements (ii) the circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements and (iii) the disclosures an entity should make about events or transactions that occurred after the balance sheet date. The adoption of the accounting standard did not have an impact on the Company's consolidated financial statements. The Company has evaluated all events or transactions that occurred through the date the Company issued these financial statements. During this period, the Company did not have any material recognizable or non-recognizable subsequent events.

*Investment Securities*

The Company classifies debt and equity securities into one of these categories: held-to-maturity, available-for-sale, or trading. Such classifications are reassessed for appropriate classification at each reporting date. Securities that are intended and expected to be held until maturity are classified as "held-to-maturity" and are carried at amortized cost for financial statement reporting. Securities that are not positively expected to be held until maturity, but are intended to be held for an indefinite period of time are classified as "available-for-sale" or "trading" and are carried at their fair value. Unrealized holding gains and losses are included in net income for those securities classified as "trading", while unrealized holding gains and losses related to those securities classified as "available-for-sale" are excluded from net income and reported net of tax as other comprehensive income and in shareholders' equity as accumulated other comprehensive income until realized. The Company did not maintain any trading securities during the three year period ended December 31, 2010.

Mortgage-backed securities held at December 31, 2010 and 2009 represent participating interests in pools of long-term first mortgage loans originated and serviced by the issuers of the securities. Mortgage-backed securities are either issued or guaranteed by the U.S. Government or its agencies including the Federal Home Loan Mortgage Corporation ("Freddie Mac"), the Federal National Mortgage Association ("Fannie Mae"), the Government National Mortgage Association ("Ginnie Mae") or other non-government entities. Investments in mortgage-backed securities issued by Ginnie Mae are fully guaranteed by the U. S. Government. Investments in mortgage-backed securities issued by Freddie Mac and Fannie Mae are not fully guaranteed by the U.S. Government, however, the Company believes that the quality of the bonds is similar to other AAA rated bonds with limited credit risk, particularly given the placement of Fannie Mae and Freddie Mac into conservatorship by the federal government in early September 2008. Market interest rate fluctuations can affect the prepayment speed of principal and the yield on the security.

**(1) Summary of Significant Accounting Policies (Continued)**

Premiums and discounts are amortized using the level yield or "interest method" over the terms of the securities. Declines in the fair value of held-to-maturity and available-for sale-securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In determining whether other-than-temporary impairment exists, management considers many factors, including (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent of the Company to hold and the determination of whether the Company will more likely than not be required to sell the security prior to a recovery in fair value. If the Company determines that (1) it intends to sell the security or (2) it is more likely than not that it will be required to sell the security before it's anticipated recovery, the other-than-temporary impairment that is recognized in earnings is equal to the difference between the fair value of the security and the Company's amortized cost in the security. If the Company determines that it (1) does not intend to sell the security and (2) it will not be more likely than not required to sell the security before it's anticipated recovery, the other-than-temporary impairment is segregated into its two components (1) the amount of impairment related to credit loss and (2) the amount of impairment related to other factors. The difference between the present value of the cash flows expected to be collected and the amortized cost is the credit loss recognized through earnings and an adjustment to the cost basis of the security. The amount of impairment related to other factors is included in other comprehensive income (loss). Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

*Provision and Allowance for Probable Loan Losses*

The allowance for probable loan losses is maintained at a level considered adequate by management to provide for probable loan losses. The allowance is increased by provisions charged to operating expense and reduced by net charge-offs. The provision for probable loan losses is the amount, which, in the judgment of management, is necessary to establish the allowance for probable loan losses at a level that is adequate to absorb known and inherent risks in the loan portfolio.

Management believes that the allowance for probable loan losses is adequate. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's bank subsidiaries' allowances for probable loan losses. Such agencies may require the Company's bank subsidiaries to make additions or reductions to their GAAP allowances based on their judgments of information available to them at the time of their examination.

*Loans*

Loans are reported at the principal balance outstanding, net of unearned discounts. Interest income on loans is reported on an accrual basis. Loan fees and costs associated with originating the loans are amortized over the life of the loan using the interest method. The Company originates mortgage loans that may subsequently be sold to an unaffiliated third party. The loans are not securitized and if sold, are sold without recourse. Loans held for sale are carried at cost and the principal amount outstanding is not significant to the consolidated financial statements.

**(1) Summary of Significant Accounting Policies (Continued)**

*Impaired Loans*

Impaired loans are those loans where it is probable that all amounts due according to contractual terms of the loan agreement will not be collected. Impaired loans are measured based on (1) the present value of expected future cash flows discounted at the loan's effective interest rate; (2) the loan's observable market price; or (3) the fair value of the collateral if the loan is collateral dependent. Substantially all of the Company's impaired loans are measured at the fair value of the collateral. In limited cases the Company may use other methods to determine the level of impairment of a loan if such loan is not collateral dependent.

*Non-Accrual Loans*

The non-accrual loan policy of the Company's bank subsidiaries is to discontinue the accrual of interest on loans when management determines that it is probable that future interest accruals will be un-collectible. As it relates to consumer loans, management charges off those loans when the loan is contractually 90 days past due. Under special circumstances, a consumer or non-consumer loan may be more than 90 days delinquent as to interest or principal and not be placed on non-accrual status. This situation generally results when a bank subsidiary has a borrower who is experiencing financial difficulties, but not to the extent that requires a restructuring of indebtedness. The majority of this category is composed of loans that are considered to be adequately secured and/or for which there are expected future payments. When a loan is placed on non-accrual status, any interest accrued, not paid is reversed and charged to operations against interest income. As it relates to non-consumer loans that are not 90 days past due, management will evaluate each of these loans to determine if placing the loan on non-accrual status is warranted. Interest income on non-accrual loans is recognized only to the extent payments are received or when, in management's opinion, the debtor's financial condition warrants reestablishment of interest accruals.

*Other Real Estate Owned*

Other real estate owned is comprised of real estate acquired by foreclosure and deeds in lieu of foreclosure. Other real estate is carried at the lower of the recorded investment in the property or its fair value less estimated costs to sell such property (as determined by independent appraisal). Prior to foreclosure, the value of the underlying loan is written down to the fair value of the real estate to be acquired by a charge to the allowance for loan probable losses, if necessary. Any subsequent write-downs are charged against other non-interest expense. Operating expenses of such properties and gains and losses on their disposition are included in other non-interest expense. Other real estate owned totaled $87,192,000 and $35,326,000 at December 31, 2010 and 2009, respectively. Other real estate owned is included in other assets.

*Bank Premises and Equipment*

Bank premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed on straight-line and accelerated methods over the estimated useful lives of the assets. Repairs and maintenance are charged to operations as incurred and expenditures for renewals and betterments are capitalized.

**(1) Summary of Significant Accounting Policies (Continued)**

*Other Investments*

Other investments include equity investments in non-financial companies, bank owned life insurance, as well as equity securities with no readily determinable fair market value. Equity investments are accounted for using the equity method of accounting. Equity securities with no readily determinable fair value are accounted for using the cost method.

*Income Taxes*

Deferred income tax assets and liabilities are determined using the asset and liability method. Under this method, the net deferred tax asset or liability is determined based on the tax effects of the differences between the book and tax basis of the various balance sheet assets and liabilities and gives current recognition to changes in tax rates and laws. The Company files a consolidated federal income tax return with its subsidiaries.

Recognition of deferred tax assets is based on management's belief that the benefit related to certain temporary differences, tax operating loss carry forwards, and tax credits are more likely than not to be realized. A valuation allowance is recorded for the amount of the deferred tax items for which it is more likely than not that the tax benefits will not be realized.

The Company evaluates uncertain tax positions at the end of each reporting period. The Company may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefit recognized in the financial statements from any such a position is measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement. As of December 31, 2010 and 2009, respectively, after evaluating all uncertain tax positions, the Company has recorded no liability for unrecognized tax benefits at the end of the reporting period. The Company would recognize any interest accrued on unrecognized tax benefits as other interest expense and penalties as other non-interest expense. During the years ended December 31, 2010, 2009 and 2008, the Company recognized no interest expense or penalties related to uncertain tax positions.

The Company files consolidated tax returns in the U.S. Federal jurisdiction and various state jurisdictions. The Company is no longer subject to U.S. federal or state income tax examinations by tax authorities for years before 2007.

*Stock Options*

Compensation expense for stock awards is based on the market price of the stock on the measurement date, which is generally the date of grant, and is recognized ratably over the service period of the award.

The fair value of stock options granted was estimated as the measurement date, which is generally the date of grant, using the Black-Sholes-Merton option-pricing model. This model was developed for use in estimating the fair value of publicly traded options that have no vesting restrictions and are fully transferable. Additionally, the model requires the input of highly subjective assumptions. Because the Company's employee stock options have characteristics significantly different from those of publicly traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the Black-Scholes-Merton option-pricing model does not necessarily provide a reliable single measure of the fair value of the Company's stock options.

**(1) Summary of Significant Accounting Policies (Continued)**

*Net Income Per Share*

Basic Earnings Per Share ("EPS") is calculated by dividing net income by the weighted average number of common shares outstanding. The computation of diluted EPS assumes the issuance of common shares for all dilutive potential common shares outstanding during the reporting period. The dilutive effect of stock options is considered in earnings per share calculations, if dilutive, using the treasury stock method.

*Goodwill and Identified Intangible Assets*

Goodwill represents the excess of costs over fair value of assets of businesses acquired. Goodwill is tested for impairment at least annually or on an interim basis if an event triggering impairment may have occurred. As of October 1, 2010, after completing goodwill testing, the Company has determined that no goodwill impairment exists.

Identified intangible assets are acquired assets that lack physical substance but can be distinguished from goodwill because of contractual or other legal rights or because the asset is capable of being sold or exchanged either on its own or in combination with a related contract, asset, or liability. The Company's identified intangible assets relate to core deposits and contract rights. As of December 31, 2010, the Company has determined that no impairment of identified intangibles exists. Identified intangible assets with definite useful lives are amortized on an accelerated basis over their estimated life. See Note 6— Goodwill and Other Intangible Assets.

*Impairment of Long-Lived Assets*

Long-lived assets, such as property, plant and equipment, and purchased intangibles subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying value of the asset to the estimated undiscounted future cash flows expected to be generated by the asset. If the carrying value of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying value of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the statement of condition and reported at the lower of the carrying value or fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposed group classified as held for sale would be presented separately in the appropriate asset and liability sections of the statement of condition.

*Consolidated Statements of Cash Flows*

For purposes of the consolidated statements of cash flows, the Company considers all short-term investments with a maturity at date of purchase of three months or less to be cash equivalents. Also, the Company reports transactions related to deposits and loans to customers on a net basis.

*Accounting for Transfers and Servicing of Financial Assets*

The Company accounts for transfers and servicing of financial assets and extinguishments of liabilities based on the application of a financial-components approach that focuses on control. After a transfer of financial assets, the Company recognizes the financial and servicing assets it controls and liabilities it has incurred, derecognizes financial assets when control has been surrendered and derecognizes liabilities

**(1) Summary of Significant Accounting Policies (Continued)**

when extinguished. The Company has retained mortgage servicing rights in connection with the sale of mortgage loans. Because the Company may not initially identify loans as originated for resale, all loans are initially treated as held for investment. The value of the mortgage servicing rights are reviewed periodically for impairment and are amortized in proportion to, and over the period of estimated net servicing income or net servicing losses. The value of the mortgage servicing rights is not significant to the consolidated statements of condition.

*Segments of an Enterprise and Related Information*

The Company operates as one segment. The operating information used by the Company's chief executive officer for purposes of assessing performance and making operating decisions about the Company is the consolidated financial statements presented in this report. The Company has four active operating subsidiaries, namely, the bank subsidiaries, otherwise known as International Bank of Commerce, Laredo, Commerce Bank, International Bank of Commerce, Zapata and International Bank of Commerce, Brownsville.

*Comprehensive Income*

Comprehensive income consists of net income and other comprehensive income (loss). Other comprehensive income (loss) includes unrealized gains and losses on securities available for sale.

*Advertising*

Advertising costs are expensed as incurred.

*Reclassifications*

Certain amounts in the prior year's presentations have been reclassified to conform to the current presentation. These reclassifications had no effect on previously reported net income or total assets.

Additionally, subsequent to the filing of the Company's annual report on Form 10K for the year ended December 31, 2009, the Company identified that cash flows arising from the purchases of available-for-sale securities, not yet settled, had been presented at the end of the prior period in the consolidated statement of cash flows as part of cash flows from operating activities instead of investing activity. The change resulted in a reclassification of $84.8 million for the year ended December 31, 2009 from net cash provided by operating activities to net cash provided by investing activities, which did not alter the net change in cash and cash equivalents reported. The impact of this reclassification is not considered material to the financial statements previously presented on the Form 10K for the year ended December 31, 2009.

*New Accounting Standards*

On April 9, 2009, the Financial Accounting Standards Board issued FASB Staff Position No. 157-4, "Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly" ("FSP No. 157-4"), included in ASC 820-10. ASC 820-10 provides additional guidance for estimating fair value in accordance with FASB ASC 820-10, "Fair Value Measurements," when the volume and level of activity for the asset or liability have significantly decreased. Additionally, the staff position also provides guidance on identifying circumstances that indicate a transaction is not orderly. The staff position stresses that even though there

**(1) Summary of Significant Accounting Policies (Continued)**

has been a significant decrease in the volume and level of activity for the asset or liability and regardless of the valuation techniques used to measure the fair value of the asset or liability, the main objective of fair value accounting measurements remains the same. As defined by the FSP, fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants as of the measurement date under current market conditions. Additionally, the staff position amends the fair value disclosures as originally required by ASC 820-10. The staff position is effective for interim and annual reporting periods ending after June 15, 2009, although early adoption is permitted for periods ending after March 15, 2009. The adoption of the staff position did not have a significant impact on the Company's consolidated financial statements.

On April 9, 2009, the Financial Accounting Standards Board issued FASB Staff Position No. 107-1 and APB 28-1, "Interim Disclosures about Fair Value of Financial Instruments" ("FSP No. 107-1 and APB 28-1"), included in ASC 825-10. The staff position amends FASB Statement No. 107, "Disclosures about Fair Value of Financial Instruments," also in ASC 825-10, to require disclosures about fair value of financial instruments for interim reporting periods of publicly traded companies as well as in annual financial statements. The FSP also amends Accounting Principles Board Opinion No. 28, "Interim Financial Reporting" to require those disclosures in summarized financial information at interim reporting periods. The new standard is effective for interim reporting periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009. The adoption of the staff accounting position did not have a significant impact on the Company's consolidated financial statements.

On April 9, 2009, the Financial Accounting Standards Board issued FASB Staff Position No. 115-2 and 124-2, "Recognition and Presentation of Other-Than-Temporary Impairments" ("FSP No. 115-2 and 124-2"), included in ASC 320-10 and amends the other-than-temporary guidance in U.S. GAAP for debt securities to make the guidance more operational and to improve the presentation and disclosure of other-than-temporary impairments in debt and equity securities in the financial statements. The staff position does not amend existing recognition and measurement guidance related to other-than-temporary impairment. The staff position requires that unless there is an intent or requirement to sell a debt security, only the amount of the estimated credit loss is recorded through earnings, while the remaining mark-to-market loss is recognized as a component of equity through other comprehensive income. Additionally, it enhances required disclosures of existing guidelines. The staff position is effective for interim and annual reporting periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009, and will be applied to all existing and new investments in debt securities. The adoption of the accounting standard did not have a significant impact on the Company's consolidated financial statements.

In August 2009, the Financial Accounting Standards Board issued Accounting Standards Update No. 2009-05, to ASC 820, "Fair Value Measurements and Disclosures." The Update provides amendments for the fair value measurement of liabilities. The Update clarifies which techniques should be used to measure fair value in the event that there are no quoted prices in active markets for an identical liability. The amendment also clarifies that when estimating the fair value of a liability, entities are not required to factor in any existing requirements that would affect the transferability of the asset. The Update is effective for the first interim and annual reporting period ending after issuance. The adoption of the update to existing accounting standards did not have a significant impact on the Company's consolidated financial statements.

**(1) Summary of Significant Accounting Policies (Continued)**

In September 2009, the Financial Accounting Standards Board issued Accounting Standards Update No. 2009-06, to update ASC 740, "Income Taxes." The Update addresses the need for additional implementation guidance in accounting for uncertainty in income taxes. The key provisions of the Update illustrate by example what should be done in the case where a decision needs to be made regarding whether the income tax is paid by the entity is attributable to the entity or its owners, what constitutes a tax position for a pass-through or tax exempt not-for-profit entity, and how the accounting for uncertainty in income taxes is impacted when a combined group include both taxable and non-taxable entities. The Update is effective for interim and annual reporting periods ending after September 15, 2009 for entities that are currently applying the standards for accounting for uncertainty in income taxes. The adoption of the update to existing accounting standards did not have a significant impact on the Company's consolidated financial statements.

In December 2009, the Financial Accounting Standards Board issued Accounting Standards Update No. 2009-16, to ASC 860, "Transfers and Servicing." The Update amends prior accounting guidance to enhance reporting about transfers of financial assets, including securitizations, and where companies have continued exposure to the risks related to the transferred financial assets. The Update eliminates the concept of a "qualifying special-purpose entity" and changes the requirements for derecognizing financial assets. The Update also requires additional disclosures about all continuing involvement by the entity in transferred financial assets including information about gains and losses resulting from transfers during the reporting period. The Update is effective for fiscal periods ending after January 1, 2010. The adoption of the update to existing accounting standards did not have a significant impact on the Company's consolidated financial statements.

In January 2010, the Financial Accounting Standards Board issued Accounting Standards Update No. 2010-06, to ASC 820, "Fair Value Measurements." The Update amends prior accounting guidance regarding fair value disclosures including required disclosure of (i) significant amounts of transfers of assets or liabilities between Levels 1 and 2 of the fair value hierarchy and the reasons for the transfers (ii) detailed gross information about activity related to assets or liabilities included in Level 3 of the fair value hierarchy for recurring fair value measurements, (iii) the policy for determining when transfers between the levels of the fair value hierarchy are recognized and (iv) the reasons for transfers of assets or liabilities in or out of Level 3 of the fair value hierarchy, with significant transfers disclosed separately. The Update further clarifies that (i) fair value disclosures should be provided for each class of assets and liabilities, where class would generally be a subset of assets or liabilities within a line item in the consolidated financial statements and (ii) disclosures about fair value inputs and techniques used for both recurring and nonrecurring fair value measurements included in Level 2 and 3 of the fair value hierarchy. The disclosures related to the detailed gross information about activity related to assets or liabilities included in Level 3 of the fair value hierarchy for recurring fair value measurements will be required for the Company beginning on January 1, 2011. The remaining disclosure requirements became effective for the Company on January 1, 2010. The adoption of the update to existing accounting standards did not have a significant impact on the Company's consolidated financial statements.

In July 2010, the Financial Accounting Standards Board issued Accounting Standards Update No. 2010-20, to ASC 310, "Receivables." The Update amends existing disclosure requirements regarding an entity's financing receivables. The main objective of the Update is intended to provide users of financial statements with greater transparency regarding an entity's allowance for credit losses and the quality of its financing receivables. The Update requires additional disclosures about (i) the credit risk inherent in the entity's portfolio of financing receivables, (ii) how the inherent risk in the portfolio is analyzed and

**(1) Summary of Significant Accounting Policies (Continued)**

assessed at arriving at the allowance for credit loss (iii) the changes and reasons for changes in the allowance for credit loss. Additionally, the Update clarifies that disclosures should be made on a disaggregated basis as defined in the Update—portfolio segment and class of financing receivable. Portfolio segment is defined as the level at which the entity develops an documents a systematic method for determining its allowance for credit loss and class of financing receivable is defined as a disaggregation of a portfolio segment. Existing disclosures are amended by the Update to include (i) a roll forward of the allowance for credit losses by portfolio segment with the ending balance disaggregated on the basis of impairment method, (ii) for each disaggregated balance, the related recorded investment in the financing receivable, (iii) the non-accrual status of financing receivable by class of financing receivable, (iv) impaired financing receivables by class. Additional disclosures required by the Update include (i) credit quality indicators by class of financing receivable, (ii) the aging of past due financing receivables by class of financing receivable, (iii) the nature and extent of troubled debt restructuring that occurred during the reporting period and their effect on the allowance for credit losses, (iv) the nature and extent of troubled debt restructurings within the previous 12 months that defaulted during the reporting period, by class of financing receivable and their impact on the allowance for credit loss, (v) significant purchases and sales of financing receivables during the reporting period disaggregated by portfolio segment. The Update was effective for the Company as of December 31, 2010, as it relates to disclosures required at the end of a reporting period. Disclosures that relate to activity during a reporting period will be required for fiscal years that begin on or after January 1, 2011. Please see Note 4—Allowance for Probable Loan Losses.

In December 2010, the Financial Accounting Standards Board issued Accounting Standards Update No. 2010-28, to ASC 350, "Intangibles—Goodwill and Other." The Update modifies Step 1 of the goodwill impairment test for reporting units that have zero or negative carrying amounts. For those reporting units, an entity is required to perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. The qualitative factors that should be evaluated in making the more likely than not determination are consistent with existing guidance in ASC 350. The Update will be effective for the Company for interim and fiscal years beginning after December 15, 2011. The adoption of the update to existing standards is not expected to have a significant impact to the Company's consolidated financial statements.

**(2) Investment Securities**

The amortized cost and estimated fair value by type of investment security at December 31, 2010 are as follows:

| | Held to Maturity | | | | |
|---|---|---|---|---|---|
| | Amortized cost | Gross unrealized gains | Gross unrealized losses | Estimated fair value | Carrying value |
| | (Dollars in Thousands) | | | | |
| Other securities | $2,450 | $— | $— | $2,450 | $2,450 |
| Total investment securities | $2,450 | $— | $— | $2,450 | $2,450 |

**(2) Investment Securities (Continued)**

| | Available for Sale | | | | |
|---|---|---|---|---|---|
| | Amortized cost | Gross unrealized gains | Gross unrealized losses | Estimated fair value | Carrying value(1) |
| | (Dollars in Thousands) | | | | |
| U.S. Treasury securities | $ 1,327 | $ — | $ — | $ 1,327 | $ 1,327 |
| Residential mortgage-backed securities | 4,876,573 | 77,741 | (29,846) | 4,924,468 | 4,924,468 |
| Obligations of states and political subdivisions | 150,122 | 636 | (4,761) | 145,997 | 145,997 |
| Equity securities | 13,825 | 864 | (24) | 14,665 | 14,665 |
| Total investment securities | $5,041,847 | $79,241 | $(34,631) | $5,086,457 | $5,086,457 |

(1) Included in the carrying value of residential mortgage-backed securities are $2,326,378 of mortgage-backed securities issued by Ginnie Mae, $2,552,062 of mortgage-backed securities issued by Fannie Mae and Freddie Mac and $46,028 issued by non-government entities

The amortized cost and estimated fair value of investment securities at December 31, 2010, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to prepay obligations with or without prepayment penalties.

| | Held to Maturity | | Available for Sale | |
|---|---|---|---|---|
| | Amortized Cost | Estimated fair value | Amortized Cost | Estimated fair value |
| | (Dollars in Thousands) | | | |
| Due in one year or less | $ 125 | $ 125 | $ 1,327 | $ 1,327 |
| Due after one year through five years | 2,325 | 2,325 | 233 | 242 |
| Due after five years through ten years | — | — | 4,642 | 4,697 |
| Due after ten years | — | — | 145,247 | 141,058 |
| Residential mortgage-backed securities | — | — | 4,876,573 | 4,924,468 |
| Equity securities | — | — | 13,825 | 14,665 |
| Total investment securities | $2,450 | $2,450 | $5,041,847 | $5,086,457 |

The amortized cost and estimated fair value by type of investment security at December 31, 2009 are as follows:

| | Held to Maturity | | | | |
|---|---|---|---|---|---|
| | Amortized cost | Gross unrealized gains | Gross unrealized losses | Estimated fair value | Carrying value |
| | (Dollars in Thousands) | | | | |
| Other securities | $2,450 | $— | $— | $2,450 | $2,450 |
| Total investment securities | $2,450 | $— | $— | $2,450 | $2,450 |

**(2) Investment Securities (Continued)**

| | Available for Sale | | | | |
|---|---|---|---|---|---|
| | Amortized cost | Gross unrealized gains | Gross unrealized losses | Estimated fair value | Carrying value(1) |
| | (Dollars in Thousands) | | | | |
| U.S. Treasury securities | $ 1,327 | $ — | $ — | $ 1,327 | $ 1,327 |
| Residential mortgage-backed securities | 4,393,731 | 113,138 | (15,105) | 4,491,764 | 4,491,764 |
| Obligations of states and political subdivisions | 132,968 | 4,102 | (204) | 136,866 | 136,866 |
| Equity securities | 13,825 | 343 | (42) | 14,126 | 14,126 |
| Total investment securities | $4,541,851 | $117,583 | $(15,351) | $4,644,083 | $4,644,083 |

(1) Included in the carrying value of residential mortgage-backed securities are $1,898,905 of mortgage-backed securities issued by Ginnie Mae, $2,533,290 of mortgage-backed securities issued by Fannie Mae and Freddie Mac and $59,569 issued by non-government entities

Residential mortgage-backed securities are securities issued by the Freddie Mac, Fannie Mae, Ginnie Mae or non-government entities. Investments in residential mortgage-backed securities issued by Ginnie Mae are fully guaranteed by the U.S. Government. Investments in mortgage-backed securities issued by Freddie Mac and Fannie Mae are not fully guaranteed by the U.S. Government, however, the Company believes that the quality of the bonds is similar to other AAA rated bonds with limited credit risk, particularly given the placement of Fannie Mae and Freddie Mac into conservatorship by the federal government in early September 2008.

The amortized cost and fair value of available for sale investment securities pledged to qualify for fiduciary powers, to secure public monies as required by law, repurchase agreements and short-term fixed borrowings was $2,524,130,000 and $2,567,965,000, respectively, at December 31, 2010.

Proceeds from the sale and call of securities available-for-sale were $1,149,021,000, $579,099,000 and $8,376,000 during 2010, 2009 and 2008, respectively, which amounts included $1,133,610,000, $544,305,000 and $0 of mortgage-backed securities. Gross gains of $33,223,000, $11,980,000 and $6,427,000 and gross losses of $14,000, $24,000 and $0 were realized on the sales in 2010, 2009 and 2008, respectively.

**(2) Investment Securities (Continued)**

Gross unrealized losses on investment securities and the fair value of the related securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2010 were as follows:

| | Less than 12 months | | 12 months or more | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| | | | (Dollars in Thousands) | | | |
| Available for sale: | | | | | | |
| Residential mortgage-backed securities | $1,166,720 | $(19,192) | $46,028 | $(10,654) | $1,212,748 | $(29,846) |
| Obligations of states and political subdivisions | 97,701 | (4,666) | 355 | (95) | 98,056 | (4,761) |
| Equity securities | 4,988 | (12) | 63 | (12) | 5,051 | (24) |
| | $1,269,409 | $(23,870) | $46,446 | $(10,761) | $1,315,855 | $(34,631) |

Gross unrealized losses on investment securities and the fair value of the related securities, aggregated by investment category and length of time that individual securities have been in a continuous loss position, at December 31, 2009 were as follows:

| | Less than 12 months | | 12 months or more | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses | Fair Value | Unrealized Losses |
| | | | (Dollars in Thousands) | | | |
| Available for sale: | | | | | | |
| Residential mortgage-backed securities | $16,581 | $ (37) | $59,879 | $(15,068) | $76,460 | $(15,105) |
| Obligations of states and political subdivisions | 14,910 | (201) | 275 | (3) | 15,185 | (204) |
| Equity securities | — | — | 33 | (42) | 33 | (42) |
| | $31,491 | $(238) | $60,187 | $(15,113) | $91,678 | $(15,351) |

The unrealized losses on investments in residential mortgage-backed securities are primarily caused by changes in market interest rates. Residential mortgage-backed securities are primarily securities issued by the Freddie Mac, Fannie Mae and Ginnie Mae. The contractual cash obligations of the securities issued by Ginnie Mae are fully guaranteed by the U.S. Government. The contractual cash obligations of the securities issued by Freddie Mac and Fannie Mae are not fully guaranteed by the U.S. Government, however, the Company believes that the quality of the bonds is similar to other AAA rated bonds with limited credit risk, particularly given the placement of Fannie Mae and Freddie Mac into conservatorship by the federal government in early September 2008. The decrease in fair value on residential mortgage-backed securities issued by Freddie Mac, Fannie Mae and Ginnie Mae is due to market interest rates. The Company has no intent to sell and will more than likely not be required to sell before a market price recovery or maturity of the securities; therefore, it is the conclusion of the Company that the investments in residential mortgage-backed securities issued by Freddie Mac, Fannie Mae and Ginnie Mae are not considered other-than-temporarily impaired. In addition, the Company has a small investment in non-agency residential mortgage-backed securities that have strong credit backgrounds and include additional credit enhancements to protect the Company from losses arising from high foreclosure rates.

**(2) Investment Securities (Continued)**

These securities have additional market volatility beyond economically induced interest rate events. It is the conclusion of the Company that the investments in non-agency residential mortgage-backed securities are other-than-temporarily impaired due to both credit and other than credit issues. An impairment charge of $8,416,000 ($5,470,000, after tax), was recorded in 2010 on the non-agency residential mortgage backed securities. The impairment charge represents the credit related impairment on the securities.

The unrealized losses on investments in other securities are caused by fluctuations in market interest rates. The underlying cash obligations of the securities are guaranteed by the entity underwriting the debt instrument. It is the belief of the Company that the entity issuing the debt will honor its interest payment schedule, as well as the full debt at maturity. The securities are purchased by the Company for their economic value. The decrease in fair value is primarily due to market interest rates and not other factors, and because the Company has no intent to sell and will more than likely not be required to sell before a market price recovery or maturity of the securities, it is the conclusion of the Company that the investments are not considered other-than-temporarily impaired.

The following table presents a reconciliation of credit-related impairment charges on available-for-sale investments recognized in earnings for the twelve months ended December 31, 2010 (in Thousands):

| | |
|---|---|
| Balance at December 31, 2009 | $ — |
| Impairment charges recognized during period | 8,416 |
| Balance at December 31, 2010 | $8,416 |

**(3) Loans**

A summary of net loans, by loan type at December 31, 2010 and 2009 is as follows:

| | December 31, | |
|---|---|---|
| | 2010 | 2009 |
| | (Dollars in thousands) | |
| Commercial, financial and agricultural | $2,615,878 | $2,703,379 |
| Real estate—mortgage | 948,982 | 954,010 |
| Real estate—construction | 1,473,471 | 1,583,057 |
| Consumer | 126,047 | 146,331 |
| Foreign | 245,625 | 280,485 |
| Total loans | $5,410,003 | $5,667,262 |

**(4) Allowance for Probable Loan Losses**

The allowance for probable loan losses consists of the aggregate loan loss allowances of the bank subsidiaries. The allowances are established through charges to operations in the form of provisions for probable loan losses. Loan losses or recoveries are charged or credited directly to the allowances. The allowance for probable loan losses of each bank subsidiary is maintained at a level considered appropriate by management, based on estimated probable losses in the loan portfolio. The allowance for probable loan losses is derived from the following elements: (i) allowances established on specific loans, which are based on a review of the individual characteristics of each loan, including the customer's ability to repay the loan, the underlying collateral values, and the industry the customer operates in (ii) allowances based on actual

**(4) Allowance for Probable Loan Losses (Continued)**

historical loss experience for similar types of loans in the Company's loan portfolio and (iii) allowances based on general economic conditions, changes in the mix of loans, company resources, border risk and credit quality indicators, among other things. All segments of the loan portfolio continue to be impacted by the prolonged economic downturn. Loans secured by real estate could be impacted negatively by the continued economic environment and resulting decrease in collateral values. Consumer loans may be impacted by continued and prolonged unemployment rates.

The Company's management continually reviews the allowance for loan loss of the bank subsidiaries using the amounts determined from the allowances established on specific loans, allowance established on quantitative historical percentages, allowance based on qualitative data, and the loans charged off and recoveries to establish an appropriate amount to maintain in the Company's allowance for loan loss. If the basis of the Company's assumptions change, the allowance for loan loss would either decrease or increase and the Company would increase or decrease the provision for loan loss charged to operations accordingly. While the calculation of the allowance for probable loan losses utilizes management's best judgment and all information available, the adequacy of the allowance is dependent on a variety of factors beyond the Company's control, including, among other things, the performance of the entire loan portfolio, the economy, changes in interest rates and the view of regulatory authorities towards loan classifications.

The specific loan loss provision is determined using the following methods. On a weekly basis, loan past due reports are reviewed by the servicing loan officer to determine if a loan has any potential problem and if a loan should be placed on the Company's internal classified report. Additionally, the Company's credit department reviews the majority of the Company's loans regardless of whether they are past due and segregates any loans with potential problems for further review. The credit department will discuss the potential problem loans with the servicing loan officers to determine any relevant issues that were not discovered in the evaluation. Also, any analysis on loans that is provided through examinations by regulatory authorities is considered in the review process. After the above analysis is completed, the Company will determine if a loan should be placed on an internal classified report because of issues related to the analysis of the credit, credit documents, collateral and/or payment history.

A summary of the transactions in the allowance for probable loan losses for the years ended December 31, 2010, 2009 and 2008 is as follows:

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| | (Dollars in Thousands) | | |
| Balance at January 1, | $ 95,393 | $ 73,461 | $61,726 |
| Losses charged to allowance | (35,240) | (38,539) | (9,134) |
| Recoveries credited to allowance | 1,517 | 1,638 | 1,056 |
| Net losses charged to allowance | (33,723) | (36,901) | (8,078) |
| Provision charged to operations | 22,812 | 58,833 | 19,813 |
| Balance at December 31, | $ 84,482 | $ 95,393 | $73,461 |

The allowance for probable loan losses is a reserve established through a provision for probable loan losses charged to expense, which represents management's best estimate of probable loan losses when evaluating loans (i) individually or (ii) collectively. The Company's provision for probable loan losses decreased from December 31, 2010 to December 31, 2009 mainly due to the decrease in the required reserves for impaired loans analyzed on an individual basis. The impaired loans have been measured based on the fair value of collateral. The majority of these loans show a fair value greater than the carrying value.

**(4) Allowance for Probable Loan Losses (Continued)**

The Company's provision for probable loan losses increased for the years ended December 31, 2009 and 2008, prompted by the analysis of management regarding the weakness in the overall economy and the impact of that weakness on the Company's loan portfolio and the related allowance for probable loan losses. While the Texas and Oklahoma economies are performing better and appear to be recovering faster than other parts of the country, Texas and Oklahoma are not completely immune to the problems associated with the U.S. economy.

The table below provides additional information on the balance of loans individually or collectively evaluated for impairment and their related allowance by loan class as of December 31, 2010:

| | 2010 | | | |
|---|---|---|---|---|
| | Loans individually evaluated for impairment | | Loans collectively evaluated for impairment | |
| | Recorded Investment | Allowance | Recorded Investment | Allowance |
| | (Dollars in Thousands) | | | |
| Domestic | | | | |
| Commercial | $ 23,426 | $ 8,138 | $ 807,098 | $13,908 |
| Commercial real estate: other construction & land development | 77,207 | 592 | 1,396,264 | 26,103 |
| Commercial real estate: farmland & commercial | 21,844 | 3,441 | 1,666,719 | 12,899 |
| Commercial real estate: multifamily | 473 | — | 96,318 | 53 |
| Residential: first lien | 2,015 | — | 531,440 | 10,059 |
| Residential: junior lien | 199 | — | 415,328 | 2,611 |
| Consumer | 29 | — | 126,018 | 6,241 |
| Foreign | 7 | — | 245,618 | 437 |
| Total | $125,200 | $12,171 | $5,284,803 | $72,311 |

Loans accounted for on a non-accrual basis at December 31, 2010, 2009 and 2008 amounted to $108,030,000, $68,338,000 and $164,230,000, respectively. The effect of such non-accrual loans reduced interest income by $3,750,000, $4,011,000 and $6,242,000 for the years ended December 31, 2010, 2009 and 2008, respectively. Amounts received on non-accruals are applied, for financial accounting purposes, first to principal and then to interest after all principal has been collected. Accruing loans contractually past due 90 days or more as to principal or interest payments at December 31, 2010, 2009 and 2008 amounted to $19,848,000, $12,089,000 and $6,274,000, respectively.

**(4) Allowance for Probable Loan Losses (Continued)**

The table below provides additional information on loans accounted for on a non-accrual basis by loan class at December 31, 2010:

| | 2010 |
|---|---|
| | (Dollars in Thousands) |
| Domestic | |
| Commercial | $ 22,614 |
| Commercial real estate: other construction & land development | 77,207 |
| Commercial real estate: farmland & commercial | 5,486 |
| Commercial real estate: multifamily | 473 |
| Residential: first lien | 2,015 |
| Residential: junior lien | 199 |
| Consumer | 29 |
| Foreign | 7 |
| Total non-accrual loans | $108,030 |

Impaired loans are those loans where it is probable that all amounts due according to contractual terms of the loan agreement will not be collected. The Company has identified these loans through its normal loan review procedures. Impaired loans are measured based on (1) the present value of expected future cash flows discounted at the loan's effective interest rate; (2) the loan's observable market price; or (3) the fair value of the collateral if the loan is collateral dependent. Substantially all of the Company's impaired loans are measured at the fair value of the collateral. In limited cases the Company may use other methods to determine the level of impairment of a loan if such loan is not collateral dependent.

The following tables detail key information regarding the Company's impaired loans by loan class for the year ended December 31, 2010:

| | December 31, 2010 | | | | |
|---|---|---|---|---|---|
| | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Recorded Investment | Interest Recognized |
| | (Dollars in Thousands) | | | | |
| Loans with Related Allowance | | | | | |
| Domestic | | | | | |
| Commercial | $23,062 | $23,071 | $ 8,138 | $23,096 | $ 42 |
| Commercial real estate: other construction & land development | 10,603 | 10,645 | 592 | 10,622 | — |
| Commercial real estate: farmland & commercial | 17,841 | 17,878 | 3,441 | 18,475 | 860 |
| Total impaired loans with related allowance | $51,506 | $51,594 | $12,171 | $52,193 | $902 |

**(4) Allowance for Probable Loan Losses (Continued)**

| | December 31, 2010 | | | |
|---|---|---|---|---|
| | Recorded Investment | Unpaid Principal Balance | Average Recorded Investment | Interest Recognized |
| | (Dollars in Thousands) | | | |
| Loans with No Related Allowance | | | | |
| Domestic | | | | |
| Commercial | $ 364 | $ 980 | $ 993 | $30 |
| Commercial real estate: other construction & land development | 66,604 | 66,755 | 68,608 | 2 |
| Commercial real estate: farmland & commercial | 4,003 | 5,606 | 5,594 | — |
| Commercial real estate: multifamily | 473 | 473 | 500 | — |
| Residential: first lien | 2,015 | 2,143 | 2,297 | — |
| Residential: junior lien | 199 | 226 | 228 | — |
| Consumer | 29 | 46 | 49 | — |
| Foreign | 7 | 7 | 19 | — |
| Total impaired loans with no related allowance | $73,694 | $76,236 | $78,288 | $32 |

The following table details key information regarding the Company's impaired loans for the years ended December 31, 2009 and 2008:

| | 2009 | 2008 |
|---|---|---|
| | (Dollars in Thousands) | |
| Balance of impaired loans where there is a related allowance for loan loss | $106,780 | $137,153 |
| Balance of impaired loans where there is no related allowance for loan loss | 11,494 | 27,786 |
| Total impaired loans | $118,274 | $164,939 |
| Allowance allocated to impaired loans | $ 30,555 | $ 20,671 |

The impaired loans included in the table above were primarily comprised of collateral dependent commercial loans, which have not been fully charged off. The average recorded investment in impaired loans was $130,481,000, $149,528,000, and $93,654,000 for the years ended December 31, 2010, 2009 and 2008, respectively. Interest income recorded on impaired loans was $934,000, $547,000 and $236,000 for the years ended December 31, 2010, 2009 and 2008. The increase in the balance of impaired loans over historical levels can be partially attributed to certain loans that filed for bankruptcy protection and a few loan relationships that deteriorated during 2009 and 2008. A portion of the impaired loans have adequate collateral and credit enhancements not requiring a related allowance for loan loss. The level of impaired loans is reflective of the economic weakness that has been created by the financial crisis and the subsequent economic downturn. Management is confident the Company's loss exposure regarding these credits will be significantly reduced due to the Company's long-standing practices that emphasize secured lending with strong collateral positions and guarantor support. Management is likewise confident the reserve for probable loan losses is adequate. The Company has no direct exposure to sub-prime loans in its loan portfolio, but the sub-prime crisis has affected the credit markets on a national level, and as a result, the Company has experienced an increasing amount of impaired loans; however, management's decision to place loans in this category does not necessarily mean that the Company will experience significant losses from these loans or significant increases in impaired loans from these levels.

**(4) Allowance for Probable Loan Losses (Continued)**

Management of the Company recognizes the risks associated with these impaired loans. However, management's decision to place loans in this category does not necessarily mean that losses will occur. In the current environment, troubled loan management can be protracted because of the legal and process problems that delay the collection of an otherwise collectable loan. Additionally, management believes that the collateral related to these impaired loans and/or the secondary support from guarantors mitigates the potential for losses from impaired loans. It is also important to note that even though the economic conditions in Texas and Oklahoma are weakened, we believe these markets are improving and better positioned to recover than many other areas of the country.

The bank subsidiaries charge off that portion of any loan which management considers to represent a loss as well as that portion of any other loan which is classified as a "loss" by bank examiners. Commercial and industrial or real estate loans are generally considered by management to represent a loss, in whole or part, when an exposure beyond any collateral coverage is apparent and when no further collection of the loss portion is anticipated based on the borrower's financial condition and general economic conditions in the borrower's industry. Generally, unsecured consumer loans are charged-off when 90 days past due.

The following table presents information regarding the aging of past due loans by loan class:

| | December 31, 2010 | | | | | | |
|---|---|---|---|---|---|---|---|
| | 30-59 Days | 60-89 Days | 90 Days or Greater | 90 Days or greater & still accruing | Total Past due | Current | Total Portfolio |
| | (Dollars in Thousands) | | | | | | |
| Domestic | | | | | | | |
| Commercial | $ 3,734 | $ 861 | $23,239 | $ 1,029 | $ 27,834 | $ 802,690 | $ 830,524 |
| Commercial real estate: other construction & land development | 2,685 | 2,896 | 50,618 | 11,507 | 56,199 | 1,417,272 | 1,473,471 |
| Commercial real estate: farmland & commercial | 3,077 | 817 | 6,600 | 1,585 | 10,494 | 1,678,069 | 1,688,563 |
| Commercial real estate: multifamily | 73 | 185 | 473 | — | 731 | 96,060 | 96,791 |
| Residential: first lien | 4,884 | 3,436 | 5,136 | 3,472 | 13,456 | 519,999 | 533,455 |
| Residential: junior lien | 703 | 272 | 457 | 277 | 1,432 | 414,095 | 415,527 |
| Consumer | 1,518 | 587 | 1,505 | 1,477 | 3,610 | 122,437 | 126,047 |
| Foreign | 196 | 380 | 501 | 501 | 1,077 | 244,548 | 245,625 |
| Total past due loans | $16,870 | $9,434 | $88,529 | $19,848 | $114,833 | $5,295,170 | $5,410,003 |

The Company's internal classified report is segregated into the following categories: (i) "Special Review Credits," (ii) "Watch List—Pass Credits," or (iii) "Watch List—Substandard Credits." The loans placed in the "Special Review Credits" category reflect the Company's opinion that the loans reflect potential weakness which require monitoring on a more frequent basis. The "Special Review Credits" are reviewed and discussed on a regular basis with the credit department and the lending staff to determine if a change in category is warranted. The loans placed in the "Watch List—Pass Credits" category reflect the Company's opinion that the credit contains weaknesses which represent a greater degree of risk, which warrant "extra attention." The "Watch List—Pass Credits" are reviewed and discussed on a regular basis with the credit department and the lending staff to determine if a change in category is warranted. The

**(4) Allowance for Probable Loan Losses (Continued)**

loans placed in the "Watch List—Substandard Credits" classification are considered to be potentially inadequately protected by the current sound worth and debt service capacity of the borrower or of any pledged collateral. These credit obligations, even if apparently protected by collateral value, have shown defined weaknesses related to adverse financial, managerial, economic, market or political conditions which may jeopardize repayment of principal and interest. Furthermore, there is the possibility that some future loss could be sustained by the bank if such weaknesses are not corrected. For loans that are classified as impaired, management evaluates these credits under Statement of Financial Accounting Standards No. 114, "Accounting by Creditors for Impairment of a Loan," now included as part of ASC 310-10, "Receivables," criteria and, if deemed necessary, a specific reserve is allocated to the credit. The specific reserve allocated under ASC 310-10, is based on (1) the present value of expected future cash flows discounted at the loan's effective interest rate; (2) the loan's observable market price; or (3) the fair value of the collateral if the loan is collateral dependent. Substantially all of the Company's loans evaluated as impaired under ASC 310-10 are measured using the fair value of collateral method. In limited cases, the Company may use other methods to determine the specific reserve of a loan under SFAS ASC 310-10 if such loan is not collateral dependent.

The allowance based on historical loss experience on the Company's remaining loan portfolio, which includes the "Special Review Credits," "Watch List—Pass Credits," and "Watch List—Substandard Credits" is determined by segregating the remaining loan portfolio into certain categories such as commercial loans, installment loans, international loans, loan concentrations and overdrafts. Installment loans are then further segregated by number of days past due. A historical loss percentage, adjusted for (i) management's evaluation of changes in lending policies and procedures, (ii) current economic conditions in the market area served by the Company, (iii) other risk factors, (iv) the effectiveness of the internal loan review function, (v) changes in loan portfolios, and (vi) the composition and concentration of credit volume is applied to each category. Each category is then added together to determine the allowance allocated under ASC 450-20.

**(4) Allowance for Probable Loan Losses (Continued)**

A summary of the loan portfolio by credit quality indicator by loan class is as follows:

| | December 31, 2010 | | | | |
|---|---|---|---|---|---|
| | Pass | Special Review | Watch List—Pass | Watch List—Substandard | Watch List—Impaired |
| | (Dollars in Thousands) | | | | |
| Domestic | | | | | |
| Commercial | $ 741,006 | $ 14,015 | $ 7,187 | $ 44,890 | $ 23,426 |
| Commercial real estate: other construction & land development | 1,100,430 | 117,058 | 53,770 | 125,006 | 77,207 |
| Commercial real estate: farmland & commercial | 1,521,243 | 42,353 | 29,936 | 73,187 | 21,844 |
| Commercial real estate: multifamily | 94,973 | 1,345 | — | — | 473 |
| Residential: first lien | 526,504 | 2,237 | 1,747 | 952 | 2,015 |
| Residential: junior lien | 415,021 | — | — | 307 | 199 |
| Consumer | 125,973 | 3 | — | 42 | 29 |
| Foreign | 234,979 | 10,108 | — | 531 | 7 |
| Total | $4,760,129 | $187,119 | $92,640 | $244,915 | $125,200 |

**(5) Bank Premises and Equipment**

A summary of bank premises and equipment, by asset classification, at December 31, 2010 and 2009 were as follows:

| | Estimated useful lives | 2010 | 2009 |
|---|---|---|---|
| | | (Dollars in Thousands) | |
| Bank buildings and improvements | 5 - 40 years | $ 388,847 | $ 384,760 |
| Furniture, equipment and vehicles | 1 - 20 years | 268,590 | 265,425 |
| Land | | 123,988 | 124,012 |
| Real estate held for future expansion: | | | |
| Land, building, furniture, fixture and equipment | 7 - 27 years | 664 | 715 |
| Less: accumulated depreciation | | (313,139) | (284,537) |
| Bank premises and equipment, net | | $ 468,950 | $ 490,375 |

**(6) Goodwill and Other Intangible Assets**

The majority of the Company's identified intangibles are in the form of amortizable core deposit premium, with the exception of $1,217,000, which represents identified intangibles in the acquisition of the

**(6) Goodwill and Other Intangible Assets (Continued)**

rights to the insurance agency contracts of InsCorp, Inc., acquired in 2008. Information on the Company's identified intangible assets follows:

| | Carrying Amount | Accumulated Amortization | Net |
|---|---|---|---|
| | (Dollars in Thousands) | | |
| **December 31, 2010:** | | | |
| Core deposit premium | $58,675 | $42,583 | $16,092 |
| Identified intangible (contract rights) | 1,568 | 351 | 1,217 |
| Total identified intangibles | $60,243 | $42,934 | $17,309 |
| **December 31, 2009:** | | | |
| Core deposit premium | $58,675 | $37,496 | $21,179 |
| Identified intangible (contract rights) | 1,333 | 154 | 1,179 |
| Total identified intangibles | $60,008 | $37,650 | $22,358 |

Amortization expense of intangible assets for the years ended December 31, 2010, 2009 and 2008, was $5,284,000, $5,286,000 and $5,195,000, respectively. Estimated amortization expense for each of the five succeeding fiscal years, and thereafter, is as follows:

| Fiscal year ending: | Total |
|---|---|
| | (in thousands) |
| 2011 | $ 5,292 |
| 2012 | 4,586 |
| 2013 | 4,567 |
| 2014 | 2,324 |
| 2015 | 387 |
| Thereafter | 153 |
| Total | $17,309 |

There were no changes in the carrying amount of goodwill for the years ended December 31, 2010 and 2009.

## (7) Deposits

Deposits as of December 31, 2010 and 2009 and related interest expense for the years ended December 31, 2010, 2009 and 2008 were as follows:

| | 2010 | 2009 |
|---|---|---|
| | (Dollars in Thousands) | |
| Deposits: | | |
| Demand—non-interest bearing | | |
| Domestic | $1,459,776 | $1,352,745 |
| Foreign | 179,300 | 164,054 |
| Total demand non-interest bearing | 1,639,076 | 1,516,799 |
| Savings and interest bearing demand | | |
| Domestic | 2,058,311 | 1,835,430 |
| Foreign | 464,531 | 427,122 |
| Total savings and interest bearing demand | 2,522,842 | 2,262,552 |
| Time, certificates of deposit | | |
| $100,000 or more | | |
| Domestic | 1,054,649 | 984,171 |
| Foreign | 1,242,524 | 1,257,561 |
| Less than $100,000 | | |
| Domestic | 741,399 | 759,902 |
| Foreign | 399,068 | 397,022 |
| Total time, certificates of deposit | 3,437,640 | 3,398,656 |
| Total deposits | $7,599,558 | $7,178,007 |

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| | (Dollars in Thousands) | | |
| Interest expense: | | | |
| Savings and interest bearing demand | | | |
| Domestic | $ 7,771 | $ 9,267 | $ 23,197 |
| Foreign | 1,612 | 1,565 | 3,454 |
| Total savings and interest bearing demand | 9,383 | 10,832 | 26,651 |
| Time, certificates of deposit | | | |
| $100,000 or more | | | |
| Domestic | 14,839 | 18,091 | 28,990 |
| Foreign | 17,084 | 23,315 | 41,383 |
| Less than $100,000 | | | |
| Domestic | 11,416 | 15,600 | 26,297 |
| Foreign | 3,628 | 5,249 | 9,809 |
| Total time, certificates of deposit | 46,967 | 62,255 | 106,479 |
| Total interest expense on deposits | $56,350 | $73,087 | $133,130 |

**(7) Deposits (Continued)**

Scheduled maturities of time deposits as of December 31, 2010 were as follows:

| | Total |
|---|---|
| | (in thousands) |
| 2011 | $3,087,213 |
| 2012 | 231,534 |
| 2013 | 67,950 |
| 2014 | 46,980 |
| 2015 | 3,456 |
| Thereafter | 507 |
| Total | $3,437,640 |

Scheduled maturities of time deposits in amounts of $100,000 or more at December 31, 2010, were as follows:

| | |
|---|---|
| Due within 3 months or less | $ 966,224 |
| Due after 3 months and within 6 months | 576,168 |
| Due after 6 months and within 12 months | 544,175 |
| Due after 12 months | 210,606 |
| | $2,297,173 |

**(8) Securities Sold Under Repurchase Agreements**

The Company's bank subsidiaries have entered into repurchase agreements with an investment banking firm and individual customers of the bank subsidiaries. The purchasers have agreed to resell to the bank subsidiaries identical securities upon the maturities of the agreements. Securities sold under repurchase agreements were mortgage-backed book entry securities and averaged $1,479,734,000 and $1,461,839,000 during 2010 and 2009, respectively, and the maximum amount outstanding at any month end during 2010 and 2009 was $1,520,714,000 and $1,500,223,000, respectively.

**(8) Securities Sold Under Repurchase Agreements (Continued)**

Further information related to repurchase agreements at December 31, 2010 and 2009 is set forth in the following table:

| | Collateral Securities | | Repurchase Borrowing | |
|---|---|---|---|---|
| | Book Value of Securities Sold | Fair Value of Securities Sold | Balance of Liability | Weighted Average Interest Rate |
| | (Dollars in Thousands) | | | |
| December 31, 2010 term: | | | | |
| Overnight agreements | $ 432,252 | $ 426,112 | $ 311,333 | .60% |
| 1 to 29 days | 26,714 | 27,177 | 16,308 | 1.15 |
| 30 to 90 days | 44,443 | 45,438 | 30,167 | 1.69 |
| Over 90 days | 1,243,634 | 1,279,248 | 1,075,462 | 3.71 |
| Total | $1,747,043 | $1,777,975 | $1,433,270 | 2.97% |
| December 31, 2009 term: | | | | |
| Overnight agreements | $ 428,543 | $ 440,262 | $ 277,153 | 1.00% |
| 1 to 29 days | 36,576 | 37,773 | 14,420 | 1.78 |
| 30 to 90 days | 61,197 | 62,918 | 39,814 | 1.89 |
| Over 90 days | 1,313,560 | 1,350,490 | 1,110,430 | 3.52 |
| Total | $1,839,876 | $1,891,443 | $1,441,817 | 2.97% |

The book value and fair value of securities sold includes the entire book value and fair value of securities partially or fully pledged under repurchase agreements.

**(9) Other Borrowed Funds**

Other borrowed funds include Federal Home Loan Bank borrowings, which are short and long-term fixed borrowings issued by the Federal Home Loan Bank of Dallas at the market price offered at the time of funding. These borrowings are secured by mortgage-backed investment securities and a portion of the Company's loan portfolio.

**(9) Other Borrowed Funds (Continued)**

Further information regarding the Company's other borrowed funds at December 31, 2010 and 2009 is set forth in the following table:

| | December 31, | |
|---|---|---|
| | 2010 | 2009 |
| | (Dollars in Thousands) | |
| Federal Home Loan Bank advances—short-term | | |
| Balance at year end | $1,020,000 | $1,347,625 |
| Rate on balance outstanding at year end | .18% | .14% |
| Average daily balance | $ 656,365 | $1,662,457 |
| Average rate | .19% | .57% |
| Maximum amount outstanding at any month end | $1,307,875 | $2,620,761 |
| Federal Home Loan Bank advances—long-term | | |
| Balance at year end | $ 6,780 | $ — |
| Rate on balance outstanding at year end | 3.51% | — |
| Average daily balance | $ 93 | $ — |
| Average rate | 3.51% | — |
| Maximum amount outstanding at any month end | $ 6,780 | $ — |

**(10) Junior Subordinated Deferrable Interest Debentures**

The Company has formed eight statutory business trusts under the laws of the State of Delaware, for the purpose of issuing trust preferred securities. The eight statutory business trusts formed by the Company (the "Trusts") have each issued Capital and Common Securities and invested the proceeds thereof in an equivalent amount of junior subordinated debentures (the "Debentures") issued by the Company. As of December 31, 2010 and 2009, the principal amount of debentures outstanding totaled $201,117,000 and $201,082,000, respectively. As a result of the participation in the TARP Capital Purchase Program, the Company may not, without the consent of the Treasury Department, redeem any of the Debentures until the earlier to occur of December 23, 2011, or the date on which the Company has redeemed all of the Series A Preferred Stock issued under the Capital Purchase Program or the date on which the Treasury has transferred all of the Series A Preferred Stock to third parties not affiliated with the Treasury.

The Debentures are subordinated and junior in right of payment to all present and future senior indebtedness (as defined in the respective indentures) of the Company, and are *pari passu* with one another. The interest rate payable on, and the payment terms of the Debentures are the same as the distribution rate and payment terms of the respective issues of Capital and Common Securities issued by the Trusts. The Company has fully and unconditionally guaranteed the obligations of each of the Trusts with respect to the Capital and Common Securities. The Company has the right, unless an Event of Default (as defined in the Indentures) has occurred and is continuing, to defer payment of interest on the Debentures for up to ten consecutive semi-annual periods on Trust I and for up to twenty consecutive quarterly periods on Trusts VI, VII, VIII, IX, X, XI and XII. If interest payments on any of the Debentures are deferred, distributions on both the Capital and Common Securities related to that Debenture would also be deferred. The redemption prior to maturity of any of the Debentures may require the prior approval of the Federal Reserve and/or other regulatory bodies.

**(10) Junior Subordinated Deferrable Interest Debentures (Continued)**

For financial reporting purposes, the Trusts are treated as investments of the Company and not consolidated in the consolidated financial statements. Although the Capital Securities issued by each of the Trusts are not included as a component of shareholders' equity on the consolidated statement of condition, the Capital Securities are treated as capital for regulatory purposes. Specifically, under applicable regulatory guidelines, the Capital Securities issued by the Trusts qualify as Tier 1 capital up to a maximum of 25% of Tier 1 capital on an aggregate basis. Any amount that exceeds the 25% threshold would qualify as Tier 2 capital. At December 31, 2010 and 2009, the total $201,117,000 and $201,082,000 of the Capital Securities outstanding qualified as Tier 1 capital.

In March 2005, the Federal Reserve Board issued a final rule that would continue to allow the inclusion of trust preferred securities in Tier 1 capital, but with stricter quantitative limits. Under the final rule, after a five-year transition period ending March 31, 2009, the aggregate amount of trust preferred securities and certain other capital elements would be limited to 25% of Tier 1 capital elements, net of goodwill, less any associated deferred tax liability. The amount of trust preferred securities and certain other elements in excess of the limit could be included in Supplementary Capital or Tier 2 capital, subject to restrictions. Tier 2 capital includes among other things, perpetual preferred stock, qualifying mandatory convertible debt securities, qualifying subordinated debt, and allowances for probable loan and lease losses, subject to limitations. Bank holding companies with significant international operations will be expected to limit trust preferred securities to 15% of Tier 1 capital elements, net of goodwill; however, they may include qualifying mandatory convertible preferred securities up to the 25% limit. On March 16, 2009, the Federal Reserve Board extended for two years the transition period. The Company believes that substantially all of the trust preferred securities issued by the Company will qualify as Tier 1 capital after the transition period ending on March 31, 2011. The Collins Amendment to the Dodd-Frank Act further restricts the use of trust preferred securities by excluding them from the regulatory capital of banking holding companies more broadly. However, for institutions with consolidated assets of less than $15 billion on December 31, 2009, such as the Company, the Collins Amendment will not apply to securities issued before May 19, 2010 and all the Company's trust preferred securities were issued before such date. Pursuant to this grandfather provision, the Company will be able to continue to treat these securities as Tier 1 capital subject to existing Federal Reserve limitations through the life of the securities.

**(10) Junior Subordinated Deferrable Interest Debentures (Continued)**

The following table illustrates key information about each of the Debentures and their interest rates at December 31, 2010:

| | Junior Subordinated Deferrable Interest Debentures | Repricing Frequency | Interest Rate | Interest Rate Index(1) | Maturity Date | Optional Redemption Date |
|---|---|---|---|---|---|---|
| | (in thousands) | | | | | |
| Trust I | $ 10,391 | Fixed | 10.18% | Fixed | June 2031 | June 2011 |
| Trust VI | $ 25,774 | Quarterly | 3.74% | LIBOR + 3.45 | November 2032 | May 2011 |
| Trust VII | $ 10,310 | Quarterly | 3.54% | LIBOR + 3.25 | April 2033 | April 2011 |
| Trust VIII | $ 25,774 | Quarterly | 3.34% | LIBOR + 3.05 | October 2033 | April 2011 |
| Trust IX | $ 41,238 | Fixed | 7.10% | Fixed | October 2036 | October 2011 |
| Trust X | $ 34,021 | Fixed | 6.66% | Fixed | February 2037 | February 2012 |
| Trust XI | $ 32,990 | Fixed | 6.82% | Fixed | July 2037 | July 2012 |
| Trust XII | $ 20,619 | Fixed | 6.85% | Fixed | September 2037 | September 2012 |
| | $201,117 | | | | | |

(1) Trust IX, X, XI and XII accrue interest at a fixed rate for the first five years, then floating at LIBOR + 1.62%, 1.65%, 1.62% and 1.45% thereafter, respectively.

**(11) Earnings per Share ("EPS")**

Basic EPS is calculated by dividing net income by the weighted average number of common shares outstanding. The computation of diluted EPS assumes the issuance of common shares for all dilutive

**(11) Earnings per Share ("EPS") (Continued)**

potential common shares outstanding during the reporting period. The calculation of the basic EPS and the diluted EPS for the years ended December 31, 2010, 2009, and 2008 is set forth in the following table:

| | Net Income (Numerator) | Shares (Denominator) | Per Share Amount |
|---|---|---|---|
| | (Dollars in Thousands, Except Per Share Amounts) | | |
| December 31, 2010: | | | |
| Basic EPS | | | |
| Net income available to common shareholders | $116,897 | 67,921,353 | $1.72 |
| Potential dilutive common shares | — | 83,088 | |
| Diluted EPS | $116,897 | 68,004,441 | $1.72 |
| December 31, 2009: | | | |
| Basic EPS | | | |
| Net income | $129,758 | 68,373,732 | $1.90 |
| Potential dilutive common shares | — | 20,892 | |
| Diluted EPS | $129,758 | 68,394,624 | $1.90 |
| December 31, 2008: | | | |
| Basic EPS | | | |
| Net income | $132,112 | 68,576,654 | $1.93 |
| Potential dilutive common shares | — | 137,736 | |
| Diluted EPS | $132,112 | 68,714,390 | $1.92 |

**(12) Employees' Profit Sharing Plan**

The Company has a deferred profit sharing plan for full-time employees with a minimum of one year of continuous employment. The Company's annual contribution to the plan is based on a percentage, as determined by the Board of Directors, of income before income taxes, as defined, for the year. Allocation of the contribution among officers and employees' accounts is based on length of service and amount of salary earned. Profit sharing costs of $4,095,000, $4,366,000 and $4,683,000 were charged to income for the years ended December 31, 2010, 2009, and 2008, respectively.

**(13) International Operations**

The Company provides international banking services for its customers through its bank subsidiaries. Neither the Company nor its bank subsidiaries have facilities located outside the United States. International operations are distinguished from domestic operations based upon the domicile of the customer.

Because the resources employed by the Company are common to both international and domestic operations, it is not practical to determine net income generated exclusively from international activities.

**(13) International Operations (Continued)**

A summary of assets attributable to international operations at December 31, 2010 and 2009 are as follows:

| | 2010 | 2009 |
|---|---|---|
| | (Dollars in Thousands) | |
| Loans: | | |
| Commercial | $195,208 | $230,464 |
| Others | 50,417 | 50,021 |
| | 245,625 | 280,485 |
| Less allowance for probable loan losses | (437) | (393) |
| Net loans | $245,188 | $280,092 |
| Accrued interest receivable | $ 1,331 | $ 1,373 |

At December 31, 2010, the Company had $120,201,000 in outstanding standby and commercial letters of credit to facilitate trade activities. The letters of credit are issued primarily in conjunction with credit facilities, which are available to various Mexican banks doing business with the Company.

Revenues directly attributable to international operations were $11,423,000, $13,681,000 and $17,084,000 for the years ended December 31, 2010, 2009 and 2008, respectively.

**(14) Income Taxes**

The Company files a consolidated U.S. Federal and State income tax return. The current and deferred portions of net income tax expense included in the consolidated statements of income are presented below for the years ended December 31:

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| | (Dollars in Thousands) | | |
| Current | | | |
| U.S. | $70,338 | $77,653 | $71,280 |
| State | 4,129 | 3,340 | 2,882 |
| Foreign | 22 | 30 | 51 |
| Total current taxes | 74,489 | 81,023 | 74,213 |
| Deferred | | | |
| U.S. | (3,394) | (8,513) | (6,030) |
| State | (138) | 5,478 | 1,347 |
| Total deferred taxes | (3,532) | (3,035) | (4,683) |
| Total income taxes | $70,957 | $77,988 | $69,530 |

**(14) Income Taxes (Continued)**

Total income tax expense differs from the amount computed by applying the U.S. Federal income tax rate of 35% for 2010, 2009 and 2008 to income before income taxes. The reasons for the differences for the years ended December 31 are as follows:

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| | (Dollars in Thousands) | | |
| Computed expected tax expense | $70,355 | $77,293 | $70,720 |
| Change in taxes resulting from: | | | |
| Tax-exempt interest income | (2,813) | (1,937) | (1,552) |
| State tax, net of federal income taxes and tax credit | 2,594 | 5,722 | 2,834 |
| Tax refunds | (2,143) | — | — |
| Litigation expense | 5,375 | — | — |
| Other investment income | (3,172) | (3,526) | (3,321) |
| Other | 761 | 436 | 849 |
| Actual tax expense | $70,957 | $77,988 | $69,530 |

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at December 31, 2010 and 2009 are reflected below:

| | 2010 | 2009 |
|---|---|---|
| | (Dollars in Thousands) | |
| Deferred tax assets: | | |
| Loans receivable, principally due to the allowance for probable loan losses | $ 34,086 | $ 35,979 |
| Other real estate owned | 323 | 76 |
| Impairment charges on available-for-sale securities | 2,946 | — |
| Accrued expenses | 304 | 170 |
| Other | 6,065 | 4,826 |
| Total deferred tax assets | 43,724 | 41,051 |
| Deferred tax liabilities: | | |
| Lease financing receivable | — | (59) |
| Bank premises and equipment, principally due to differences on depreciation | (24,272) | (24,786) |
| Net unrealized gains on available for sale investment securities | (15,833) | (36,355) |
| Identified intangible assets and goodwill | (18,383) | (17,819) |
| Other | (7,750) | (8,600) |
| Total deferred tax liabilities | (66,238) | (87,619) |
| Net deferred tax liability | $(22,514) | $(46,568) |

The net deferred tax liability of $22,514,000 at December 31, 2010 and $46,568,000 at December 31, 2009 is included in other liabilities in the consolidated statements of condition.

**(14) Income Taxes (Continued)**

State net operating loss carryforwards were fully utilized in 2009. They originally expired beginning in June 2013 and ending in December 2024.

**(15) Stock Options**

On April 1, 2005, the Board of Directors adopted the 2005 International Bancshares Corporation Stock Option Plan (the "2005 Plan"). Effective May 19, 2008, the 2005 Plan was amended to increase the number of shares available for stock option grants under the 2005 Plan by 300,000 shares. The 2005 Plan replaced the 1996 International Bancshares Corporation Key Contributor Stock Option Plan (the "1996 Plan"). Under the 2005 Plan, both qualified incentive stock options ("ISOs") and non-qualified stock options ("NQSOs") may be granted. Options granted may be exercisable for a period of up to 10 years from the date of grant, excluding ISOs granted to 10% shareholders, which may be exercisable for a period of up to only five years. As of December 31, 2010, 193,197 shares were available for future grants under the 2005 Plan.

The fair value of each option award granted under the plan is estimated on the date of grant using a Black-Scholes-Merton option valuation model that uses the assumptions noted in the following table. Expected volatility is based on the historical volatility of the price of the Company's stock. The Company uses historical data to estimate the expected dividend yield and employee termination rates within the valuation model. The expected term of options is derived from historical exercise behavior. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant. No options were granted for the year ended December 31, 2010.

| | 2009 | 2008 |
|---|---|---|
| Expected Life (Years) | 6.13 | 6.13 |
| Dividend yield | 2.99% | 2.75% |
| Interest rate | 2.12% | 1.44% |
| Volatility | 41.81% | 31.08% |

A summary of option activity under the stock option plans for the twelve months ended December 31, 2010 is as follows:

| | Number of options | Weighted average exercise price | Weighted average remaining contractual term (years) | Aggregate intrinsic value ($) |
|---|---|---|---|---|
| Options outstanding at December 31, 2009 | 823,592 | $20.54 | | |
| Plus: Options granted | — | — | | |
| Less: | | | | |
| Options exercised | 174 | 10.40 | | |
| Options expired | — | — | | |
| Options forfeited | 58,436 | 19.09 | | |
| Options outstanding at December 31, 2010 | 764,982 | $20.65 | 3.81 | $2,154,000 |
| Options fully vested and exercisable at December 31, 2010 | 387,438 | $24.19 | 2.43 | $ 143,000 |

**(15) Stock Options (Continued)**

Stock-based compensation expense included in the consolidated statements of income for the twelve months ended December 31, 2010, 2009 and 2008 was approximately $534,000, $655,000 and $692,000, respectively. As of December 31, 2010, there was approximately $655,000 of total unrecognized stock-based compensation cost related to non-vested options granted under the Company plans that will be recognized over a weighted average period of 1.4 years.

A summary of the status of the Company's non-vested options as of December 31, 2010, and changes during the twelve months ended December 31, 2010, is presented below:

| Non-vested Options | Options | Weighted average grant-date fair value ($) |
|---|---|---|
| Non-vested options at December 31, 2009 | 519,177 | $4.80 |
| Granted | — | — |
| Vested | 91,358 | 6.03 |
| Forfeited | 50,275 | 4.93 |
| Non-vested options at December 31, 2010 | 377,544 | $4.48 |

Other information pertaining to option activity during the twelve month period ending December 31, 2010, 2009 and 2008 is as follows:

| | Twelve Months Ended December 31, | | |
|---|---|---|---|
| | 2010 | 2009 | 2008 |
| Weighted average grant date fair value of stock options granted | $ — | $ 3.31 | $ 4.90 |
| Total fair value of stock options vested | $551,000 | $522,000 | $624,000 |
| Total intrinsic value of stock options exercised | $ 2,000 | $581,000 | $591,000 |

**(16) Long Term Restricted Stock Units**

As a participant in the Troubled Asset Relief Program Capital Purchase Program (the "CPP"), the Company must comply with the Interim Final Rule on TARP Standards for Compensation and Corporate Governance issued in June 2009 by the Treasury, which implements the provisions of Section 111 of the Emergency Economic Stabilization Act of 2008, as amended by the American Recovery and Reinvestment Act of 2009. Pursuant to these provisions, the Company is subject to certain compensation restrictions, which include a prohibition on the payment or accrual of any bonuses (including equity-based incentive compensation) to certain officers and employees except for awards of CPP-compliant long-term restricted stock and stock units.

On December 18, 2009, the Company's board of directors (the "Board") adopted the 2009 International Bancshares Corporation Long-Term Restricted Stock Unit Plan (the "Plan") to give the Company additional flexibility in the compensation of its officers, employees, consultants and advisors in compliance with all applicable laws and restrictions.

The Plan authorizes the Company to issue Restricted Stock Units ("RSUs") to officers, employees, consultants and advisors of the Company and its subsidiaries. The Plan provides that RSUs shall be issued

**(16) Long Term Restricted Stock Units (Continued)**

by a committee of the Board appointed by the Board from time to time consisting of at least two (2) members of the Board, each of whom is both a non-employee director and an outside director. On December 18, 2009, the Board adopted resolutions creating the Long-Term Restricted Stock Unit Plan Committee to administer the Plan. RSUs issued under the Plan are not equity and are payable only in cash. The Plan provides for both the issuance of CPP-compliant long-term RSUs as well as RSUs that are not CPP-compliant.

Dennis E. Nixon, the Company's President, Chairman of the Board and a director of the Company, received an award of CPP-compliant RSUs, granted as of December 15, 2010, in the amount of $400,000 for his performance in 2010. Mr. Nixon was also awarded CPP-compliant RSU's granted as of December 18, 2009, in the amount of $250,000 for his performance during 2009. In order to meet the requirements of a CPP-compliant RSU, Mr. Nixon's RSUs do not exceed one-third of his total annual compensation.

**(17) Commitments, Contingent Liabilities and Other Tax Matters**

The Company leases portions of its banking premises and equipment under operating leases. Total rental expense for the years ended December 31, 2010, 2009 and 2008 were $12,800,000, $12,600,000 and $11,700,000, respectively. Future minimum lease payments due under non-cancellable operating leases at December 31, 2010 were as follows:

| Fiscal year ending: | Total (in thousands) |
|---|---|
| 2011 | $ 9,472 |
| 2012 | 6,280 |
| 2013 | 4,306 |
| 2014 | 2,759 |
| 2015 | 1,629 |
| Thereafter | 3,881 |
| Total | $28,327 |

It is expected that certain leases will be renewed, as these leases expire. Aggregate future minimum rentals to be received under non-cancellable sub-leases greater than one year at December 31, 2010 were $9,500,000.

Cash of approximately $67,745,000 and $60,154,000 at December 31, 2010 and 2009, respectively, was maintained to satisfy regulatory reserve requirements.

The Company is involved in various legal proceedings that are in various stages of litigation. Some of these actions allege "lender liability" claims on a variety of theories and claim substantial actual and punitive damages. The Company has determined, based on discussions with its counsel that any material loss in such actions, individually or in the aggregate, is remote or the damages sought, even if fully recovered, would not be considered material to the consolidated financial position or results of operations of the Company. However, many of these matters are in various stages of proceedings and further developments could cause management to revise its assessment of these matters.

**(17) Commitments, Contingent Liabilities and Other Tax Matters (Continued)**

The Company is involved in a dispute related to certain tax matters that were inherited by the Company in its 2004 acquisition of LFIN. The dispute involves claims by the former controlling shareholders of LFIN related to approximately $14 million of tax refunds received by the Company based on deductions taken in 2003 by LFIN in connection with losses on loans acquired from a failed thrift and a dispute LFIN had with the FDIC regarding the tax benefits related to the failed thrift acquisition which originated in 1988. On March 5, 2010, judgment was entered on a jury verdict rendered against the Company in the U.S. District Court for the Western District of Oklahoma (the "Court"). Other than the tax refunds that are in dispute, the Company does not have any other disputes regarding tax refunds received by the Company in connection with the LFIN acquisition. An amended judgment was entered in the case on November 19, 2010, in the amount of approximately $24.25 million and it is, final and appealable. During December 2010, the Company deposited $24.4 million with the Court in lieu of a supersedeas bond and the Company is currently appealing the judgment.

During the third quarter of 2010, the Internal Revenue Service refunded approximately $1.8 million in tax and $1.5 million in interest on the tax in connection with an adjustment in basis on prior lease-financing transactions where the Company's lead bank subsidiary had received a Notice of Final Partnership Administrative Adjustments ("FPAA"). The interest received on the tax refund was recognized in other interest income and the related tax was included as a credit to provision for income tax expense on the consolidated statement of income.

In October 2010, the Company was named as a defendant in two purported class-action lawsuits, including one filed in the United States District Court for the Southern District of Texas and one filed in the United States District Court for the Southern District of Florida where similar lawsuits against a number of other banks are currently pending in a multi-district proceeding known as "In re Checking Account Overdraft Litigation." The lawsuits challenge the manner in which IBC assesses and collects overdraft fees on ATM and debit transactions and IBC's policies related to posting order. The Texas lawsuit was dismissed without prejudice on January 12, 2011, when the parties stipulated to arbitrate the matter. The Florida case is in early stages, with no responsive pleadings or motions having been filed. No class has been certified in the case. At this state of the lawsuits, the Company cannot determine the probability of a material adverse result or reasonably estimate a range of potential exposures, if any. The Company intends to defend the action vigorously.

**(18) Transactions with Related Parties**

In the ordinary course of business, the subsidiaries of the Company make loans to directors and executive officers of the Corporation, including their affiliates, families and companies in which they are principal owners. In the opinion of management, these loans are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons and do not involve more than normal risk of collectability or present other unfavorable features. The aggregate amounts receivable from such related parties amounted to approximately $53,052,000 and $67,681,000 at December 31, 2010 and 2009, respectively.

**(19) Financial Instruments with Off-Statement of Condition Risk and Concentrations of Credit Risk**

In the normal course of business, the bank subsidiaries are party to financial instruments with off-statement of condition risk to meet the financing needs of their customers. These financial instruments include commitments to their customers. These financial instruments involve, to varying degrees, elements

**(19) Financial Instruments with Off-Statement of Condition Risk and Concentrations of Credit Risk (Continued)**

of credit risk in excess of the amounts recognized in the consolidated statement of condition. The contract amounts of these instruments reflect the extent of involvement the bank subsidiaries have in particular classes of financial instruments. At December 31, 2010, the following financial amounts of instruments, whose contract amounts represent credit risks, were outstanding:

| | |
|---|---|
| Commitments to extend credit | $1,125,468,000 |
| Credit card lines | 64,252,000 |
| Standby letters of credit | 111,295,000 |
| Commercial letters of credit | 8,906,000 |

The Company enters into a standby letter of credit to guarantee performance of a customer to a third party. These guarantees are primarily issued to support public and private borrowing arrangements. The credit risk involved is represented by the contractual amounts of those instruments. Under the standby letters of credit, the Company is required to make payments to the beneficiary of the letters of credit upon request by the beneficiary so long as all performance criteria have been met. At December 31, 2010, the maximum potential amount of future payments is $111,295,000. At December 31, 2010, the fair value of these guarantees is not significant. Unsecured letters of credit totaled $29,160,000 and $29,384,000 at December 31, 2010 and 2009, respectively.

The Company enters into commercial letters of credit on behalf of its customers which authorize a third party to draw drafts on the Company up to a stipulated amount and with specific terms and conditions. A commercial letter of credit is a conditional commitment on the part of the Company to provide payment on drafts drawn in accordance with the terms of the commercial letter of credit.

The bank subsidiaries' exposure to credit loss in the event of nonperformance by the other party to the above financial instruments is represented by the contractual amounts of the instruments. The bank subsidiaries use the same credit policies in making commitments and conditional obligations as they do for on-statement of condition instruments. The bank subsidiaries control the credit risk of these transactions through credit approvals, limits and monitoring procedures. Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates normally less than one year or other termination clauses and may require the payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The bank subsidiaries evaluate each customer's credit-worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the subsidiary banks upon extension of credit, is based on management's credit evaluation of the customer. Collateral held varies, but may include residential and commercial real estate, bank certificates of deposit, accounts receivable and inventory.

The bank subsidiaries make commercial, real estate and consumer loans to customers principally located in South, Central and Southeast Texas and the State of Oklahoma. Although the loan portfolio is diversified, a substantial portion of its debtors' ability to honor their contracts is dependent upon the economic conditions in these areas, especially in the real estate and commercial business sectors.

**(20) Capital Requirements**

On December 23, 3008, as part of the Troubled Asset Relief Program Capital Purchase Program (the "TARP Capital Purchase Program") of the United States Department of the Treasury ("Treasury"), the

**(20) Capital Requirements (Continued)**

Company entered into a Letter Agreement incorporating an attached Securities Purchase Agreement—Standard Terms (collectively, the "Securities Purchase Agreement") with the Treasury. The closing of the transactions contemplated in the Securities Purchase Agreement occurred on December 23, 2008.

Under the Securities Purchase Agreement, the Company agreed to sell 216,000 shares of the Company's fixed-rate cumulative perpetual preferred stock, Series A, par value $.01 per share (the "Senior Preferred Stock"), having a liquidation preference of $1,000 per share, for a total price of $216,000,000. The Senior Preferred Stock will pay dividends at the rate of 5% per year for the first five years and 9% per year thereafter. The Senior Preferred Stock has no maturity date and ranks senior to the Company's common stock with respect to the payment of dividends and distributions and amounts payable upon liquidation, dissolution and winding up of the Company. The Senior Preferred Stock generally is non-voting except for class voting rights on matters that would adversely affect the rights of the holders of the Senior Preferred Stock. The Senior Preferred Stock qualifies for inclusion in Tier 1 capital for regulatory capital purposes and the issuance of the Senior Preferred Stock increased the capital ratios of the Company.

In conjunction with the purchase of the Senior Preferred Stock, the Treasury received a warrant (the "Warrant") to purchase 1,326,238 shares of the Company's common stock (the "Warrant Shares") at $24.43 per share, which would represent an aggregate common stock investment in the Company on exercise of the warrant in full equal to 15% of the Senior Preferred Stock investment. The term of the Warrant is ten years. The per share exercise price and the number of shares issuable upon exercise of the Warrant is subject to adjustment pursuant to customary anti-dilutive provisions in certain events, such as stock splits, certain distributions of securities or other assets to holders of the Company's common stock, and upon certain issuances of the Company's common stock at or below specified prices relative to the initial per share exercise price of the Warrant. The Warrant is immediately exercisable. Both the Senior Preferred Stock and Warrant will be accounted for as components of Tier 1 capital.

Bank regulatory agencies limit the amount of dividends, which the bank subsidiaries can pay the Corporation, through IBC Subsidiary Corporation, without obtaining prior approval from such agencies. At December 31, 2010, the subsidiary banks could pay dividends of up to $465,000,000 to the Company without prior regulatory approval and without adversely affecting their "well capitalized" status. In addition to legal requirements, regulatory authorities also consider the adequacy of the bank subsidiaries' total capital in relation to their deposits and other factors. These capital adequacy considerations also limit amounts available for payment of dividends. The Company historically has not allowed any subsidiary bank to pay dividends in such a manner as to impair its capital adequacy.

The Company and the bank subsidiaries are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company must meet specific capital guidelines that involve quantitative measures of the Company's assets, liabilities, and certain off-statement of condition items as calculated under regulatory accounting practices. The Company's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

**(20) Capital Requirements (Continued)**

Additionally, as a result of the Company's participation in the TARP Capital Purchase Program, the Company is restricted in the payment of dividends and may not, without Treasury Department's consent, declare or pay any dividend on the Company Common Stock other than a regular semi-annual dividend of not more than $.33 per share, as adjusted for any stock dividend or stock split. The restriction ceases to exist only on the earlier to occur of December 23, 2011 or the date on which the Company has redeemed all of the Series A Preferred Stock issued as part of the Capital Purchase Program or the date on which the Treasury has transferred all of the Preferred Stock to third parties not affiliated with the Treasury. Also, all accrued and unpaid dividends on the Senior Preferred Stock would have to be fully paid before the Company paid any dividends on its Common Stock. On April 7, 2009, the Company gained consent from the Treasury Department (the "Treasury Consent") to use the regular semi-annual cash dividend funds of not more than $.33 per share, as adjusted for any stock dividend or stock split, to pay quarterly dividends and to repurchase common stock. Any cash dividends combined with amounts spent in conjunction with the Company's stock repurchase program will be limited by the restrictions set forth in the Treasury Consent.

A company that participates in the TARP Capital Purchase Program must adopt certain standards for executive compensation under the Emergency Economic Stabilization Act of 2008 (EESA) and the American Recovery and Reinvestment Act of 2009 (the "ARRA") which was signed into law on February 17, 2009. While the U.S. Treasury must promulgate regulations to implement the executive compensation restrictions and standards set forth in the ARRA, the new law significantly expands the executive compensation restrictions previously imposed by the EESA. Such restrictions apply to any entity that has received or will receive funds under the TARP Capital Purchase Program, and shall generally continue to apply for as long as any obligation arising from securities issued under TARP, including preferred stock issued under the Capital Purchase Program, remain outstanding. These ARRA restrictions shall not apply to any TARP Capital Purchase Program recipient during such time when the federal government (i) only holds any warrants to purchase common stock of such recipient or (ii) holds no preferred stock or warrants to purchase common stock of such recipient. As a result of the Company's participation in the TARP Capital Purchase Program, the restrictions and standards set forth in the ARRA shall be applicable to the Company, subject to regulations promulgated by the U.S. Treasury.

Pursuant to the provisions of the ARRA, the Company may be permitted to repay the $216 million it received under the TARP Capital Purchase Program, without regard to certain repayment restrictions in the Securities Purchase Agreement, which restricted the Company's ability to redeem the Senior Preferred Stock during the first three years following the date of investment. The redemption of the Senior Preferred Stock is subject to the consent of the Federal Reserve Bank of Dallas, which is the Company's primary Federal banking regulator. To date, the Company has not redeemed any of the Senior Preferred Stock.

Quantitative measures established by regulation to ensure capital adequacy require the Company to maintain minimum amounts and ratios (set forth in the table on the following page) of Total and Tier 1 capital to risk-weighted assets and of Tier 1 capital to average assets. Management believes, as of December 31, 2010, that the Company and each of the bank subsidiaries met all capital adequacy requirements to which it is subject.

As of December 31, 2010, the most recent notification from the Federal Deposit Insurance Corporation categorized all the bank subsidiaries as well capitalized under the regulatory framework for prompt corrective action. To be categorized as "well capitalized" the Company and the bank subsidiaries must maintain minimum Total risk-based, Tier 1 risk based, and Tier 1 leverage ratios as set forth in the table. There are no conditions or events since that notification that management believes have changed the categorization of the Company or any of the bank subsidiaries as well capitalized.

### (20) Capital Requirements (Continued)

The Company's and the bank subsidiaries' actual capital amounts and ratios for 2010 are presented in the following table:

| | Actual | | For Capital Adequacy Purposes | | To Be Well Capitalized Under Prompt Corrective Action Provisions | |
|---|---|---|---|---|---|---|
| | Amount | Ratio | Amount | Ratio | Amount | Ratio |
| | | | (greater than or equal to) | (greater than or equal to) | (greater than or equal to) | (greater than or equal to) |
| | | | (Dollars in Thousands) | | | |
| As of December 31, 2010: | | | | | | |
| Total Capital (to Risk Weighted Assets): | | | | | | |
| Consolidated | $1,413,299 | 20.72% | $545,668 | 8.00% | N/A | N/A |
| International Bank of Commerce, Laredo | 957,234 | 16.39 | 467,249 | 8.00 | $584,061 | 10.00% |
| International Bank of Commerce, Brownsville | 112,888 | 25.60 | 35,283 | 8.00 | 44,103 | 10.00 |
| International Bank of Commerce, Zapata | 54,072 | 30.96 | 13,971 | 8.00 | 17,463 | 10.00 |
| Commerce Bank | 62,129 | 31.67 | 15,692 | 8.00 | 19,615 | 10.00 |
| Tier 1 Capital (to Risk Weighted Assets): | | | | | | |
| Consolidated | $1,327,889 | 19.47% | $272,834 | 4.00% | N/A | N/A |
| International Bank of Commerce, Laredo | 889,247 | 15.23 | 233,624 | 4.00 | $350,437 | 6.00% |
| International Bank of Commerce, Brownsville | 107,340 | 24.34 | 17,641 | 4.00 | 26,462 | 6.00 |
| International Bank of Commerce, Zapata | 51,869 | 29.70 | 6,985 | 4.00 | 10,478 | 6.00 |
| Commerce Bank | 59,752 | 30.46 | 7,846 | 4.00 | 11,769 | 6.00 |
| Tier 1 Capital (to Average Assets): | | | | | | |
| Consolidated | $1,327,889 | 11.58% | $458,500 | 4.00% | N/A | N/A |
| International Bank of Commerce, Laredo | 889,247 | 9.29 | 382,886 | 4.00 | $478,608 | 5.00% |
| International Bank of Commerce, Brownsville | 107,340 | 12.78 | 33,586 | 4.00 | 41,983 | 5.00 |
| International Bank of Commerce, Zapata | 51,869 | 10.90 | 19,035 | 4.00 | 23,793 | 5.00 |
| Commerce Bank | 59,752 | 11.33 | 21,095 | 4.00 | 26,369 | 5.00 |

**(20) Capital Requirements (Continued)**

The Company's and the bank subsidiaries' actual capital amounts and ratios for 2009 are also presented in the following table:

| | Actual | | For Capital Adequacy Purposes | | To Be Well Capitalized Under Prompt Corrective Action Provisions | |
|---|---|---|---|---|---|---|
| | Amount | Ratio | Amount | Ratio | Amount | Ratio |
| | | | (greater than or equal to) | (greater than or equal to) | (greater than or equal to) | (greater than or equal to) |
| | (Dollars in Thousands) | | | | | |
| As of December 31, 2009: | | | | | | |
| Total Capital (to Risk Weighted Assets): | | | | | | |
| Consolidated | $1,321,656 | 18.99% | $556,763 | 8.00% | N/A | N/A |
| International Bank of Commerce, Laredo | 881,679 | 14.80 | 476,708 | 8.00 | $595,885 | 10.00% |
| International Bank of Commerce, Brownsville | 104,964 | 22.70 | 36,984 | 8.00 | 46,230 | 10.00 |
| International Bank of Commerce, Zapata | 50,648 | 29.00 | 13,973 | 8.00 | 17,466 | 10.00 |
| Commerce Bank | 61,157 | 30.12 | 16,244 | 8.00 | 20,305 | 10.00 |
| Tier 1 Capital (to Risk Weighted Assets): | | | | | | |
| Consolidated | $1,234,929 | 17.74% | $278,381 | 4.00% | N/A | N/A |
| International Bank of Commerce, Laredo | 810,417 | 13.60 | 238,354 | 4.00 | $357,531 | 6.00% |
| International Bank of Commerce, Brownsville | 99,179 | 21.45 | 18,492 | 4.00 | 27,738 | 6.00 |
| International Bank of Commerce, Zapata | 49,120 | 28.12 | 6,987 | 4.00 | 10,480 | 6.00 |
| Commerce Bank | 58,703 | 28.91 | 8,122 | 4.00 | 12,183 | 6.00 |
| Tier 1 Capital (to Average Assets): | | | | | | |
| Consolidated | $1,234,929 | 10.95% | $451,133 | 4.00% | N/A | N/A |
| International Bank of Commerce, Laredo | 810,417 | 8.59 | 377,496 | 4.00 | $471,870 | 5.00% |
| International Bank of Commerce, Brownsville | 99,179 | 12.32 | 32,189 | 4.00 | 40,237 | 5.00 |
| International Bank of Commerce, Zapata | 49,120 | 11.13 | 17,651 | 4.00 | 22,063 | 5.00 |
| Commerce Bank | 58,703 | 13.17 | 17,835 | 4.00 | 22,293 | 5.00 |

**(21) Fair Value**

Effective January 1, 2008, the Company adopted Statement of Financial Accounting Standards No. 157 ("SFAS No. 157"), "Fair Value Measurements" for financial assets and liabilities. Additionally, in accordance with Financial Accounting Standards Board Staff Position No. 157-2, ("FSP No 157-2"), "Effective date of FASB Statement No. 157," the Company delayed application of SFAS No. 157 for non-financial assets and non-financial liabilities until January 1, 2009, except for those that are recognized or disclosed at fair value on a recurring basis. SFAS No. 157 and FSP No. 157-2 are now included in the Accounting Standards Codification ("ASC") in Topic 820, "Fair Value Measurements and Disclosures" ("ASC 820"). ASC 820 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. ASC 820 applies to all financial instruments that are being measured and reported on a fair value basis. ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date; it also establishes a fair value hierarchy that prioritizes the inputs used in valuation methodologies into the following three levels:

- Level 1 Inputs—Unadjusted quoted prices in active markets for identical assets or liabilities.

**(21) Fair Value (Continued)**

- Level 2 Inputs—Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 Inputs—Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or other valuation techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy is set forth below.

The following table represents assets and liabilities reported on the consolidated balance sheets at their fair value as of December 31, 2010 by level within the fair value measurement hierarchy.

| | | Fair Value Measurements at Reporting Date Using (in thousands) | | |
|---|---|---|---|---|
| | Assets/Liabilities Measured at Fair Value December 31, 2010 | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| *Measured on a recurring basis:* | | | | |
| Assets: | | | | |
| U.S. Treasury securities | | | | |
| Available-for-sale | $ 1,327 | $ — | $ 1,327 | $ — |
| Residential mortgage-backed securities | | | | |
| Available-for-sale | 4,924,468 | — | 4,878,440 | 46,028 |
| States and political subdivisions | | | | |
| Available-for-sale | 145,997 | — | 145,997 | — |
| Other | | | | |
| Available-for-sale | 14,665 | 14,665 | — | — |
| *Measured on a non-recurring basis:* | | | | |
| Assets: | | | | |
| Impaired Loans | 39,335 | — | — | 39,335 |
| Non-financial assets: | | | | |
| Other real estate owned | 52,319 | — | — | 52,319 |

**(21) Fair Value (Continued)**

The following table represents assets and liabilities reported on the consolidated balance sheets at their fair value as of December 31, 2009 by level within the fair value measurement hierarchy.

| | | Fair Value Measurements at Reporting Date Using (in thousands) | | |
|---|---|---|---|---|
| | Assets/Liabilities Measured at Fair Value December 31, 2009 | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| *Measured on a recurring basis:* | | | | |
| Assets: | | | | |
| U.S. Treasury securities | | | | |
| Available-for-sale | $ 1,327 | $ — | $ 1,327 | $ — |
| Residential mortgage-backed securities | | | | |
| Available-for-sale | 4,491,764 | — | 4,432,195 | 59,569 |
| States and political subdivisions | | | | |
| Available-for-sale | 136,866 | — | 136,866 | — |
| Other | | | | |
| Available-for-sale | 14,126 | 14,126 | — | — |
| *Measured on a non-recurring basis:* | | | | |
| Assets: | | | | |
| Impaired Loans | 76,225 | — | — | 76,225 |
| Non-Financial Assets | | | | |
| Other real estate owned | 15,255 | — | — | 15,255 |

Investment securities available-for-sale are classified within level 2 and level 3 of the valuation hierarchy, with the exception of certain equity investments that are classified within level 1. For investments classified as level 2 in the fair value hierarchy, the Company obtains fair value measurements for investment securities from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions, among other things. Investment securities classified as level 3 are non-agency mortgage-backed securities. The non-agency mortgage-backed securities held by the Company are traded in in-active markets and markets that have experienced significant decreases in volume and level of activity, as exhibited by few recent transactions, a significant decline or absence of new issuances, price quotations that are not based on comparable securities transactions and wide bid-ask spreads among other factors. As a result of the inability to use quoted market prices to determine fair value for these securities, the Company determined that fair value, as determined by level 3 inputs in the fair value hierarchy, is more appropriate for financial reporting and more consistent with the expected performance of the investments. For the investments classified within level 3 of the fair value hierarchy, the Company used a discounted cash flow model to determine fair value. Inputs in the model included both historical performance and expected future performance based on information currently available. Assumptions used in the discounted cash flow model included estimates on future principal prepayment rates, default and loss severity rates. The Company estimates that future principal prepayment rates will range from 4-5% and used a 13% discount rate. Default rates used in the model were 10-11% for the first year and 7% thereafter, and loss severity rates started at 60% for the first year and are declined by 10% for the following three years, and remains at 20% thereafter.

**(21) Fair Value (Continued)**

The following table presents a reconciliation of activity for such mortgage-backed securities on a net basis (Dollars in thousands):

| | |
|---|---|
| Balance at December 31, 2009 | $59,569 |
| Principal paydowns, net of discount amortization | (9,538) |
| Total unrealized gains (losses) included in: | |
| Other comprehensive income | 4,413 |
| Net income | (8,416) |
| Balance at December 31, 2010 | $46,028 |

Certain financial assets and financial liabilities are measured at fair value on a nonrecurring basis. The instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment).

As of December 31, 2010, the Company's financial instruments measured at fair value on a non-recurring basis are limited to impaired loans. Impaired loans are classified within level 3 of the valuation hierarchy. The fair value of impaired loans is derived in accordance with FASB ASC 310, "Receivables". The fair value of impaired loans is based on the fair value of the collateral, as determined through an external appraisal process, discounted based on internal criteria. Impaired loans are primarily comprised of collateral-dependent commercial loans. Non-financial assets measured at fair value on a non-recurring basis are limited to other real estate owned. Other real estate owned is comprised of real estate acquired by foreclosure and deeds in lieu of foreclosure. Other real estate owned is carried at the lower of the recorded investment in the property or its fair value less estimated costs to sell such property (as determined by independent appraisal) within level 3 of the fair value hierarchy. Prior to foreclosure, the value of the underlying loan is written down to the fair value of the real estate to be acquired by a charge to the allowance for probable loan losses, if necessary. The fair value is reviewed periodically and subsequent write downs are made accordingly. Other real estate owned is included in other assets on the consolidated financial statements.

The fair value estimates, methods, and assumptions for the Company's financial instruments at December 31, 2010 and December 31, 2009 are outlined below.

*Cash and Due From Banks and Federal Funds Sold*

For these short-term instruments, the carrying amount is a reasonable estimate of fair value.

*Investment securities held-to-maturity*

The carrying amounts of investments held-to-maturity approximate fair value.

*Investment Securities*

For investment securities, which include U. S. Treasury securities, obligations of other U. S. government agencies, obligations of states and political subdivisions and mortgage pass through and related securities, fair values are based on quoted market prices or dealer quotes. Fair values are based on the value of one unit without regard to any premium or discount that may result from concentrations of

**(21) Fair Value (Continued)**

ownership of a financial instrument, probable tax ramifications, or estimated transaction costs. See disclosures of fair value of investment securities in Note 2.

*Loans*

Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type such as commercial, real estate and consumer loans as outlined by regulatory reporting guidelines. Each category is segmented into fixed and variable interest rate terms and by performing and non-performing categories.

For variable rate performing loans, the carrying amount approximates the fair value. For fixed rate performing loans, except residential mortgage loans, the fair value is calculated by discounting scheduled cash flows through the estimated maturity using estimated market discount rates that reflect the credit and interest rate risk inherent in the loan. For performing residential mortgage loans, fair value is estimated by discounting contractual cash flows adjusted for prepayment estimates using discount rates based on secondary market sources or the primary origination market. At December 31, 2010, and December 31, 2009, the carrying amount of fixed rate performing loans was $1,337,827,000 and $1,303,049,000 respectively, and the estimated fair value was $1,226,413,000 and $1,200,343,000, respectively.

*Accrued Interest*

The carrying amounts of accrued interest approximate fair value.

*Deposits*

The fair value of deposits with no stated maturity, such as non-interest bearing demand deposit accounts, savings accounts and interest bearing demand deposit accounts, was equal to the amount payable on demand as of December 31, 2010 and December 31, 2009. The fair value of time deposits is based on the discounted value of contractual cash flows. The discount rate is based on currently offered rates. At December 31, 2010 and December 31, 2009, the carrying amount of time deposits was $3,437,640,000 and $3,398,656,000, respectively, and the estimated fair value was $3,449,980,000 and $3,412,538,000, respectively.

*Securities Sold Under Repurchase Agreements and Other Borrowed Funds*

Securities sold under repurchase agreements include both short and long-term maturities. Due to the contractual terms of the short-term instruments, the carrying amounts approximated fair value at December 31, 2010 and December 31, 2009. The fair value of the long-term instruments is based on established market spreads. At December 31, 2010 and December 31, 2009, the carrying amount of long-term repurchase agreements was $1,000,000,000 and the estimated fair value was $1,123,774,000 and $1,099,064,000, respectively. Other borrowed funds are short and long-term Federal Home Loan Bank borrowings. Due to the contractual terms of these financial instruments, the carrying amounts approximated fair value at December 31, 2010 and December 31, 2009.

*Junior Subordinated Deferrable Interest Debentures*

The Company currently has fixed and floating junior subordinated deferrable interest debentures outstanding. Due to the contractual terms of the floating rate junior subordinated deferrable interest

**(21) Fair Value (Continued)**

debentures, the carrying amounts approximated fair value at December 31, 2010 and December 31, 2009. The fair value of the fixed junior subordinated deferrable interest debentures is based on established market spreads to the debentures. At December 31, 2010 and December 31, 2009, the carrying amount of fixed junior subordinated deferrable interest debentures was $139,259,000 and $139,224,000, respectively, and the estimated fair value was $74,103,000 and $65,762,000, respectively.

*Commitments to Extend Credit and Letters of Credit*

Commitments to extend credit and fund letters of credit are principally at current interest rates and therefore the carrying amount approximates fair value.

*Limitations*

Fair value estimates are made at a point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Fair value estimates are based on existing on-and off-statement of condition financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. Other significant assets and liabilities that are not considered financial assets or liabilities include the bank premises and equipment and core deposit value. In addition, the tax ramifications related to the effect of fair value estimates have not been considered in the above estimates.

## (22) International Bancshares Corporation (Parent Company Only) Financial Information

**Statements of Condition**
**(Parent Company Only)**

**December 31, 2010 and 2009**
**(Dollars in Thousands)**

| | 2010 | 2009 |
|---|---|---|
| ASSETS | | |
| Cash | $ 24,414 | $ 16,712 |
| Other investments | 65,485 | 61,270 |
| Notes receivable | 250 | 100 |
| Investment in subsidiaries | 1,577,038 | 1,532,961 |
| Other assets | 3,874 | 3,260 |
| Total assets | $1,671,061 | $1,614,303 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Liabilities: | | |
| Junior subordinated deferrable interest debentures | $ 201,117 | $ 201,082 |
| Due to IBC Trading | 21 | 21 |
| Other liabilities | 10,706 | 5,730 |
| Total liabilities | 211,844 | 206,833 |
| Shareholders' equity: | | |
| Preferred shares | 208,068 | 205,742 |
| Common shares | 95,711 | 95,711 |
| Surplus | 162,276 | 161,258 |
| Retained earnings | 1,214,743 | 1,122,290 |
| Accumulated other comprehensive income | 28,777 | 65,878 |
| | 1,709,575 | 1,650,879 |
| Less cost of shares in treasury | (250,358) | (243,409) |
| Total shareholders' equity | 1,459,217 | 1,407,470 |
| Total liabilities and shareholders' equity | $1,671,061 | $1,614,303 |

## (23) International Bancshares Corporation (Parent Company Only) Financial Information

**Statements of Income**
**(Parent Company Only)**

**Years ended December 31, 2010, 2009 and 2008**
**(Dollars in Thousands)**

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| Income: | | | |
| Dividends from subsidiaries | $ 51,720 | $ 45,122 | $ 53,460 |
| Interest income on notes receivable | 5 | 6 | 80 |
| Interest income on other investments | 10,090 | 8,191 | 5,313 |
| Other interest income | 546 | 914 | 486 |
| Other | (742) | 7,225 | 65 |
| Total income | 61,619 | 61,458 | 59,404 |
| Expenses: | | | |
| Interest expense (Debentures) | 12,201 | 12,535 | 14,137 |
| Other interest expense | — | — | 88 |
| Other | 3,408 | 1,751 | 1,793 |
| Total expenses | 15,609 | 14,286 | 16,018 |
| Income before federal income taxes and equity in undistributed net income of subsidiaries | 46,010 | 47,172 | 43,386 |
| Income tax benefit | (2,090) | 743 | (3,593) |
| Income before equity in undistributed net income of subsidiaries | 48,100 | 46,429 | 46,979 |
| Equity in undistributed net income of subsidiaries | 81,923 | 96,313 | 85,133 |
| Net income | 130,023 | 142,742 | 132,112 |
| Preferred stock dividends and discount accretion | 13,126 | 12,984 | — |
| Net income available to common shareholders | $116,897 | $129,758 | $132,112 |

## (24) International Bancshares Corporation (Parent Company Only) Financial Information

### Statements of Cash Flows (Parent Company Only)

### Years ended December 31, 2010, 2009 and 2008 (Dollars in Thousands)

| | 2010 | 2009 | 2008 |
|---|---|---|---|
| Operating activities: | | | |
| Net income | $130,023 | $ 142,742 | $132,112 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Accretion of junior subordinated interest deferrable debentures | 35 | 35 | 119 |
| Investment securities transactions, net | 1,135 | (6,586) | — |
| Accretion of investment securities discounts | (232) | (325) | — |
| Stock compensation expense | 534 | 655 | 692 |
| Increase in other liabilities | 4,976 | (309) | 1,443 |
| Equity in undistributed net income of subsidiaries | (81,923) | (96,414) | (85,133) |
| Net cash provided by operating activities | 54,548 | 39,798 | 49,233 |
| Investing activities: | | | |
| Contributions to subsidiaries | — | (138,103) | (57,114) |
| Proceeds of repurchase agreement with banks | — | — | 1,000 |
| Principal collected on mortgage-backed securities | 3,324 | 2,791 | — |
| Net (increase) decrease in notes receivable | (150) | 250 | 1,491 |
| Increase in other assets | (8,311) | (9,215) | (5,000) |
| Net cash used in investing activities | (5,137) | (144,277) | (59,623) |
| Financing activities: | | | |
| Proceeds from issuance of preferred stock | — | — | 216,000 |
| Proceeds from stock transactions | 484 | 2,705 | 894 |
| Payments of cash dividends—common | (24,444) | (23,262) | (45,253) |
| Payments of cash dividends—preferred | (10,800) | (9,660) | — |
| Purchase of treasury stock | (6,949) | (9,346) | (1,077) |
| Net cash (used in) provided by financing activities | (41,709) | (39,563) | 170,564 |
| Increase (decrease) in cash | 7,702 | (144,042) | 160,174 |
| Cash at beginning of year | 16,712 | 160,754 | 580 |
| Cash at end of year | $ 24,414 | $ 16,712 | $160,754 |

**INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES**
**Condensed Quarterly Income Statements**
**(Dollars in Thousands, Except Per Share Amounts)**
**(Unaudited)**

| | Fourth Quarter | Third Quarter | Second Quarter | First Quarter |
|---|---|---|---|---|
| **2010** | | | | |
| Interest income | $111,612 | $114,255 | $113,080 | $119,822 |
| Interest expense | 26,564 | 27,902 | 29,643 | 29,927 |
| Net interest income | 85,048 | 86,353 | 83,437 | 89,895 |
| Provision for probable loan losses | 7,317 | 6,837 | 1,429 | 7,229 |
| Non-interest income | 50,898 | 46,889 | 49,400 | 71,597 |
| Non-interest expense | 75,305 | 79,379 | 79,464 | 105,577 |
| Income before income taxes | 53,324 | 47,026 | 51,944 | 48,686 |
| Income taxes | 22,904 | 13,477 | 17,936 | 16,640 |
| Net income | $ 30,420 | $ 33,549 | $ 34,008 | $ 32,046 |
| Preferred Stock Dividends | 3,295 | 3,286 | 3,277 | 3,268 |
| Net income available to common shareholders | $ 27,125 | $ 30,263 | $ 30,731 | $ 28,778 |
| Per common share: | | | | |
| Basic | | | | |
| Net income | $ .40 | $ .45 | $ .45 | $ .42 |
| Diluted | | | | |
| Net income | $ .40 | $ .45 | $ .45 | $ .42 |

**INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES**
**Condensed Quarterly Income Statements**
**(Dollars in Thousands, Except Per Share Amounts)**
**(Unaudited)**

| | Fourth Quarter | Third Quarter | Second Quarter | First Quarter |
|---|---|---|---|---|
| **2009** | | | | |
| Interest income | $126,279 | $126,704 | $134,178 | $140,216 |
| Interest expense | 30,818 | 32,257 | 34,651 | 42,070 |
| Net interest income | 95,461 | 94,447 | 99,527 | 98,146 |
| Provision for probable loan losses | 13,404 | 10,346 | 22,858 | 12,225 |
| Non-interest income | 51,934 | 50,875 | 56,192 | 42,012 |
| Non-interest expense | 74,878 | 78,746 | 85,181 | 70,226 |
| Income before income taxes | 59,113 | 56,230 | 47,680 | 57,707 |
| Income taxes | 22,005 | 19,257 | 16,547 | 20,179 |
| Net income | $ 37,108 | $ 36,973 | $ 31,133 | $ 37,528 |
| Preferred Stock Dividends | 3,259 | 3,250 | 3,242 | 3,233 |
| Net income available to common shareholders | $ 33,849 | $ 33,723 | $ 27,891 | $ 34,295 |
| Per common share: | | | | |
| Basic | | | | |
| Net income | $ .50 | $ .49 | $ .41 | $ .50 |
| Diluted | | | | |
| Net income | $ .50 | $ .49 | $ .41 | $ .50 |

## INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES
## Condensed Average Statements of Condition
## (Dollars in Thousands, Except Per Share Amounts)
## (Unaudited)

Distribution of Assets, Liabilities and Shareholders' Equity

The following table sets forth a comparative summary of average interest earning assets and average interest bearing liabilities and related interest yields for the years ended December 31, 2010, 2009, and 2008:

| | 2010 | | | 2009 | | | 2008 | | |
|---|---|---|---|---|---|---|---|---|---|
| | Average Balance | Interest | Average Rate/Cost | Average Balance | Interest | Average Rate/Cost | Average Balance | Interest | Average Rate/Cost |
| | (Dollars in Thousands) | | | | | | | | |
| *Assets* | | | | | | | | | |
| Interest earning assets: | | | | | | | | | |
| Loan, net of unearned discounts: | | | | | | | | | |
| Domestic | $ 5,294,744 | $302,779 | 5.72% | $ 5,474,162 | $322,143 | 5.88% | $ 5,360,116 | $353,635 | 6.60% |
| Foreign | 247,486 | 11,423 | 4.62 | 274,627 | 13,626 | 4.96 | 283,444 | 17,083 | 6.03 |
| Investment securities: | | | | | | | | | |
| Taxable | 4,095,542 | 135,106 | 3.30 | 4,281,148 | 185,931 | 4.34 | 4,120,008 | 188,928 | 4.59 |
| Tax-exempt | 144,199 | 7,240 | 5.02 | 104,140 | 5,070 | 4.87 | 72,117 | 3,514 | 4.87 |
| Federal funds sold | — | — | — | — | — | — | 53,019 | 927 | 1.75 |
| Other | 99,671 | 2,221 | 2.23 | 69,813 | 607 | .87 | 9,874 | 516 | 5.23 |
| Total interest-earning assets | 9,881,642 | 458,769 | 4.64% | 10,203,890 | 527,377 | 5.17% | 9,898,578 | 564,603 | 5.70% |
| Non-interest earning assets: | | | | | | | | | |
| Cash and due from banks | 285,894 | | | 285,811 | | | 236,656 | | |
| Bank premises and equipment, net | 475,460 | | | 479,281 | | | 445,487 | | |
| Other assets | 715,278 | | | 738,568 | | | 728,038 | | |
| Less allowance for probable loan losses | (90,900) | | | (82,194) | | | (64,917) | | |
| Total | $11,267,374 | | | $11,625,356 | | | $11,243,842 | | |
| *Liabilities and Shareholders' Equity* | | | | | | | | | |
| Interest bearing liabilities: | | | | | | | | | |
| Savings and interest bearing demand deposits | $ 2,389,699 | $ 9,383 | .39% | $ 2,135,147 | $ 10,832 | .51% | $ 2,286,000 | $ 26,651 | 1.17% |
| Time deposits: | | | | | | | | | |
| Domestic | 1,804,106 | 26,255 | 1.46 | 1,718,744 | 33,691 | 1.96 | 1,702,549 | 55,287 | 3.25 |
| Foreign | 1,673,426 | 20,712 | 1.24 | 1,607,431 | 28,564 | 1.78 | 1,644,997 | 51,192 | 3.11 |
| Securities sold under repurchase agreements | 1,479,764 | 44,216 | 2.99 | 1,462,017 | 44,723 | 3.06 | 1,436,374 | 50,400 | 3.51 |
| Other borrowings | 656,459 | 1,269 | .19 | 1,662,489 | 9,451 | .57 | 1,395,220 | 33,976 | 2.44 |
| Junior subordinated interest deferrable debentures | 201,099 | 12,201 | 6.07 | 201,064 | 12,535 | 6.23 | 201,042 | 14,137 | 7.03 |
| Senior notes | — | — | — | — | — | — | — | 88 | — |
| Total interest bearing liabilities | 8,204,553 | 114,036 | 1.39% | 8,786,892 | 139,796 | 1.59% | 8,666,182 | 231,731 | 2.67% |
| Non-interest bearing liabilities: | | | | | | | | | |
| Demand Deposits | 1,639,119 | | | 1,480,994 | | | 1,455,036 | | |
| Other liabilities | 44,431 | | | 70,060 | | | 132,306 | | |
| Shareholders' equity | 1,379,271 | | | 1,287,410 | | | 990,318 | | |
| Total | $11,267,374 | | | $11,625,356 | | | $11,243,842 | | |
| Net interest income | | $344,733 | | | $387,581 | | | $332,872 | |
| Net yield on interest earning assets | | | 3.49% | | | 3.80% | | | 3.36% |

## INTERNATIONAL BANCSHARES CORPORATION
## OFFICERS AND DIRECTORS

**OFFICERS**

DENNIS E. NIXON
Chairman of the Board and President

R. DAVID GUERRA
Vice President

EDWARD J. FARIAS
Vice President

IMELDA NAVARRO
Treasurer

WILLIAM CUELLAR
Auditor

MARISA V. SANTOS
Secretary

HILDA V. TORRES
Assistant Secretary

**DIRECTORS**

DENNIS E. NIXON
President, International Bank of Commerce

IRVING GREENBLUM
International Investments/Real Estate

R. DAVID GUERRA
President
International Bank of Commerce
Branch in McAllen, TX

DANIEL B. HASTINGS, JR.
Licensed U. S. Custom Broker
President
Daniel B. Hastings, Inc.

DOUG HOWLAND
Owner
Construction & Construction Materials Company
Investments

IMELDA NAVARRO
Senior Executive Vice President
International Bank of Commerce

SIOMA NEIMAN
International Entrepreneur

PEGGY NEWMAN
Investments

LARRY NORTON
President
Norton Stores, Inc.

LEONARDO SALINAS
Investments

ANTONIO R. SANCHEZ, JR.
Chairman of the Board
Sanchez Oil & Gas Corporation
Investments

GUILLERMO TREVINO
President
Southern Distributing, Inc.

*We do more*
*Hacemos más*