

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

☒ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2010

or

☐TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period fromto

Commission file number: 0-09439

INTERNATIONAL BANCSHARES CORPORATION

(Exact Name of Registrant as Specified in its Charter)

Texas

(State or other jurisdiction of
Incorporation or organization)

74-2157138

(I.R.S. Employer
Identification No.)

1200 San Bernardo Avenue

Laredo, Texas 78042-1359

(Address of principal executive office and Zip Code)

(956) 722-7611

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
None	None

Securities Registered Pursuant to Section 12(g) of the Act:

Common Stock (\$1.00 par value)

(Title of Class)

Indicate by check mark if the Registrant is a well known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☒ No ☐

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Act. Yes ☐ No ☒

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K Section 229.405 of this chapter is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

Indicate by check mark if the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "small reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated filer ☒

Accelerated filer ☐

Non-accelerated filer ☐
(Do not check if a
smaller reporting company)

Smaller reporting company ☐

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes ☐ No ☒

The aggregate market value of the voting stock held by non-affiliates of the Registrant as of June 30, 2010 was \$1,130,017,000 based on the closing sales price per share of the Registrant's common stock on such date as reported by NASDAQ.

As of February 22, 2011, there were 67,701,671 shares of the Registrant's Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the following documents are incorporated by reference into the designated parts of this Form 10-K:
(a) Annual Report to security holders for the fiscal year ended December 31, 2010 (in Parts I and II) and (b) Proxy Statement relating to the Company's 2011 Annual Meeting of Shareholders (in Part III).

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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

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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

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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.

Item 1. Business

General

The Company is a financial holding company with its principal corporate offices in Laredo, Texas. Four bank subsidiaries provide commercial and retail banking services through 278 main banking and branch facilities located in 107 communities in South, Central and Southeast Texas and the State of Oklahoma. The Company was originally incorporated under the General Corporation Law of the State of Delaware in 1979. Effective June 7, 1995, the Company's state of incorporation was changed from Delaware to Texas. The Company was organized for the purpose of operating as a bank holding company within the meaning of the Bank Holding Company Act of 1956, as amended (the "BHCA"), and as such, is subject to supervision and regulation by the Board of Governors of the Federal Reserve System (the "FRB"). As a registered bank holding company, the Company may own one or more banks and may engage directly, or through subsidiary corporations, in those activities closely related to banking which are specifically permitted under the BHCA and by the FRB. Effective March 13, 2000, the Company became certified as a financial holding company. As a financial holding company, the Company may engage in a broad list of financial and non-financial activities. The Company's principal assets at December 31, 2010 consisted of all the outstanding capital stock of four Texas state banking associations (the "Banks" or "bank subsidiaries"). All of the Company's bank subsidiaries are members of the Federal Deposit Insurance Corporation (the "FDIC").

The bank subsidiaries are in the business of gathering funds from various sources and investing these funds in order to earn a return. Funds gathering primarily takes the form of accepting demand and time deposits from individuals, partnerships, corporations and public entities. Investments principally are made in loans to various individuals and entities as well as in debt securities of the U.S. Government and various other entities whose payments are guaranteed by the U.S. Government. Historically, the bank subsidiaries have primarily focused on providing commercial banking services to small and medium sized businesses located in their trade areas and international banking services. In recent years, the bank subsidiaries have also emphasized consumer and retail banking, including mortgage lending, as well as branches situated in retail locations and shopping malls.

The Company's philosophy focuses on customer service as represented by its motto, "We Do More." The Banks maintain a strong commitment to their local communities by, among other things, appointing selected members of the communities in which the Banks' branches are located to local advisory boards (the "local boards"). The local boards direct the operations of the branches, with the supervision of the lead Bank's board of directors, and assist in introducing prospective customers to the Banks as well as developing or modifying products and services to meet customer needs. The Banks function largely on a decentralized basis and the Company believes that such decentralized structure enhances the commitment of the Banks to the communities in which their branches are located. In contrast to many of their principal competitors, the credit decisions of the Banks are made locally and promptly. The Company believes that the knowledge and expertise afforded by the local boards are key components to sound credit decisions. Expense control is an essential element in the Company's profitability. The Company has centralized virtually all of the Banks' back office support and investment functions in order to achieve consistency and cost efficiencies in the delivery of products and services.

On July 28, 1980, the Company acquired all of the outstanding shares of its predecessor, International Bank of Commerce ("IBC"), which is today the flagship bank of the Company, representing the majority of the Company's banking assets. IBC was chartered under the banking laws of Texas in 1966 and has its principal place of business at 1200 San Bernardo Avenue, Laredo, Webb

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County, Texas. It is a wholly-owned subsidiary of the Company. Since the acquisition of the flagship bank in 1980, the Company has formed three banks: (i) Commerce Bank, a Texas state banking association which commenced operations in 1982, located in Laredo, Texas ("Commerce Bank"); (ii) International Bank of Commerce, Brownsville, a Texas state banking association which commenced operations in 1984, located in Brownsville, Texas ("IBC-Brownsville"); and (iii) International Bank of Commerce, Zapata, a Texas state banking association which commenced operations in 1984, located in Zapata, Texas ("IBC-Zapata").

During the last several years, the Company has acquired various financial institutions and banking assets in its trade area and expanded its trade area to the State of Oklahoma. The community-focus of the subsidiary banks and the involvement of the local boards has resulted in the Company becoming aware of acquisition possibilities in the ordinary course of its business and in many instances before other potential purchasers. The Company's decision to pursue an acquisition is based on a multitude of factors, including the ability to efficiently assimilate the operations and assets of the acquired entity, the cost efficiencies to be attained and the growth potential of the market.

The Company also has five direct non-banking subsidiaries. They are (i) IBC Life Insurance Company, a Texas chartered subsidiary which reinsures a small percentage of credit life and accident and health risks related to loans made by bank subsidiaries, (ii) IBC Trading Company, an export trading company which is currently inactive, (iii) IBC Subsidiary Corporation, a second-tier bank holding company incorporated in the State of Delaware, (iv) IBC Capital Corporation, a company incorporated in the State of Delaware for the purpose of holding certain investments of the Company and (v) Premier Tierra Holdings, Inc., a liquidating subsidiary formed under the laws of the State of Texas. The Company owns a fifty percent interest in Gulfstar Group I, Ltd. and related entities, which are involved in investment banking activities. The Company also owns a controlling interest in three merchant banking entities.

Website Access to Reports

The Company makes its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports, filed or furnished pursuant to section 13(a) or 15(d) of the Securities Exchange Act of 1934 available free of charge on or through the Company's internet website, www.ibc.com, as soon as reasonably practicable after such materials are electronically filed with, or furnished to, the Securities and Exchange Commission ("SEC"). Additionally, the Company has posted on its website a code of ethics that applies to its directors and executive officers (including the Company's chief executive officer and financial officer). The Company's website also includes the charter for its Audit Committee and the Company's Excessive or Luxury Expenditure Policy. The Company's website will also include the Proxy Statement relating to the Company's 2011 Annual Meeting of Shareholders upon filing of the definitive Proxy Statement with the SEC.

Services and Employees

The Company, through its bank subsidiaries, IBC, Commerce Bank, IBC-Zapata and IBC-Brownsville, is 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. Certain of the bank subsidiaries are very active in facilitating international trade along the United States border with Mexico and elsewhere. The international banking business of the Company includes providing letters of credit, making commercial and industrial loans, and providing a nominal amount of currency exchange. Each bank subsidiary also offers other related services, such as credit cards, travelers' checks, safety deposit, collection, notary public, escrow, drive-up and walk-up facilities and other customary banking services. Additionally, each bank subsidiary makes available certain securities products through third party providers. The bank subsidiaries also make banking services available during traditional and nontraditional banking hours through their

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network of 440 automated teller machines, and through their 278 branches situated in retail locations and shopping malls. Additionally, IBC introduced IBC Bank Online, an Internet banking product, in order to provide customers online access to banking information and services 24 hours a day.

The Company owns U.S. service mark registrations for "INTERNATIONAL BANK OF COMMERCE," "INTERNATIONAL BANK OF COMMERCE CENTRE," "OVERDRAFT COURTESY," "IBC," "IBC CONNECTION," "IBC ELITE," "IBC ELITE ADVANTAGE," "IBC BANK," "BIZ RITE CHECKING," "GOT YOU COVERED," "FREE BEE," "IT'S A BRIGHTER CHRISTMAS," a design mark depicting a bee character, a design mark depicting the United States and Mexico, and a design mark depicting "IBC" with the United States and Mexico. In addition, the Company owns Texas service mark registrations for "RITE CHECKING," "THE CLUB," "WALL STREET INTERNATIONAL," "INTERNATIONAL BANK OF COMMERCE," "WE DO MORE," a composite mark depicting "CHECK'N SAVE" with a design, a composite mark depicting "WALL STREET INTERNATIONAL," with a design and a design mark depicting the United States and Mexico. The Company also owns Oklahoma service mark registrations for "CHECK 'N SAVE," "RITE CHECKING," "THE CLUB," and "WE DO MORE." The Company also owns a pending application for federal registration of another proprietary service mark and is regularly investigating the availability of service mark registrations related to certain proprietary products.

No material portion of the business of the Company may be deemed seasonal and the deposit and loan base of the Company's bank subsidiaries is diverse in nature. There has been no material effect upon the Company's capital expenditures, earnings or competitive position as a result of Federal, State or local environmental regulation.

As of December 31, 2010, the Company and its subsidiaries employed approximately 2,964 persons full-time and 783 persons part-time.

Competition

The Company is the third largest independent Texas bank holding company. The primary market area of the Company is South, Central and Southeast Texas, an area bordered on the east by the Galveston area, to the northwest by Roundrock, to the southwest by Del Rio and to the southeast by Brownsville, as well as the State of Oklahoma. The Company has increased its market share in its primary market area over the last several years through strategic acquisitions. The Company, through its bank subsidiaries, competes for deposits and loans with other commercial banks, savings and loan associations, credit unions and non-bank entities, which non-bank entities serve as an alternative to traditional financial institutions and are considered to be formidable competitors. The percentage of bank-related services being provided by non-bank entities has increased dramatically during the last several years.

The Company and its bank subsidiaries do a large amount of business for customers domiciled in Mexico, with an emphasis in Northern 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. Such deposits comprised approximately 30%, 31% and 30% of the bank subsidiaries' total deposits for the three years ended December 31, 2010, 2009 and 2008, respectively.

Under the Gramm-Leach-Bliley Act ("GLBA"), effective March 11, 2000, banks, securities firms and insurance companies may affiliate under an entity known as a financial holding company which may then serve its customers' varied financial needs through a single corporate structure. GLBA has significantly changed the competitive environment in which the Company and its subsidiaries conduct business. The financial services industry is also likely to become even more competitive as further technological advances enable more companies to provide financial services. These technological advances may diminish the importance of depository institutions and other financial intermediaries in the transfer of funds between parties.

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Supervision and Regulation

GENERAL—THE COMPANY. In addition to the generally applicable state and Federal laws governing businesses and employers, the Company and its bank subsidiaries are further extensively regulated by special Federal and state laws governing financial institutions. These laws comprehensively regulate the operations of the Company's bank subsidiaries and include, among other matters, requirements to maintain reserves against deposits; restrictions on the nature and amount of loans that may be made and the interest that may be charged thereon; restrictions on the amounts, terms and conditions of loans to directors, officers, large shareholders and their affiliates; restrictions related to investments in activities other than banking; and minimum capital requirements. The descriptions are qualified in their entirety by reference to the full text of the applicable statutes, regulations and policies. With few exceptions, state and Federal banking laws have as their principal objective either the maintenance of the safety and soundness of the Federal deposit insurance system or the protection of consumers, rather than the specific protection of shareholders of the Company. Further, the earnings of the Company are affected by the fiscal and monetary policies of the Federal Reserve System, which regulates the national money supply in order to mitigate recessionary and inflationary pressures. These monetary policies influence to a significant extent the overall growth of bank loans, investments and deposits and the interest rates charged on loans or paid on time and savings deposits. The nature of future monetary policies and the effect of such policies on the future earnings and business of the Company cannot be predicted.

The Dodd-Frank Act

On July 21, 2010, sweeping financial regulatory reform legislation entitled the "Dodd-Frank Wall Street Reform and Consumer Protection Act" (the "Dodd-Frank Act") was signed into law. The Dodd-Frank 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 requirement 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 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 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.

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- Require publicly-traded bank holding companies with \$10 billion in assets or more, like the Company, to create a risk committee responsible for the oversight of risk management of the enterprise.
- Implement corporate governance revisions, including executive compensation and proxy access by shareholders 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 December 31, 2012 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.
- Permit interstate branching de novo without the need to acquire an existing bank.
- Extensive new restrictions and requirements relating to residential mortgage transactions.

Many aspects of the Dodd-Frank 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 are likely to increase the costs associated with deposits as well as place limitations on certain revenues those deposits may generate. Provisions in the legislation that require revisions to the capital requirements of the Company could require the Company to seek other sources of capital in the future. Some of the rules that have been proposed and, in some cases, adopted to comply with the Dodd-Frank Act are discussed further below.

EMERGENCY ECONOMIC STABILIZATION ACT. On October 3, 2008, the President signed into law the Emergency Economic Stabilization Act of 2008 or ("EESA"), which, among other measures, authorized the Secretary of the Treasury to establish the Troubled Asset Relief Program ("TARP"). Pursuant to TARP, the U.S. Treasury has the authority to, among other things, purchase up to \$700 billion of mortgages, mortgage-backed securities and certain other financial instruments from financial institutions for the purpose of stabilizing and providing liquidity to the U.S. financial markets. In addition, under TARP, the Treasury created a capital purchase program ("CPP"), pursuant to which it provides access to capital that will serve as Tier 1 capital to financial institutions through a standardized program to acquire preferred stock (accompanied by warrants) from eligible financial institutions. On December 23, 2008, the Company sold \$216 million of Series A Preferred Stock to the Treasury under the CPP. On February 17, 2009, President Obama signed into law the American Recovery and Reinvestment Act of 2009 (the "ARRA"). ARRA was intended to provide a stimulus to the U.S. economy in the wake of the economic downturn brought about by the subprime mortgage crisis and the resulting credit crunch. ARRA includes federal tax cuts, expansion of unemployment benefits and other social welfare provisions, and domestic spending in education, healthcare, and infrastructure, including the energy structure. ARRA also includes numerous non-economic recovery related items, including a limitation on executive compensation of certain of the most highly-compensated employees and executive officers of financial institutions, such as the Company, that

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participated in the TARP Capital Purchase Program. The restrictions in the new law, which will be further described in rules to be adopted by the Commission and standards to be established by the Treasury Department, include the following:

- Limits on compensation incentives for risk taking by senior executive officers.
- Requirement of recovery of any compensation paid based on inaccurate financial information.
- Prohibition on "Golden Parachute Payments."
- Prohibition on compensation plans that would encourage manipulation of reported earnings to enhance the compensation of employees.
- Publicly registered CPP recipients must establish a board compensation committee comprised entirely of independent directors, for the purpose of reviewing employee compensation plans.
- Prohibition on bonus, retention award, or incentive compensation, except for limited payments of long term restricted stock units payable in stock or cash.
- Limitation on luxury expenditures.
- CPP recipients are required to permit a separate non-binding shareholder vote to approve the compensation of executives, as disclosed pursuant to the SEC's compensation disclosure rules.
- The chief executive officer and chief financial officer of each CPP recipient will be required to provide a written certification of compliance with these standards to the SEC.

Pursuant to the ARRA, subject to consultation with the appropriate Federal banking agency, the Treasury Secretary shall permit a CPP participant to repay the CPP funds that they received without regard to whether the financial institution has replaced such funds from any other source, and when such CPP funds are repaid, the Treasury Secretary will liquidate warrants associated with the CPP funds at the current market price, however, in certain instances the determination of the market price of the warrants has taken considerable time.

FRB APPROVALS. The Company is a registered bank holding company within the meaning of the BHCA, and is subject to supervision by the FRB and to a certain extent the Texas Department of Banking (the "DOB"). The Company is required to file with the FRB annual reports and other information regarding the business operations of itself and its subsidiaries. It is also subject to examination by the FRB. Under the BHCA, a bank holding company is, with limited exceptions, prohibited from acquiring direct or indirect ownership or control of any voting stock of any company which is not a bank or bank holding company, and must engage only in the business of banking, managing, controlling banks, and furnishing services to or performing services for its subsidiary banks. One of the exceptions to this prohibition is the ownership of shares of any company provided such shares do not constitute more than 5% of the outstanding voting shares of the company and so long as the FRB does not disapprove such ownership. Another exception to this prohibition is the ownership of shares of a company the activities of which the FRB has specifically determined to be so closely related to banking, managing or controlling banks as to be a proper incident thereto.

The BHCA and the Change in Bank Control Act of 1978 require that, depending on the circumstances, either FRB approval must be obtained or notice must be furnished to the FRB and not disapproved prior to any person or company acquiring "control" of a bank holding company, such as the Company, subject to certain exceptions for certain transactions. Control is conclusively presumed to exist if an individual or company acquires 25% or more of any class of voting securities of the bank holding company. Control is rebuttably presumed to exist if a person acquires 10% or more but less than 25% of any class of voting securities where the bank holding company, such as the Company, has registered Securities under Section 12 of the Securities Exchange Act of 1934 (the "Exchange Act").

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As a bank holding company, the Company is required to obtain approval prior to merging or consolidating with any other bank holding company, acquiring all or substantially all of the assets of any bank or acquiring ownership or control of shares of a bank or bank holding company if, after the acquisition, the Company would directly or indirectly own or control 5% or more of the voting shares of such bank or bank holding company.

THE USA PATRIOT ACT. Combating money laundering and terrorist financing is a major focus of financial institution regulatory policy. The USA PATRIOT ACT of 2001 substantially expanded the responsibilities of U.S. financial institutions with respect to countering money laundering and terrorist activities. The implementing regulations impose obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing and to verify the identity of their customers. Also, the USA Patriot Act requires the bank regulatory agencies to consider the record of a bank or bank holding company in combating money laundering activities in their evaluation of bank and bank holding company merger or acquisition transactions. The Company has a program in place to monitor and enforce its policies on money laundering, corruption and bribery as well as its policies on prohibiting the use of Company assets to finance or otherwise aid alleged terrorist groups. Failure of a financial institution to maintain and implement adequate programs to combat money laundering and terrorist financing, or to comply with all the relevant laws or regulations, could have serious legal and reputational consequences for the institution.

OFFICE OF FOREIGN ASSETS CONTROL REGULATION. The United States has imposed economic sanctions that affect transactions with designated foreign countries, nationals and others. These are typically known as the "OFAC" rules based on their administration by the U.S. Treasury Department Office of Foreign Assets Control ("OFAC"). The OFAC administered sanctions take many forms, including without limitation, restrictions on trade or investment and the blocking of certain assets related to the designated foreign countries and nationals. Blocked assets, which may include bank deposits, cannot be paid out, withdrawn, set off or transferred in any manner without a license from OFAC. Failure to comply with the OFAC sanctions could have serious legal and reputational consequences.

GRAMM-LEACH-BLILEY. The Gramm-Leach-Bliley Act of 1999 ("GLBA") eliminates the barriers to affiliations among banks, securities firms, insurance companies and other financial service providers. GLBA provides for a new type of financial holding company structure under which affiliations among these entities may occur. Under GLBA, a financial holding company may engage in a broad list of financial activities and any non-financial activity that the FRB determines is complementary to a financial activity and poses no substantial risk to the safety and soundness of depository institutions or the financial system. In addition, GLBA permitted certain non-banking financial and financially related activities to be conducted by financial subsidiaries of banks.

Under GLBA, a bank holding company may become certified as a financial holding company by filing a declaration with the FRB, together with a certification that each of its subsidiary banks is well capitalized, is well managed, and has at least a satisfactory rating under the Community Reinvestment Act of 1977 ("CRA"). The Company has elected to become a financial holding company under GLBA and the election was made effective by the FRB as of March 13, 2000. During the second quarter of 2000, IBC established an insurance agency subsidiary which acquired two insurance agencies. As part of the Local Financial Corporation ("LFIN") acquisition in 2004, the Company acquired a securities firm registered under the Exchange Act, IBC Investments, Inc. A financial holding company that has a securities affiliate registered under the Act or a qualified insurance affiliate may make permissible merchant banking investments. As of December 31, 2010, the Company has made 27 merchant banking investments. The Dodd-Frank Act requires that bank holding companies must be "well-capitalized" and "well-managed" in order to engage in the expanded financial activities permissible for financial holding companies under GLBA.

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The FRB and the Secretary of the Treasury have regulations governing the scope of permissible merchant banking investments. The investments that may be made under this authority are substantially broader in scope than the investment activities otherwise permissible for bank holding companies, and are referred to as "merchant banking investments" in "portfolio companies." Before making a merchant banking investment, a financial holding company must either be or have a securities affiliate registered under the Exchange Act or a qualified insurance affiliate. The merchant banking investments may be made by the financial holding company or any of its subsidiaries, other than a depository institution or subsidiary of a depository institution. The regulations place restrictions on the ability of a financial holding company to become involved in the routine management or operation of any of its portfolio companies. The regulation also generally limits the ownership period of merchant banking investments to no more than ten years.

The FRB, the Office of the Comptroller of the Currency (the "OCC"), and the FDIC have rules governing the regulatory capital treatment of equity investments in non-financial companies held by banks, bank holding companies and financial holding companies. The rule applies a graduated capital charge on covered equity investments which would increase as the proportion of such investments to Tier 1 Capital increases.

PREEMPTION. At the beginning of 2004, the OCC issued final rules clarifying when federal law overrides state law for national banks and their operating subsidiaries and confirming that only the OCC has the right to examine and take enforcement action against those institutions. However, the Dodd-Frank Act limits the applicability of the preemption doctrine so that state laws affecting national banks are preempted only in certain circumstances.

FINANCIAL PRIVACY. The federal banking regulators adopted rules that limit the ability of banks and other financial institutions to disclose non-public information about consumers to non-affiliated third parties. Pursuant to the rules, financial institutions must provide disclosure of privacy policies to consumers and in some instances allow consumers to prevent disclosure of certain personal information to a nonaffiliated third party. These privacy provisions affect how customer information is transmitted through diversified financial companies and conveyed to outside vendors.

NASDAQ LISTING STANDARDS. The Company is traded on the NASDAQ Stock Market. The Company must comply with the listing standards of the NASDAQ Stock Market. In addition to other matters, the listing standards address disclosure requirements and standards relating to board independence and other corporate governance matters.

INTERSTATE BANKING. The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 ("Interstate Banking Act"), rewrote federal law governing the interstate expansion of banks in the United States. Under the Interstate Banking Act, adequately capitalized, well managed bank holding companies with FRB approval may acquire banks located in any State in the United States, provided that the target bank meets the minimum age (up to a maximum of five years, which is the maximum Texas has adopted) established by the host State. Under the Interstate Banking Act, an anti-concentration limit will bar interstate acquisitions that would give a bank holding company control of more than ten percent (10%) of all deposits nationwide or thirty percent (30%) of any one State's deposits, or such higher or lower percentage established by the host State. The anti-concentration limit in Texas has been set at twenty percent (20%) of all federally insured deposits in Texas. As allowed by the Interstate Banking Act, the Company acquired LFIN, including its Oklahoma financial institution, during 2004. The Dodd-Frank Act changes the requirements for interstate branching by permitting de novo interstate branching if, under the laws of the state where the new branch is to be established, a state bank chartered in that state would be permitted to establish a branch.

FRB ENFORCEMENT POWERS. The FRB has certain cease-and-desist and divestiture powers over bank holding companies and non-banking subsidiaries where their actions would constitute a serious threat to the safety, soundness or stability of a subsidiary bank. These powers may be exercised

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through the issuance of cease-and-desist orders or other actions. In the event a bank subsidiary experiences either a significant loan loss or rapid growth of loans or deposits, the Company may be compelled by the FRB to invest additional capital in the bank subsidiary. Further, the Company would be required to guaranty performance of the capital restoration plan of any undercapitalized bank subsidiary. The FRB is also empowered to assess civil money penalties against companies or individuals who violate the BHCA in amounts up to \$1,000,000 per day, to order termination of non-banking activities of non-banking subsidiaries of bank holding companies and to order termination of ownership and control of a non-banking subsidiary. Under certain circumstances the Texas Banking Commissioner may bring enforcement proceedings against a bank holding company in Texas.

COMPANY DIVIDENDS. The Company is subject to regulatory policies and requirements relating to the payment of dividends, including requirements to maintain adequate capital above regulatory minimums. The FRB is authorized to determine under certain circumstances relating to the financial condition of a bank holding company, that the payment of dividends would be an unsafe or unsound practice and to prohibit payment thereof. In addition, in the current financial and economic environment, the FRB has indicated that bank holding companies should carefully review their dividend policy and has discouraged payment ratios that are at maximum allowable levels unless both asset quality and capital are very strong.

CROSS-GUARANTEE PROVISIONS. The Financial Institutions Reform Recovery and Enforcement Act of 1989 ("FIRREA") contains a "cross-guarantee" provision which generally makes commonly controlled insured depository institutions liable to the FDIC for any losses incurred in connection with the failure of a commonly controlled depository institution.

SOURCE OF STRENGTH DOCTRINE. FRB policy has historically required bank holding companies to act as a source of financial and managerial strength to their subsidiary banks. The Dodd-Frank Act codifies this policy as a statutory requirement. Under this requirement, the Company is expected to commit resources to support its subsidiary banks, including at times when the Company may not be in a financial position to provide such resources. Any capital loans by a bank holding company to any of its subsidiary banks are subordinate in right of payment to deposits and to certain other indebtedness of such subsidiary banks. In the event of a bank holding Company's bankruptcy, any commitment by the bank holding company to a federal bank regulatory agency to maintain the capital of a subsidiary bank will be assumed by the bankruptcy trustee and entitled to priority of payment.

GENERAL—BANK SUBSIDIARIES. All of the bank subsidiaries of the Company are state banks subject to regulation by, and supervision of, the Texas DOB and the FDIC.

DEPOSIT INSURANCE. All of the bank subsidiaries of the Company are examined by the FDIC, which currently insures the deposits of each member bank up to applicable limits. Deposits of each of the bank subsidiaries are insured by the FDIC through the DIF to the extent provided by law. The FDIC uses a risk-based assessment system that imposes premiums based upon a matrix that takes into account a bank's capital level and supervisory rating. As of January 1, 2007, the previous nine risk categories utilized in the risk matrix were condensed into four risk categories which continue to be distinguished by capital levels and supervisory ratings. During 2007, the bank subsidiaries of the Company were required to pay deposit insurance premiums. Under the Federal Deposit Insurance Reform Act of 2005, which became law in 2006, the bank subsidiaries of the Company received a one-time assessment credit that can be applied against future premiums, subject to certain limitations. During 2009, the remaining credit was used to offset a portion of the deposit insurance premiums owed by the bank subsidiaries of the Company. During 2009, the bank subsidiaries of the Company paid Financing Corporation ("FICO") assessments related to outstanding FICO bonds to the FDIC as a collection agent. The FICO is a mixed-ownership government corporation whose sole purpose was to serve as a financing vehicle for the defunct Federal Savings & Loan Insurance Corporation.

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In December 2008, the FDIC issued a final rule that raised the then current assessment rates uniformly by 7 basis points for the first quarter of 2009 assessment, which resulted in annualized assessment rates for institutions, such as the Subsidiary Banks in Risk Category 1 ("Risk Category 1 institutions"), ranging from 12 to 14 basis points (basis points representing cents per \$100 of assessable deposits). In February 2009, the FDIC issued final rules to amend the DIF restoration plan, change the risk-based assessment system and set assessment rates for Risk Category 1 institutions beginning in the second quarter of 2009. The initial base assessment rates for Risk Category 1 institutions range from 12 to 16 basis points, on an annualized basis. After the effect of potential base-rate adjustments, total base assessment rates range from 7 to 24 basis points.

In May 2009, the FDIC issued a final rule which levied a special assessment applicable to all insured depository institutions totaling 5 basis points of each institution's total assets, less Tier 1 capital, as of June 30, 2009, not to exceed 10 basis points of domestic deposits. The special assessment was part of the FDIC's efforts to rebuild the DIF. Deposit insurance expenses for the Subsidiary Banks during 2009 included \$5.1 million accrued in the second quarter related to the special assessment.

In November 2009, the FDIC issued a rule that required all deposit institutions, with limited exceptions, to prepay their estimated quarterly risk-based assessments for the fourth quarter of 2009, and for all of 2010, 2011, and 2012. As of December 31, 2010, \$27.6 million in pre-paid risk-based assessments is included in other assets in the accompanying consolidated balance sheet.

In October 2010, the FDIC adopted a new DIF restoration plan to ensure that the fund reserve ratio reaches 1.35% by September 30, 2020, as required by the Dodd-Frank Act. Under the new restoration plan, the FDIC will forego the uniform three-basis point increase in initial assessment rates scheduled to take place on January 1, 2011, and maintain the current schedule of assessment rates for all depository institutions. At least semi-annually, the FDIC will update its loss and income projections for the fund and, if needed, will increase or decrease assessment rates, following notice-and-comment rulemaking if required.

In November 2010, the FDIC issued a final rule to implement provisions of the Dodd-Frank Act that provide for temporary unlimited coverage for non-interest bearing transaction accounts. The separate coverage for non-interest bearing transaction accounts became effective on December 31, 2010 and terminates on December 31, 2012.

In February 2011, the FDIC issued a final rule effective April 1, 2011 that set a target size for the insurance fund and changed the deposit insurance assessment base from total domestic deposits to average total assets minus average tangible equity, as required by the Dodd-Frank Act. The rule finalizes a target size for the DIF at 2 percent of insured deposits. It also implements a lower assessment rate schedule when the fund reaches 1.15 percents and, in lieu of dividends, provides for a lower rate schedule when the reserve ratio reaches 2 percent and 2.5 percent. The final rule creates a risk-based scorecard assessment system for banks with more than \$10 billion in assets. The scorecards include financial measures that the FDIC believes are predictive of long-term performance. While the final rule is expected to be revenue neutral, it is possible that the rule will change the Company's overall FDIC assessment. The Company cannot provide any assurance as to the effect of any further change in its deposit insurance premium rate, should such a change occur, as such changes are dependent upon a variety of factors, some of which are beyond the Company's control.

Under the FDIA, the FDIC may terminate deposit insurance upon a finding that the institution has engaged in unsafe and unsound practices, is in an unsafe or uninsured condition to continue operations, or has violated any applicable law, regulation, rule or order of condition imposed by the FDIC.

CAPITAL ADEQUACY. The Company and its bank subsidiaries are currently required to meet certain minimum regulatory capital guidelines utilizing total capital-to-risk-weighted assets and Tier 1

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Capital elements. The guidelines make regulatory capital requirements more sensitive to differences in risk profiles among banking organizations, consider off-balance sheet exposure in assessing capital adequacy, and encourage the holding of liquid, low-risk assets. At least one-half of the minimum total capital must be comprised of Core Capital or Tier 1 Capital elements. Tier 1 Capital of the Company is comprised of common shareholders' equity and permissible amounts related to the trust preferred securities. The deductible core deposit intangibles and goodwill booked in connection with all the financial institution acquisitions of the Company after February 1992 are deducted from the sum of core capital elements when determining the capital ratios of the Company.

In addition, the FRB has established minimum leverage ratio guidelines for bank holding companies. These guidelines provide for a minimum leverage ratio of Tier 1 capital to adjusted average quarterly assets ("leverage ratio") equal to three percent for bank holding companies that meet certain specified criteria, including having the highest regulatory rating. All other bank holding companies will generally be required to maintain a leverage ratio of at least four to five percent. The Company's leverage ratio at December 31, 2010 was 11.58%. The guidelines also provide that bank holding companies experiencing internal growth or making acquisitions will be expected to maintain strong capital positions substantially above the minimum supervisory levels without significant reliance on intangible assets. Furthermore, the guidelines indicate that the FRB will continue to consider a "tangible tier 1 leverage ratio" (deducting all intangibles) in evaluating proposals for expansion or new activity. The FRB has not advised the Company of any specific minimum leverage ratio or tangible Tier 1 leverage ratio applicable to it. For a bank holding company to be considered "well-capitalized" under the regulatory framework for prompt corrective action, its leverage ratio must be at least 5.0%.

Each of the Company's bank subsidiaries is subject to similar capital requirements adopted by the FDIC. Each of the Company's bank subsidiaries had a leverage ratio in excess of five percent as of December 31, 2010. As of that date, the federal banking agencies had not advised any of the bank subsidiaries of any specific minimum leverage ratio applicable to it.

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.

Effective December 19, 1992, the federal bank regulatory agencies adopted regulations which mandate a five-tier scheme of capital requirements and corresponding supervisory actions to implement the prompt corrective action provisions of FDICIA. The regulations include requirements for the capital categories that will serve as benchmarks for mandatory supervisory actions. Under the regulations, the highest of the five categories would be a well capitalized institution with a total

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risk-based capital ratio of 10%, a Tier 1 risk-based capital ratio of 6% and a Tier 1 leverage ratio of 5%. An institution would be prohibited from declaring any dividends, making any other capital distribution or paying a management fee if the capital ratios drop below the levels for an adequately capitalized institution, which are 8%, 4% and 4%, respectively. The corresponding provisions of FDICIA mandate corrective actions are taken if a bank is undercapitalized. Based on the Company's and each of the bank subsidiaries' capital ratios as of December 31, 2010, the Company and each of the bank subsidiaries were classified as "well capitalized" under the applicable regulations.

The risk-based standards that apply to bank holding companies and banks incorporate market and interest rate risk components. Applicable banking institutions are required to adjust their risk-based capital ratio to reflect market risk. Under the market risk capital guidelines, capital is allocated to support the amount of market risk related to a financial institution's ongoing trading activities. Financial institutions are allowed to issue qualifying unsecured subordinated debt (Tier 3 capital) to meet a part of their market risks. The Company does not have any Tier 3 capital and did not need Tier 3 capital to offset market risks. In January 2010, the federal bank regulators issued a final risk-based capital rule related to new accounting standards that make substantive changes in how banking organizations account for more items, including securitized assets that previously had been taken off banks' balance sheets. Dodd-Frank directs the banking agencies to issue capital requirements for banking institutions that are countercyclical. These will require a higher level of capital to be maintained in times of economic expansion and a lower level of capital during times of economic contraction.

The federal regulatory authorities' risk-based capital guidelines are based upon the 1988 capital accord of the Basel Committee on Banking Supervision (the "BIS"). The BIS is a committee of central banks and bank supervisors/regulators from the major industrialized countries that develops broad policy guidelines for use by each country's supervisors in determining the supervisory policies they apply. In June 2004, the BIS released a new capital accord to replace the 1988 capital accord with an update in November 2005 ("BIS II"). BIS II would set capital requirements for operational risk, and refine the existing capital requirements for credit risk and market risk exposures. The United States federal banking agencies are developing proposed revisions to their existing capital adequacy regulations and standards based on BIS II. A definitive final rule for implementing BIS II in the United States that would apply only to internationally active banking organizations, or "core banks"—defined as those with consolidated total assets of \$250 billion or more or consolidated on-balance sheet foreign exposures of \$10 billion or more became effective as of April 1, 2008. Other U.S. banking organizations may elect to adopt the requirements of this rule (if they meet applicable qualification requirements), but they will not be required to apply them. The rule also allows a banking organization's primary federal supervisor to determine that the application of the rule would not be appropriate in light of the bank's asset size, level of complexity, risk profile, or scope of operations. The Company is not required to comply with BIS II at this time.

In July 2008, the banking agencies issued a proposed rule that would give banking organizations that are not required to comply with Basel II the option to implement a new risk-based capital framework. This framework would adopt the standardized approach of Basel II for credit risk, the basic indicator approach of Basel II for operational risk, and related disclosure requirements. While this proposed rule generally parallels the relevant approaches under Basel II, it diverges where United States markets have unique characteristics and risk profiles, most notably with respect to risk weighting residential mortgage exposures. Comments on the proposed rule were due to the agencies by October 27, 2008, but a definitive final rule has not been issued.

The Dodd-Frank Act requires the Federal Reserve Board, the OCC and the FDIC to adopt regulations imposing a continuing "floor" of the BIS risk-based capital requirements in cases where the BIS risk-based capital requirements and any changes in capital regulations resulting from Basel-III (see below) otherwise would permit lower requirements. In December 2010, the Federal Reserve Board, the

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OCC and the FDIC issued a joint notice of proposed rulemaking that would implement this requirement.

In December 2010, the Basel Committee released its final framework for strengthening international capital and liquidity regulation, now officially identified by the Basel Committee as "Basel III." Basel III, when implemented by the U.S. banking agencies and fully phased-in, will require bank holding companies and their bank subsidiaries to maintain substantially more capital, with a greater emphasis on common equity.

The Basel III final capital framework, among other things, (i) introduces as a new capital measure "Common Equity Tier 1" ("CET1"), (ii) specifies that Tier 1 capital consists of CET1 and "Additional Tier 1 capital" instruments meeting specified requirements, (iii) defines CET1 narrowly by requiring that most adjustments to regulatory capital measures be made to CET1 and not to the other components of capital and (iv) expands the scope of the adjustments as compared to existing regulations.

Basel III also provides for a "countercyclical capital buffer," generally to be imposed when national regulators determine that excess aggregate credit growth becomes associated with a buildup of systemic risk. The capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a ratio of CET1 to risk-weighted assets above the minimum but below the conservation buffer will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall.

The U.S. banking agencies have indicated informally that they expect to propose regulations implementing Basel III in mid-2011 with final adoption of implementing regulations in mid-2012. Notwithstanding its release of the Basel III framework as a final framework, the Basel Committee is considering further amendments to Basel III, including the imposition of additional capital surcharges on globally systemically important financial institutions. In addition to Basel III, Dodd-Frank requires or permits the Federal banking agencies to adopt regulations affecting banking institutions' capital requirements in a number of respects, including potentially more stringent capital requirements for systemically important financial institutions. Accordingly, the regulations ultimately applicable to the Company may be substantially different from the Basel III final framework as published in December 2010. Requirements to maintain higher levels of capital or to maintain higher levels of liquid assets could adversely impact the Company's net income and return on equity.

LIQUIDITY REQUIREMENTS. Historically, regulation and monitoring of bank and bank holding company liquidity has been addressed as a supervisory matter, without required formulaic measures. The Basel III final framework requires banks and bank holding companies to measure their liquidity against specific liquidity tests that, although similar in some respects to liquidity measures historically applied by banks and regulators for management and supervisory purposes, going forward will be required by regulation. These new standards are subject to further rulemaking and their terms may well change before implementation.

STATE ENFORCEMENT POWERS. The Banking Commissioner of Texas may determine to close a Texas state bank when he finds that the interests of depositors and creditors of a state bank are jeopardized through its insolvency or imminent insolvency and that it is in the best interest of such depositors and creditors that the bank be closed. The Texas DOB also has broad enforcement powers over the bank subsidiaries, including the power to impose orders, remove officers and directors, impose fines and appoint supervisors and conservators.

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DEPOSITOR PREFERENCE. Because the Company is a legal entity separate and distinct from its bank subsidiaries, its right to participate in the distribution of assets of any subsidiary upon the subsidiary's liquidation or reorganization will be subject to the prior claims of the subsidiary's creditors. In the event of a liquidation or other resolution of a subsidiary bank, the claims of depositors and other general or subordinated creditors of the bank are entitled to a priority of payment over the claims of holders of any obligation of the institution to its shareholders, including any depository institution holding company (such as the Company) or any shareholder or creditor thereof.

CRA. Under the CRA, the FDIC is required to assess the record of each bank subsidiary to determine if the bank meets the credit needs of its entire community, including low and moderate-income neighborhoods served by the institution, and to take that record into account in its evaluation of any application made by the bank for, among other things, approval of the acquisition or establishment of a branch or other deposit facility, an office relocation, a merger, or the acquisition of shares of capital stock of another financial institution. The FDIC prepares a written evaluation of an institution's record of meeting the credit needs of its entire community and assigns a rating. The FIRREA requires federal banking agencies to make public a rating of a bank's performance under the CRA. The Company's bank subsidiaries conduct an award-winning financial literacy program in their communities as part of their community outreach. Further, there are fair lending laws, including the Equal Credit Opportunity Act and the Fair Housing Act, which prohibit discrimination in connection with lending decisions. The bank regulators periodically conduct fair lending evaluations of banks and IBC is currently undergoing such an evaluation. Three of the subsidiary banks of the Company received a "Satisfactory" CRA rating in its most recently completed examination; however, in February 2011, IBC received a "Needs to Improve" CRA rating as a result of alleged fair lending issues associated with mortgage origination activities of IBC in prior years. Unless and until IBC's CRA rating improves, IBC will be ineligible for expedited treatment and is unlikely to receive approval for branch, merger, and acquisition applications and IBC and the Company will be subject to certain other regulatory limitations.

CONSUMER LAWS. In addition to the laws and regulations discussed herein, the Bank is also subject to numerous consumer laws and regulations that are designed to protect consumers in transactions with banks. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must deal with customers when taking deposits or making loans to such customers. The Bank must comply with the applicable provisions of these consumer protection laws and regulations as part of their ongoing customer relations. The Dodd-Frank Act provides for comprehensive new rules regulating mortgage activities and creates a new Bureau of Consumer Financial Protection (the "CFPB"). Authority to implement almost all federal consumer financial protection laws will be transferred to the CFPB. The CFPB will have broad authority, among other matters, to declare acts or practices to be "unfair, deceptive, or abusive," to require consumer disclosures and to restrict the use of certain arbitration clauses.

AFFILIATE TRANSACTIONS. The Company, IBC and the other bank subsidiaries of the Company are "affiliates" within the meaning of Section 23A of the Federal Reserve Act which sets forth certain restrictions on loans and extensions of credit between a bank subsidiary and affiliates, on investments in an affiliate's stock or other securities, and on acceptance of such stock or other securities as collateral for loans. Such restrictions prevent a bank holding company from borrowing from any of its bank subsidiaries unless the loans are secured by specific obligations. Further, such secured loans and investments by a bank subsidiary are limited in amount, as to a bank holding company or any other affiliate, to 10% of such bank subsidiary's capital and surplus and, as to the bank holding company and its affiliates, to an aggregate of 20% of such bank subsidiary's capital and surplus. Certain restrictions do not apply to 80% or more owned sister banks of bank holding companies. Each bank subsidiary of the Company is wholly-owned by the Company. Section 23B of the Federal Reserve Act requires that the terms of affiliate transactions be comparable to terms of similar non-affiliate

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transactions. The Dodd-Frank Act expands the limitation on affiliate transactions, it will require that the 10% of capital limit on covered transactions begin to apply to non-bank financial subsidiaries. "Covered transactions" are defined by statute to include a loan or extension of credit, as well as a purchase of securities issued by an affiliate, a purchase of assets (unless otherwise exempted by the Federal Reserve Board) from the affiliate, the acceptance of securities issued by the affiliate as collateral for a loan, and the issuance of a guarantee, acceptance or letter of credit on behalf of an affiliate.

INSIDER LOANS. The restrictions on loans to directors, executive officers, principal shareholders and their related interests (collectively referred to herein as "insiders") contained in the Federal Reserve Act and Regulation O apply to all insured institutions and their subsidiaries and holding companies. These restrictions include limits on loans to one borrower, prohibition on preferential terms, and other conditions that must be met before such a loan can be made. There is also an aggregate limitation on all loans to insiders and their related interests. These loans cannot exceed the institution's total unimpaired capital and surplus, and the FDIC may determine that a lesser amount is appropriate. Insiders are subject to enforcement actions for knowingly accepting loans in violation of applicable restrictions.

LENDING RESTRICTIONS. The operations of the Banks are also subject to lending limit restrictions pertaining to the extension of credit and making of loans to one borrower. Further, under the BHCA and the regulations of the FRB thereunder, the Company and its subsidiaries are prohibited from engaging in certain tie-in arrangements with respect to any extension of credit or provision of property or services; however, the FRB adopted a rule relaxing tying restrictions by permitting a bank holding company to offer a discount on products or services if a customer obtains other products or services from such company. In February 2005, the banking agencies issued best practices guidelines on overdraft protection programs which state that overdraft protection programs are an extension of credit, but are not subject to Truth-in-Lending disclosure requirements. On November 12, 2009, the FRB issued final rules amending Regulation E that prohibit financial institutions from charging consumer fees for paying overdrafts on ATM and on-time debit card transactions, unless the consumer consents or opts-in to the overdraft service for those types of transactions.

DIVIDENDS. The ability of the Company to pay dividends is largely dependent on the amount of cash derived from dividends declared by its bank subsidiaries. The payment of dividends by any bank or bank holding company is affected by the requirement to maintain adequate capital as discussed above. The ability of the Banks, as Texas banking associations, to pay dividends is restricted under Texas law. A Texas bank generally may not pay a dividend reducing its capital and surplus without the prior approval of the Texas Banking Commissioner. The FDIC has the right to prohibit the payment of dividends by a bank where the payment is deemed to be an unsafe and unsound banking practice. Additionally, as a result of the Company's participation in the CPP, 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 Preferred Stock issued as part of the CPP program or the date on which the Treasury has transferred all of the Preferred Stock to third parties not affiliated with the Treasury. At December 31, 2010, there was an aggregate of approximately \$465,000,000 available for the payment of dividends to the Company by IBC, Commerce Bank, IBC-Zapata and IBC-Brownsville under the applicable restrictions, assuming that each of such banks continues to be classified as "well capitalized." Further, the Company could expend the entire \$465,000,000 and continue to be classified as "well capitalized". Note 20 of Notes to Consolidated Financial Statements of the Company in the 2010 Annual Report is incorporated herein by reference.

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POWERS. As a result of FDICIA, the authority of the FDIC over state-chartered banks was expanded. FDICIA limits state-chartered banks to only those principal activities permissible for national banks, except for other activities specifically approved by the FDIC. The new Texas Banking Act includes a parity provision which establishes procedures for state banks to notify the Banking Commissioner if the bank intends to conduct any activity permitted for a national bank that is otherwise denied to a state bank. The Banking Commissioner has thirty (30) days to prohibit the activity. Also, the Texas Finance Code includes, a super parity provision with procedures for state banks to notify the Banking Commissioner if the bank intends to conduct any activity permitted for any depository institution in the United States. The Banking Commissioner has thirty (30) days to prohibit the activity.

INCENTIVE COMPENSATION. In June 2010, the Federal Reserve, OCC and FDIC issued a comprehensive final guidance on incentive compensation policies intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk-taking. The guidance, which covers all employees that have the ability to materially affect the risk profile of an organization, either individually or as part of a group, is based upon the key principles that a banking organization's incentive compensation arrangements should (i) provide incentives that do not encourage risk-taking beyond the organization's ability to effectively identify and manage risks, (ii) be compatible with effective internal controls and risk management, and (iii) be supported by strong corporate governance, including active and effective oversight by the organization's board of directors.

The Federal Reserve will review, as part of the regular, risk-focused examination process, the incentive compensation arrangements of banking organizations, such as the Company. These reviews will be tailored to each organization based on the scope and complexity of the organization's activities and the prevalence of incentive compensation arrangements. The findings of the supervisory initiatives will be included in reports of examination. Deficiencies will be incorporated into the organization's supervisory ratings, which can affect the organization's ability to make acquisitions and take other actions. Enforcement actions may be taken against a banking organization if its incentive compensation arrangements, or related risk-management control or governance processes, pose a risk to the organization's safety and soundness and the organization is not taking prompt and effective measures to correct the deficiencies.

The Dodd-Frank Act requires the federal banking agencies and the Securities and Exchange Commission to jointly prescribe regulations or guidelines that require financial institutions with \$1 billion or more in assets to disclose to the appropriate federal regulator, the structure of all incentive-based compensation arrangements sufficient to determine whether the compensation structure provides an executive officer, employee, director, or principal shareholder with excessive compensation, fees, or benefits, or could lead to material financial loss to the financial institutions. On February 7, 2011, the FDIC issued a notice of proposed rulemaking that would prohibit bank incentive-based compensation arrangements that encourage inappropriate risk taking, are deemed excessive, or may lead to material losses. The proposal would apply to financial institutions with more than \$1 billion in assets, like the Company. The rule also includes heightened standards for financial institutions with \$50 billion or more in total consolidated assets that requires at least 50 percent of incentive-based payments for designated executives to be deferred for a minimum of three years. The interagency rule must be approved by all of the five federal members of the FFIEC, the SEC and the Federal Housing Finance Agency before comments on the rule are sought.

Effective April 1, 2011, Regulation Z is amended to restrict incentive compensation programs with regard to residential mortgage programs. Such limitations affect mortgage brokers as well as loan officers in the subsidiary banks. Compensation may be tied to volume but not to terms or conditions of the transaction other than the amount of credit extended.

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The scope and content of the U.S. banking regulators' policies on executive compensation are continuing to develop and are likely to continue evolving in the near future. It cannot be determined at this time whether compliance with such policies will adversely affect the Company's ability to hire, retain and motivate its key employees.

LEGISLATIVE AND REGULATORY INITIATIVES. From time to time, various legislative and regulatory initiatives are introduced in Congress and state legislatures, as well as by regulatory agencies. Such initiatives may include proposals to expand or contract the powers of bank holding companies and depository institutions or proposals to substantially change the financial institution regulatory system. Such legislation could change banking statutes and the operating environment of the Company in substantial and unpredictable ways. Such changes could have a material effect on the business of the Company. The Company cannot predict whether any such changes will be adopted and the Company cannot determine the ultimate effect that potential legislation, if enacted, or implementing regulations with respect thereto, would have upon the financial condition or results of operations of the Company or its subsidiaries.

Item 1A. Risk Factors

Risk Factors

An investment in the Company's common stock is subject to risks inherent to the Company's business. Described below are the material risks and uncertainties that management believes may affect the Company. You should carefully consider the risks and uncertainties the Company describes below and the other information in this Annual Report or incorporated by reference before deciding to invest in, or retain, shares of the Company's common stock. These are not the only risks and uncertainties that the Company faces. Additional risks and uncertainties that the Company does not know about or that the Company currently believes are immaterial, or that the Company has not predicted, may also harm the Company's business operations or adversely affect the Company. If any of these risks or uncertainties actually occurs, the Company's business, financial condition, operating results or liquidity could be materially harmed. This report is qualified in its entirety by these risk factors.

Risks Related to the Company's Business

Losses from loan defaults may exceed the allowance the Company establishes for that purpose, which could have an adverse effect on the Company's business.

There are inherent risks associated with the Company's lending activities. Losses from loan defaults may exceed the allowance the Company establishes for that purpose. Like all financial institutions, the Company maintains an allowance for probable loan losses to provide for losses inherent in the loan portfolio. The allowance for probable loan losses reflects management's best estimate of loan losses in the loan portfolio at the relevant balance sheet date. The level of the allowance reflects management's continuing evaluation of the specific credit risks, the Company's historical loan loss experience, current loan portfolio quality, composition and growth of the loan portfolio, and economic, political and regulatory conditions and unidentified losses inherent in the current loan portfolio. The determination of an appropriate level of loan loss allowance is an inherently difficult process and is based on numerous assumptions. In addition, bank regulatory agencies periodically review the Company's allowance for loan losses and may require an increase in the provision for probable loan losses or the recognition of further loan charge-offs, based on judgments different than those of management. As a result, the Company's allowance for loan losses may not be adequate to cover actual losses, and future provisions for loan losses may adversely affect the Company's earnings. The Company believes its allowance for probable loan losses is adequate at December 31, 2010.

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If real estate values in the Company's target markets decline, the loan portfolio would be impaired.

A significant portion of the Company's loan portfolio consists of loans secured by real estate located in the markets served by the Company. Real estate values and real estate markets are generally affected by, among other things, changes in national, regional, or local economic conditions; fluctuations in interest rates and the availability of loans to potential purchases, changes in the tax laws and other governmental statutes, regulations, and policies; and acts of nature. If real estate prices decline significantly in any of these markets, the value of the real estate collateral securing the Company's loans would be reduced. Such a reduction in the value of the Company's collateral could increase the number of impaired loans and adversely affect the Company's financial performance.

The Company's subsidiary banks face strong competition in their market areas, which may limit their asset growth and profitability.

The Company's primary market areas are South, Central and Southeast Texas, including Austin and Houston, and the State of Oklahoma. The banking business in these areas is extremely competitive, and the level of competition facing the Company may increase further, which may limit the growth and profitability of the Company. Each of the Company's subsidiary banks experience competition in both lending and attracting funds from other banks, savings institutions, credit unions and non-bank financial institutions located within its market area, many of which are significantly larger institutions. Non-bank competitors competing for deposits and deposit type accounts include mortgage bankers and brokers, finance companies, credit unions, securities firms, money market funds, life insurance companies, and mutual funds. For loans, the Company encounters competition from other banks, savings associations, finance companies, mortgage bankers and brokers, insurance companies, small loan and credit card companies, credit unions, pension trusts, and securities firms. Many of the Company's competitors have fewer regulatory constraints and may have lower cost structures. Additionally, due to their size, many competitors may be able to achieve economies of scale and, as a result, may offer a broader range of products and services as well as better pricing for those products and services than the Company offers. Also, technology and other changes are allowing parties to complete financial transactions that historically have involved banks through alternative methods. The process of eliminating banks as intermediaries could result in the loss of fee income, as well as the loss of customer deposits and the related income generated from those deposits. The loss of revenue streams and the reduction of lower cost deposits as a source of funds could have a material adverse affect on the Company's financial condition and results of operations.

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.

The Company relies on deposits, repurchase agreements, advances from the Federal Home Loan Bank ("FHLB") of Dallas and other borrowings to fund its operations. The subsidiary banks have also historically relied on certificates of deposit. While the Company has reduced its reliance on certificates of deposit and has been successful in promoting its transaction and non-transaction deposit products (demand deposit accounts, money market, savings and checking), jumbo deposits nevertheless constituted a large portion of total deposits at December 31, 2010. Jumbo deposits tend to be a more volatile source of funding. Although management has historically been able to replace such deposits on maturity if desired, no assurance can be given that the Company would be able to replace such funds at any given point in time.

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The Company's business is subject to interest rate risk and variations in interest rates may negatively affect the Company's financial performance.

The Company is unable to predict fluctuations of market interest rates, which are affected by many factors, including:

- Inflation;
- Recession;
- Changes in consumer spending, borrowing and saving habits;
- A rise in unemployment;
- Tightening of the money supply; and
- Domestic and international disorder and instability in domestic and foreign financial markets.

Changes in the interest rate environment may reduce the Company's profits. The Company expects that the bank subsidiaries will continue to realize income from the differential or "spread" between the interest earned on loans, securities and other interest-earning assets, and the interest paid on deposits, borrowings and other interest-bearing liabilities. Net interest spreads are affected by the difference between the maturities and repricing characteristics of interest-earning assets and interest-bearing liabilities. Earnings could be adversely affected if the net interest spreads are reduced. Changes in interest rates and other factors could result in write downs of carrying values of securities held in our securities available-for-sale portfolio and such changes could reduce earnings of the Company.

The Company is subject to extensive regulation which could adversely affect the Company including, without limitation, changes in U.S.—Mexico trade and travel along the Texas border.

The Company's operations are subject to extensive regulation by federal, state and local governmental authorities and are subject to various laws and judicial and administrative decisions imposing requirements and restrictions on part or all of the Company's operations. Because the Company's business is highly regulated, the laws, rules and regulations applicable to the Company are subject to regular modification and change. There can be no assurance that there will be no laws, rules or regulations adopted in the future, or changes in accounting policies and practices, which could make compliance more difficult or expensive, or otherwise adversely affect the Company's business, financial condition or prospects. The Dodd-Frank Act, enacted in July 2010, instituted major changes to the banking and financial institutions regulatory regimes. These changes and other changes to statutes and regulations, including changes in the interpretation or implementation of statutes, regulations or policies, could affect the Company in substantial and unpredictable ways. Such changes could subject the Company to additional costs, limit the types of financial services and products the Company may offer and/or increase the ability of non-banks to offer competing financial services and products, among other things. Failure to comply with laws, regulations or policies could result in sanctions by regulatory agencies, civil money penalties and/or reputation damage, which could have a material adverse effect on the Company's business, financial condition and results of operations. Additionally, any 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 Immigration Responsibility Act of 1996 could affect the Company negatively, and any possible negative consequences from an adverse immigration law could also have a negative effect on the Company's operations.

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The Company's potential future acquisitions and branch expansion could be adversely affected by a number of factors.

Acquisitions of other financial institutions and branch expansion have been a key element of the Company's growth. There are a number of factors that may impact the ability of the Company to continue to grow through acquisition transactions, including strong competition from other financial institutions who are active or potential acquirers of financial institutions in the existing or future markets of the Company. Acquisitions of other financial institutions and new branches must be approved by bank regulators and such approvals are dependent on many factors, including the results of regulatory examinations and CRA ratings. Unless and until IBC's CRA rating improves, the inability to receive regulatory approvals for proposed acquisitions and branch expansions could adversely affect the future growth and prospects of the Company.

The Company relies heavily on its chief executive officer.

The Company has experienced substantial growth in assets and deposits during the past, particularly since Dennis E. Nixon became our President in 1979. Although Mr. Nixon is the chief executive officer and one of the Company's substantial shareholders, the Company does not have an employment agreement with Mr. Nixon and the loss of his services could have a material adverse effect on the Company's business and prospects.

System failure or breaches of our network security could subject us to increased operating costs as well as litigation and other liabilities.

The computer systems and network infrastructure our Company uses could be vulnerable to unforeseen problems. Our operations are dependent upon our ability to protect our computer equipment against damage from fire, power loss, telecommunications failure or a similar catastrophic event. Any damage or failure that causes an interruption in our operations could have an adverse effect on our customers. In addition, we must be able to protect the computer systems and network infrastructure utilized by us against physical damage, security breaches and service disruption caused by the Internet or other users. Such computer break-ins and other disruptions would jeopardize the security of information stored in and transmitted through our computer systems and network infrastructure, which may result in significant liability to us. While the Company conducts its own data processing, it is reliant on certain external vendors to provide products and services necessary to maintain day-to-day operations of the Company. Accordingly, the Company's operations are exposed to risks that these vendors will not perform in accordance with contracted arrangements and in a manner that adequately protects the operations of the Company.

The Company may desire or need to raise additional capital in the future, and such capital may not be available when needed or at all.

The Company may desire or need to raise additional capital in the future to provide it with sufficient capital resources and liquidity to meet its commitments and business needs, particularly if its asset quality or earnings were to deteriorate significantly. The Company's ability to raise additional capital, if needed, will depend on, among other things, conditions in the capital markets at that time, which are outside of its control, and the Company's financial performance. The Company cannot assure that such capital will be available on acceptable terms or at all. If the Company needs to raise capital in the future, it may have to do so when many other financial institutions are also seeking to raise capital and would have to compete with those institutions for investor. An inability to raise additional capital on acceptable terms when needed could have a materially adverse effect on the Company's businesses, financial condition and results of operations.

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Severe weather, natural disasters, acts of war or terrorism and other external events could significantly impact the Company's business.

Severe weather, natural disasters, acts of war or terrorism and other adverse external events could have a significant impact on the Company's ability to conduct business. In addition, such events could affect the stability of the Company's deposit base, impair the ability of borrowers to repay outstanding loans, impair the value of collateral securing loans, cause significant property damage, result in loss of revenue and cause the Company to incur additional expenses. Although management has established disaster recovery policies and procedures, the occurrence of any such event in the future could have a material adverse effect on the Company's business.

An impairment in the carrying value of our goodwill could negatively impact our earnings and capital.

Goodwill is initially recorded at fair value and is not amortized, but is reviewed for impairment at least annually or more frequently if events or changes in circumstances indicate that the carrying value may not be recoverable. Given the current economic environment and conditions in the financial markets, we could be required to evaluate the recoverability of goodwill prior to our normal annual assessment if we experience disruption in our business, unexpected significant declines in our operating results, or sustained market capitalization declines. These types of events and the resulting analyses could result in goodwill impairment charges in the future, which would be recorded as charges against earnings. The decrease in earnings resulting from impairment charges could also negatively impact other performance measures; however, for regulatory purposes, goodwill is eliminated in calculating the Company's regulatory ratios such as its regulatory capital ratios. We performed an annual goodwill impairment assessment as of October 1, 2010. Based on our analyses, we concluded that the fair value of our reporting units exceeded the carrying value of our assets and liabilities and, therefore, goodwill was not considered impaired. Depending on the response of the financial industry to the legal, regulatory and competitive changes related to interchange fees, overdraft services and interest on demand deposit accounts, financial institutions may need to change their policies, procedures and operating plans in the future to compete more effectively and such changes may require certain financial institutions to take a goodwill impairment charge to account for anticipated reduction in revenue related to such changes.

The Company Is Subject To Environmental Liability Risk Associate With Lending Activities.

A significant portion of the Company's loan portfolio is secured by real property. During the ordinary course of business, the Company may foreclose on and take title to properties securing certain loans. In doing so, there is a risk that hazardous or toxic substances could be found on these properties. If hazardous or toxic substances are found, the Company may be liable for remediation costs, as well as for personal injury and property damage. Environmental laws may require the Company to incur substantial expenses and may materially reduce the affected property's value or limit the Company's ability to use or sell the affected property. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase the Company's exposure to environmental liability. The remediation costs and any other financial liabilities associated with an environmental hazard could have a material adverse effect on the Company's financial condition and results of operations.

The Company's Controls and Procedures May Fail or be Circumvented

Management regularly reviews and updates the Company's internal controls, disclosure controls and procedures and corporate governance policies and procedures. Any system of controls, however well designed and operated, is based in part on certain assumptions and can provide only reasonable, not absolute, assurances that the objectives of the system are met. Any failure or circumvention of the Company's controls and procedures or failure to comply with regulations related to controls and

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procedures could have a material adverse effect on the Company's business, results of operations and financial condition.

New Lines of Business or New Products and Services May be Subject the Company to Additional Risks

From time to time, the Company may implement new lines of business or offer new products and services within existing lines of business. There are substantial risks and uncertainties associated with these efforts, particularly in instances where the markets are not fully developed. In developing and marketing new lines of business and/or new products and services, the Company may invest significant time and resources. Initial timetables for the introduction and development of new lines of business and/or new products may not be achieved and price and profitability targets may not prove feasible. Compliance with regulations, competitive alternatives, and shifting market preferences, may also impact the successful implementation of a new line of business or a new product or service. Failure to successfully manage these risks in the development and implementation of new lines of business or new products or services could have a material adverse effect on the Company's business, results of operations and financial condition.

Risks Related to the Company's Industry

Changes in economic and political conditions could adversely affect the Company's earnings, as our borrowers' ability to repay loans and the value of the collateral securing our loans decline.

The Company's success depends, to a certain extent, upon economic and political conditions, local, national and international with respect to Mexico, as well as governmental monetary policies. Conditions such as inflation, recession, unemployment, changes in interest rates, changes in capital markets, money supply, political issues, legislative and regulatory changes and other factors beyond the Company's control may adversely affect the Company's asset quality, deposit levels and loan demand and, therefore, the Company's earnings. The Company is particularly affected by conditions in its primary market areas of South, Central and Southeast Texas, including Austin and Houston, and the State of Oklahoma. While economic conditions in the Company's primary markets have begun to improve, there is no assurance that the improvement will continue. If the weakened economic conditions in the Company's primary market areas worsen or fail to improve, the Company could experience an increase in loan delinquencies and non-performing assets, decreases in loan collateral values and a decrease in demand for the Company's products and services, any of which could have a material adverse impact on the Company's financial condition and results of operations.

The Company depends on the accuracy and completeness of information about customers and counterparties as well as the soundness of other financial institutions with which the Company interacts.

In deciding whether to extend credit or enter into other transactions, the Company may rely on information furnished by or on behalf of customers and counterparties, including financial statements, credit reports and other financial information. The Company may also rely on representations of those customers, counterparties, financial institutions or other third parties, such as independent auditors, as to the accuracy and completeness of that information. Reliance on inaccurate or misleading financial statements, credit reports or other financial information or problems with the soundness of other financial institutions with which the Company interacts could have a material adverse impact on the Company's business and, in turn, the Company's financial condition and results of operations.

If the Company does not adjust to rapid changes in the financial services industry, its financial performance may suffer.

The Company's ability to deliver strong financial performance and returns on investment to shareholders will depend in part on its ability to expand the scope of available financial services to

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meet the needs and demands of its customers and its ability to stay abreast of technological innovations and evaluate those technologies that will enable it to compete on a cost-effective basis.

In addition to the challenge of competing against other banks in attracting and retaining customers for traditional banking services, the Company's competitors also include securities dealers, brokers, mortgage bankers, investment advisors, specialty finance and insurance companies who seek to offer one-stop financial services that may include services that banks have not been able or allowed to offer to their customers in the past. The increasingly competitive environment is primarily a result of changes in regulation, changes in technology and product delivery systems and the accelerating pace of consolidation among financial service providers. Such changes in the financial industry may result in the loss of fee income, as well as the loss of customer deposits and the related income generated from those deposits. The loss of these revenue streams and the lower cost deposits as a source of funds could have a material adverse effect on the Company's financial condition and results of operations.

Further, the costs of new technology, including personnel, can be high in both absolute and relative terms. There can be no assurance, given the fast pace of change and innovation, that the Company's technology, either purchased or developed internally, will meet or continue to meet the needs of the Company and the needs of our customers.

The Recent Repeal of Federal Prohibitions on Payment of Interest on Demand Deposits Could Increase the Company's Interest Expense.

All federal prohibitions on the ability of financial institutions to pay interest on demand deposit accounts were repealed as part of the Dodd-Frank Act. As a result, beginning on July 21, 2011, financial institutions could commence offering interest on demand deposits to compete for clients. The Company does not yet know what interest rates other institutions may offer. The Company's interest expense will increase and its net interest margin will decrease if it begins offering interest on demand deposits to attract additional customers or maintain current customers, which could have a material adverse effect on the Company's business, financial condition and results of operations.

The Dodd-Frank Regulatory Reform Act and other regulatory developments could negatively impact the revenue streams of the Company related to interchange fees and consumer services and result in a contraction of retail banking of the Company.

The Dodd-Frank Reform Act authorizes the Federal Reserve to regulate interchange fees paid to banks on debit card transactions to ensure that they are reasonable and proportional to the cost of processing individual transactions, and prohibits debit card networks and issuers from requiring transactions to be processed on a single payment network. The impact of the FDIC Overdraft Payment Supervisory Guidance could jeopardize the profitability of a number of retail sites of the Company and could result in a reduction of revenue from the Company's overdraft courtesy services. The impact of these provisions on the Company's revenue from interchange fees and overdraft courtesy services is uncertain at this time and will depend upon Federal Reserve final implementing regulations and the implementation of the FDIC Overdraft Payment Supervisory Guidance. The Reform Act also creates a Consumer Finance Protection Bureau. While banks with less than \$10 billion in assets, such as each of the subsidiary banks of the Company, based on their asset size as of December 31, 2010, are exempt from the primary examination, and enforcement powers of the CFPA, it is expected that the new agency's rulemaking will affect all banks. The impact of the CFPA is uncertain at this time, but the initiatives of the CFPA could negatively impact revenue streams of the Company related to consumer services. The reduction of revenue from retail banking services coupled with the repeal of the federal prohibition on the payment of interest on demand deposits, could result in a contraction of retail banking of the Company.

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The limitation of preemption in the Dodd-Frank Reform Act, the powers of the new Consumer Financial Protection Bureau, and the FDIC Overdraft Payment Supervisory Guidance may increase the likelihood of lawsuits against financial institutions.

The Dodd-Frank Reform Act provides that courts must make preemption determinations on a case-by-case basis with the respect to particular state laws and can no longer rely on blanket preemption determinations. The new CFPB is specifically authorized to protect consumers from "unfair," "deceptive," and "abusive" acts and practices. Depending on the future actions of the CFPB, the likelihood of lawsuits against financial institutions related to allegedly "unfair," "deceptive" and "abusive" acts and practices could increase. Depending on the future actions of the FDIC Overdraft Payment Supervisory Guidance could result in an increase of lawsuits related to the overdraft courtesy services of financial institutions. There are already a number of lawsuits pending against financial institutions in multi-district proceedings known as "In re Checking Account Overdraft Litigation" related to the overdraft courtesy program of financial institutions. In the third quarter of 2010, IBC 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 in the multi-district proceeding. In January 2011, the Texas lawsuit was dismissed without prejudice when the parties stipulated to arbitrate the matter.

Risks Related to the Company's Stock

The Company's stock price may be volatile.

Several factors could cause the Company's stock price to fluctuate substantially in the future. These factors include among other things:

- Actual or anticipated variations in earnings;
- Recommendations by securities analysts;
- The Company's announcements of developments related to its businesses;
- Operating and stock performance of other companies deemed to be peers;
- New technology used or services offered by traditional and non-traditional competitors;
- Continued low trading volume in the Company's stock;
- The volatile impact of short selling activity in the Company's stock;
- News reports of trends, concerns and other issues related to the financial services industry; and
- Changes in the Company's ability to pay dividends;
- Changes in government regulations, policies and guidance.

The Company's stock price may fluctuate significantly in the future, and these fluctuations may be unrelated to the Company's performance. General market price declines or market volatility in the future could adversely affect the price of its common stock, and the current market price may not be indicative of future market prices.

The holders of our junior subordinated debentures have rights that are senior to those of our shareholders.

As of December 31, 2010, we had \$201 million in junior subordinated debentures outstanding that were issued to our statutory trusts. The trusts purchased the junior subordinated debentures from us using the proceeds from the sale of trust preferred securities to third party investors. Payments of the principal and interest on the trust preferred securities are conditionally guaranteed by us to the extent not paid or made by each trust, provided the trust has funds available for such obligations.

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The junior subordinated debentures are senior to our shares of common stock and the Senior Preferred Stock. As a result, we must make payments on the junior subordinated debentures (and the related trust preferred securities) before any dividends can be paid on our common stock or preferred stock and, in the event of our bankruptcy, dissolution or liquidation, the holders of the debentures must be satisfied before any distributions can be made to our shareholders. If certain conditions are met, we have the right to defer interest payments on the junior subordinated debentures (and the related trust preferred securities) at any time or from time to time for a period not to exceed 10 consecutive semi-annual periods on one of the trusts and up to 20 consecutive quarters in a deferral period on the other seven trusts, during which time no dividends may be paid to holders of our common stock or preferred stock.

Risks Related to Participation in the CPP

We may be adversely affected by our participation in the CPP.

In connection with our sale of Senior Preferred Stock to the Treasury Department under the Capital Purchase Program, the Company also issued to the Treasury Department a warrant to purchase 1,326,238 shares of our common stock. The terms of the transaction with the Treasury will result in limitations on our ability to pay dividends and repurchase our shares. Until December 23, 2011 or until Treasury no longer holds any shares of the Series A Preferred Stock, the Company will not be able to increase cash dividends above current levels (\$.33 per share of common stock on a semi-annual basis). In addition, we will not be able to pay any dividends at all on our common stock unless we are current on our dividend payments on the Senior Preferred Stock. These restrictions, as well as the dilutive impact of the warrant, may have a negative effect on the market price of our common stock.

Unless the Company is able to redeem the Senior Preferred Stock prior to February 15, 2014, the cost of this capital will increase substantially on that date, from 5.00% on the liquidation preference of \$1,000 per share of Senior Preferred Stock (approximately \$10,800,000 annually) to 9.00% on the liquidation preference of \$1,000 per share of Senior Preferred Stock (approximately \$19,440,000 annually). Depending on our financial condition at the time, this increase in dividends on the Series A Preferred Stock could have a negative effect on our liquidity.

The terms of the Securities Purchase Agreement in which we entered into with Treasury pursuant to the CPP provides that the Treasury may unilaterally amend any provision of the Purchase Agreement to the extent required to comply with any changes in applicable federal law that may occur in the future. We have no assurances that changes in applicable law affecting the Purchase Agreement will not occur in the future. Such changes may place restrictions on our business or results of operations, which may adversely affect the market price of our common stock.

The programs established or to be established under the EESA and Capital Purchase Program may have adverse effects upon the Company. The Company may face increased regulation of the financial services industry. Compliance with such regulation may increase the Company's costs and limit its ability to pursue business opportunities. The affects of additional CPP related legislation and regulatory programs on the Company cannot reliably be determined at this time.

You may not receive dividends on the common stock.

Holders of our common stock are entitled to receive dividends only when, as and if declared by our Board of Directors. Although we have historically declared cash dividends on our common stock, we are not required to do so and our Board of Directors may reduce or eliminate our common stock dividend in the future. Further, the terms of the Senior Preferred Stock limit our payment of dividends on common stock, as described above. This could adversely affect the market price of our common stock.

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We may experience increases in the cost of compensation programs

In addition, pursuant to the Securities Purchase Agreement we adopted Treasury's standards for executive compensation for the period during which the Treasury holds the equity issued pursuant to the Securities Purchase Agreement, including the common stock that may be issued pursuant to the warrant. These standards include an agreement not to deduct for tax purposes executive compensation in excess of \$500,000 for each applicable senior executive. This change to the deductibility limit on executive compensation increased the costs of our compensation programs for the year ended December 31, 2010 and will likely increase the overall cost of our compensation programs in future periods during with the Company is a TARP participant.

We may lose members of our management team due to compensation restrictions.

The Company's ability to retain key officers and employees may be negatively impacted by recent legislation and regulation affecting the financial services industry. On February 17, 2009, the American Recovery and Reinvestment Act of 2009 (the "ARRA") was signed into law and the related rules of the Treasury Department were adopted on June 15, 2009. The ARRA, among other things, significantly expands the executive compensation restrictions previously imposed by the Emergency Economic Stabilization Act of 2008. 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 of the preferred stock issued under the Capital Purchase Program remains outstanding and held by the Treasury Department. As a result of our 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. Such restrictions and standards may further impact management's ability to retain key officers and employees as well as the Company's ability to compete with financial institutions that are not subject to the same limitations as the Company under the ARRA.

Item 1B. *Unresolved Staff Comments*

N/A

Item 2. *Properties*

The principal offices of the Company and IBC are located at 1200 San Bernardo Avenue, Laredo, Texas and 2418 Jacaman Road, Laredo, Texas in buildings owned and completely occupied by the Company and IBC and containing approximately 147,000 square feet. The bank subsidiaries of IBC have 278 main banking and branch facilities. All the facilities are customary to the banking industry. The bank subsidiaries own most of their banking facilities and the remainder are leased. The facilities are located in the regions of Laredo, San Antonio, Houston, Zapata, Eagle Pass, the Rio Grande Valley of Texas, the Coastal Bend area of Texas, and throughout the State of Oklahoma.

As Texas state-chartered banks, no bank subsidiary of the Company may, without the prior written consent of the Banking Commissioner, invest an amount in excess of its Tier 1 capital in bank facilities, furniture, fixtures and equipment. None of the Company's bank subsidiaries exceeds such limitation.

Item 3. *Legal Proceedings*

The Company and its bank subsidiaries are 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 and its subsidiaries have determined, based on discussions with their 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 and its subsidiaries.

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However, many of these matters are in various stages of proceedings and further developments could cause management to revise its assessment of these matters. Further information regarding legal proceedings has been provided in Note 17 of the Notes to consolidated financial statements located on page 76 of the 2010 Annual Report to Shareholders which is incorporated herein by reference.

Item 4A. Executive Officers of the Registrant

Certain information is set forth in the following table concerning the executive officers of the Company, each of whom has been elected to serve until the 2010 Annual Meeting of Shareholders and until his successor is duly elected and qualified.

<u>Name</u>	<u>Age</u>	<u>Position of Office</u>	<u>Officer of the Company Since</u>
Dennis E. Nixon	68	Chairman of the Board of the Company since 1992 and President of the Company since 1979, Chief Executive Officer and Director of IBC	1979
R. David Guerra	58	Vice President of the Company since 1986 and President of IBC McAllen Branch and Director of IBC	1986
Imelda Navarro	53	Treasurer of the Company since 1982 and Senior Executive Vice President of IBC and Director of IBC since 2002	1982

There are no family relationships among any of the named persons. Each executive officer has held the same position or another executive position with the Company during the past five years.

PART II

Item 5. Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

The information set forth under the caption "Preferred Stock, Common Stock and Dividends," "Stock Repurchase Program," and "Equity Compensation Plan Information" located on pages 27 through 29 of Registrant's 2010 Annual Report is incorporated herein by reference.

Item 6. Selected Financial Data

The information set forth under the caption "Selected Financial Data" located on page 1 of Registrant's 2010 Annual Report is incorporated herein by reference.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The information set forth under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operations" located on pages 2 through 29 of Registrant's 2010 Annual Report is incorporated herein by reference.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

The information set forth under the caption "Liquidity and Capital Resources" located on pages 19 through 25 of Registrant's 2010 Annual Report is incorporated herein by reference.

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Item 8. *Financial Statements and Supplementary Data*

The consolidated financial statements located on pages 31 through 87 of Registrant's 2010 Annual Report are incorporated herein by reference.

The condensed quarterly income statements located on pages 88 and 89 of Registrant's 2010 Annual Report are incorporated herein by reference.

Item 9. *Changes In and Disagreements with Accountants on Accounting and Financial Disclosure*

None.

Item 9A. *Controls and Procedures*

As of the end of the period covered by this Annual Report on Form 10-K, an evaluation was carried out by the management of International Bancshares Corporation, (the "Corporation") with the participation of its Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Corporation's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934). Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures were effective as of the end of the period covered by this report. Additionally, there were no changes in the Corporation's internal control over financial reporting that occurred during the quarter ended December 31, 2010 that have materially affected, or are reasonably likely to materially affect, the Corporation's internal control over financial reporting.

Management's Report on Internal Control Over Financial Reporting

The management of the Company is responsible for establishing and maintaining adequate internal controls over financial reporting, as defined under Rules 13a-15(f) and 15d-15(f) of the Securities Exchange Act of 1934. The Company's internal control over financial reporting is a process designed under the supervision of the Company's Chief Executive Officer and Chief Financial Officer to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company's financial statements for external purposes in accordance with generally accepted accounting principles.

As of December 31, 2010, management assessed the effectiveness of the design and operation of the Company's internal controls over financial reporting based on the criteria for effective internal control over financial reporting established in "Internal Control—Integrated Framework," issued by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission. Based on the assessment, management determined that the Company maintained effective internal control over financial reporting as of December 31, 2010, based on those criteria.

McGladrey & Pullen, LLP, the independent registered public accounting firm that audited the 2010 consolidated financial statements of the Company included in this Annual Report on Form 10-K, has audited the effectiveness of the Company's internal control over financial reporting as of December 31, 2010. Their report, which expresses an unqualified opinion, on the effectiveness of the Company's internal control over financial reporting as of December 31, 2010 is included in this Item under the heading "Report of Independent Registered Public Accounting Firm."

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders
International Bancshares Corporation

We have audited 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. International Bancshares Corporation and subsidiaries' management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit 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 effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (a) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (b) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (c) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, International Bancshares Corporation and subsidiaries maintained, in all material respects, effective 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.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated statements of condition 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 of International Bancshares Corporation and subsidiaries and our report dated February 28, 2011 expressed an unqualified opinion.

/s/ McGladrey & Pullen, LLP

Dallas, Texas
February 28, 2011

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Item 9B. *Other Information*

None.

PART III

Item 10. *Directors, Executive Officers and Corporate Governance*

There is incorporated in this Item 10 by reference (i) that portion of the Company's definitive proxy statement relating to the Company's 2011 Annual Meeting of Shareholders entitled "ELECTION OF DIRECTORS," (ii) the portion of the Company's definitive proxy statement entitled "Audit Committee" in the portion entitled "MEETINGS AND COMMITTEES OF THE BOARD OF DIRECTORS," (iii) the portion of the Company's definitive proxy statement entitled "Code of Ethics," in the portion entitled "CORPORATE GOVERNANCE," (iv) that portion of the Company's definitive proxy statement entitled "SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE," and (v) Item 4A of this report entitled "Executive Officers of the Registrant."

Item 11. *Executive Compensation*

There is incorporated in this Item 11 by reference (i) that portion of the Company's definitive proxy statement relating to the Company's 2011 Annual Meeting of Shareholders entitled "EXECUTIVE COMPENSATION," which includes, without limitation, the compensation committee certification required under the CPP, and (ii) that portion entitled "Salary and Steering Committee and Stock Option Plan Committee Interlocks and Insider Participation" in the portion entitled "MEETINGS AND COMMITTEES OF THE BOARD OF DIRECTORS."

Item 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters*

There are incorporated in this Item 12 by reference those portions of the Company's definitive proxy statement relating to the Company's 2011 Annual Meeting of Shareholders entitled "PRINCIPAL SHAREHOLDERS," "SECURITY OWNERSHIP OF MANAGEMENT," and "Equity Compensation Plan Information" in the portion entitled "EXECUTIVE COMPENSATION."

Item 13. *Certain Relationships and Related Transactions, and Director Independence*

There is incorporated in this Item 13 by reference (i) that portion of the Company's definitive proxy statement relating to the Company's 2011 Annual Meeting of Shareholders entitled "INTEREST OF MANAGEMENT IN CERTAIN TRANSACTIONS" and (ii) that portion entitled "Director Independence" in the portion entitled "CORPORATE GOVERNANCE."

Item 14. *Principal Accounting Fees and Services*

There is incorporated in this Item 14 by reference that portion of the Company's definitive proxy statement relating to the Company's 2011 Annual Meeting of Shareholders entitled "PRINCIPAL ACCOUNTANT FEES AND SERVICES."

PART IV

Item 15. Exhibits, Financial Statement Schedules

(a) Documents

1. The consolidated financial statements of the Company and subsidiaries are incorporated into Item 8 of this report by reference from the 2010 Annual Report to Shareholders filed as an exhibit hereto and they include:

Reports of Independent Registered Public Accounting Firm

Consolidated:

Statements of Condition as of December 31, 2010 and 2009

Statements of Income for the years ended December 31, 2010, 2009 and 2008

Statements of Comprehensive Income for the years ended December 31, 2010, 2009 and 2008

Statements of Shareholders' Equity for the years ended December 31, 2010, 2009 and 2008

Statements of Cash Flows for the years ended December 31, 2010, 2009 and 2008

Notes to Consolidated Financial Statements

2. All Financial Statement Schedules are omitted as the required information is inapplicable or the information is presented in the consolidated financial statements or related notes.
3. The following exhibits have previously been filed by the Registrant or are included in this report following the Index to Exhibits:

(3)(a)*—Articles of Incorporation of International Bancshares Corporation incorporated herein as an exhibit by reference to the Current Report, Exhibit 3.1 therein, under the Securities Exchange Act of 1934, filed by Registrant on Form 8-K with the Securities and Exchange Commission on June 20, 1995, SEC File No. 09439.

(3)(b)*—Articles of Amendment to the Articles of Incorporation of International Bancshares Corporation dated May 22, 1998 incorporated herein by reference to Exhibit 3(c) of the Registrant's Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 31, 1999, SEC file No. 09439.

(3)(c)*—Articles of Amendment to the Articles of Incorporation of International Bancshares Corporation dated May 21, 2002 incorporated herein by reference to Exhibit 3(d) of the Registrant's Annual Report on form 10-K filed with the Securities and Exchange Commission on March 12, 2004, SEC File No. 09439.

(3)(d)*—Articles of Amendment to the Articles of Incorporation of International Bancshares Corporation filed with the Secretary of State of the State of Texas on May 17, 2005, incorporated herein as an exhibit by reference to the Current Report, Exhibit 3.1 therein, under the Securities Exchange Act of 1934, filed by Registrant on Form 8-K with the Securities and Exchange Commission on May 20, 2005, SEC File No. 09439.

(3)(e)* Articles of Amendment to the Articles of Incorporation of International Bancshares Corporation filed with the Secretary of State of the State of Texas on December 22, 2008, incorporated herein as an exhibit by reference to the Current Report, Exhibit 3.1 therein, filed by registrant on Form 8-K with the Commission on December 23, 2008, Commission File No. 09439.

(3)(f)* Certificate of Designations for 216,000 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A, of International Bancshares Corporation, filed with the Secretary of State of the State of Texas on December 22, 2008, incorporated herein as an exhibit by

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reference to the Current Report, Exhibit 3.2 therein, filed by registrant on Form 8-K with the Commission on December 23, 2008, Commission File No. 09439.

(3)(g)* Amended and Restated By-Laws of International Bancshares Corporation, incorporated herein as an exhibit by reference to the Current Report, Exhibit 3.1 therein, filed by registrant on Form 8-K with the Commission on December 18, 2009, Commission File No. 09439.

(4)(a)* Warrant, dated December 23, 2008, to purchase shares of common stock of International Bancshares Corporation, incorporated herein as an exhibit by reference to the Current Report, Exhibit 4.1 therein, filed by registrant on Form 8-K with the Commission on December 23, 2008, Commission File No. 09439.

(4)(b)* Form of Certificate for the Fixed Rate Cumulative Perpetual Preferred Stock, Series A, par value \$0.01 per share incorporated herein as an exhibit by reference to the Current Report, Exhibit 4.2 therein, filed by registrant on Form 8-K with the Commission on December 23, 2008, Commission File No. 09439.

(10a)*+—Letter Agreement, dated as of December 23, 2008, and the Securities Purchase Agreement—Standard Terms, which the Letter Agreement incorporates by reference, between International Bancshares Corporation and the United States Department of the Treasury, incorporated herein as an exhibit by reference to the Current Report, Exhibit 10.1 therein, filed by registrant on Form 8-K with the Commission on December 23, 2008, Commission File No. 09439.

(10b)*+—The 1996 International Bancshares Corporation Stock Option Plan incorporated herein by reference to Exhibit 99.1 to the Post Effective Amendment No. 1 to Form S-8 filed with the Securities and Exchange Commission on March 21, 1997, SEC File No. 333-11689.

(10c)*+—2005 International Bancshares Corporation Stock Option Plan incorporated herein as an exhibit by reference to the Current Report, Exhibit 10.1 therein, under the Securities Exchange Act of 1934, filed by the Company on Form 8-K with the Securities and Exchange Commission on April 1, 2005, SEC File No. 09439.

(10d)*—Agreement and Plan of Merger dated as of January 22, 2004, among International Bancshares Corporation, LFC Acquisitions Corp. and Local Financial Corporation incorporated herein as an exhibit by reference to the Current Report, under the Securities Exchange Act of 1934, filed by Registrant on Form 8-K with the Securities and Exchange Commission on January 22, 2004, SEC File No. 09439.

(10e)*—International Bancshares Corporation 2006 Executive Incentive Compensation Plan, filed by Registrant on Form DEF 14A with the Securities and Exchange Commission on April 17, 2008, SEC File No. 09439.

(10f)*—International Bancshares Corporation Long-Term Restricted Stock Unit Plan, filed by Registrant on Form 8-K with the Securities and Exchange Commission on December 12, 2009, SEC File No. 09439.

(13)**—International Bancshares Corporation 2010 Annual Report

(21)—List of Subsidiaries of International Bancshares Corporation as of February 22, 2011

(23)—Consent of Independent Registered Public Accounting Firm

(31a)—Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

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(31b)—Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

(32a)++—Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(32b)++—Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(99a)—Certification of Chief Executive Officer pursuant to 31 C.F.R. Section 30.15

(99b)—Certification of Chief Financial Officer pursuant to 31 C.F.R. Section 30.15

101++—Interactive Data File

* Previously filed

+ Executive Compensation Plans and Arrangements

** Deemed filed only with respect to those portions thereof incorporated herein by reference

++ Attached as Exhibit 101 to this report are the following documents formatted in XBRL (Extensible Business Reporting Language): (i) the Condensed Consolidated Statement of Earnings for the years ended December 31, 2010, 2009 and 2008 (ii) the Condensed Consolidated Balance Sheet as of December 31, 2010 and 2009, and (iii) the Condensed Consolidated Statement of Cash Flows for the years ended December 31, 2010 and 2009. Users of this data are advised pursuant to Rule 406T of Regulation S-T that this interactive data file is deemed not filed or part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, is deemed not filed for purposes of section 18 of the Securities and Exchange Act of 1934, and otherwise is not subject to liability under these sections.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

INTERNATIONAL BANCSHARES CORPORATION
(Registrant)

By: /s/ Dennis E. Nixon

Dennis E. Nixon
President

Date: February 28, 2011

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons on behalf of the Registrant and in the capacities and on the date indicated.

<u>Signatures</u>	<u>Title</u>	<u>Date</u>
/s/ Dennis E. Nixon Dennis E. Nixon	President and Director (Principal Executive Officer)	February 28, 2011
/s/ Imelda Navarro Imelda Navarro	Treasurer (Principal Financial Officer and Principal Accounting Officer)	February 28, 2011
/s/ Irving Greenblum Irving Greenblum	Director	February 28, 2011
/s/ R. David Guerra R. David Guerra	Director	February 28, 2011
/s/ Daniel B. Hastings, Jr. Daniel B. Hastings, Jr.	Director	February 28, 2011
/s/ Doug Howland Doug Howland	Director	February 28, 2011
/s/ Sioma Neiman Sioma Neiman	Director	February 28, 2011

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<u>Signatures</u>	<u>Title</u>	<u>Date</u>
/s/ Peggy J. Newman Peggy J. Newman	Director	February 28, 2011
/s/ Larry Norton Larry Norton	Director	February 28, 2011
/s/ Leonardo Salinas Leonardo Salinas	Director	February 28, 2011
/s/ Antonio R. Sanchez, Jr. Antonio R. Sanchez, Jr.	Director	February 28, 2011
/s/ Guillermo Trevino Guillermo Trevino	Director	February 28, 2011

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Exhibit Index

Exhibit 13—	International Bancshares Corporation 2010 Annual Report, Exhibit 13, page 1
Exhibit 21—	List of Subsidiaries of International Bancshares Corporation as of February 22, 2011
Exhibit 23—	Consent of Independent Registered Public Accounting Firm
Exhibit 31(a)—	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
Exhibit 31(b)—	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
Exhibit 32(a)—	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
Exhibit 32(b)—	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
Exhibit (99a)—	Certification of Chief Executive Officer pursuant to 31 C.F.R. Section 30.15
Exhibit (99b)—	Certification of Chief Financial Officer pursuant to 31 C.F.R. Section 30.15

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	2009	2008
	Average	Average	Average
	Rate/Cost	Rate/Cost	Rate/Cost
<i>Assets</i>			
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 %
<i>Liabilities</i>			
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			2009 compared to 2008		
	Net increase (decrease) due to			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
	<u>\$ 84,482</u>	<u>100.0%</u>	<u>\$ 95,393</u>	<u>100.0%</u>	<u>\$ 73,461</u>	<u>100.0%</u>	<u>\$ 61,726</u>	<u>100.0%</u>	<u>\$ 64,537</u>	<u>100.0%</u>

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	<u>\$ 218,784</u>	<u>\$ 201,013</u>	<u>8.8%</u>	<u>\$ 189,809</u>	<u>5.9%</u>

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	<u>\$ 339,725</u>	<u>\$ 309,031</u>	<u>9.9%</u>	<u>\$ 301,226</u>	<u>2.6%</u>

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	<u>\$ 5,088,907</u>	<u>\$ 4,646,533</u>	<u>\$ 5,074,180</u>

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		After five but		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	<u>\$ 2,564</u>	1.87%	<u>\$ 3,465</u>	5.45%	<u>\$ 542,789</u>	4.23%	<u>\$ 4,493,029</u>	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	<u>\$ 1,825</u>	1.45%	<u>\$ 625</u>	1.41%	<u>\$ —</u>	—%	<u>\$ —</u>	—%

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	<u>245,625</u>	<u>280,485</u>	<u>328,948</u>	<u>285,008</u>	<u>309,144</u>
Total loans	5,410,003	5,667,262	5,872,833	5,536,629	5,034,884
Unearned discount	<u>—</u>	<u>—</u>	<u>—</u>	(1)	(74)
Loans, net of unearned discount	<u>\$ 5,410,003</u>	<u>\$ 5,667,262</u>	<u>\$ 5,872,833</u>	<u>\$ 5,536,628</u>	<u>\$ 5,034,810</u>

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	<u>161,772</u>	<u>82,571</u>	<u>1,282</u>	<u>245,625</u>
Total	<u>\$ 2,002,479</u>	<u>\$ 2,204,093</u>	<u>\$ 128,402</u>	<u>\$ 4,334,974</u>

	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	<u>\$ 270,709</u>	<u>\$ 2,061,786</u>

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
	<u>\$ 245,625</u>	<u>\$ 437</u>

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	<u>102</u>
Net recoveries	(125)
Provision charged to expense	<u>169</u>
Balance at December 31, 2010	<u>\$ 437</u>

Deposits

	2010	2009
	Average Balance	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
	\$	<u>2,297,173</u>

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 (in thousands)	Repricing Frequency	Interest Rate	Interest Rate Index	Maturity Date	Optional Redemption Date
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
	<u>\$ 201,117</u>					

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- (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:

Contractual Cash Obligations	Payments due by Period (Dollars in Thousands)				
	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	<u>\$ 2,689,494</u>	<u>\$ 1,461,294</u>	<u>\$ 12,034</u>	<u>\$ 4,388</u>	<u>\$ 1,211,778</u>

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.

		<u>High</u>	<u>Low</u>
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

		<u>High</u>	<u>Low</u>
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:

<u>Date</u>	<u>Stock Dividend</u>
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	<u>26,616</u>	<u>\$ 17.10</u>	<u>26,616</u>	

(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.

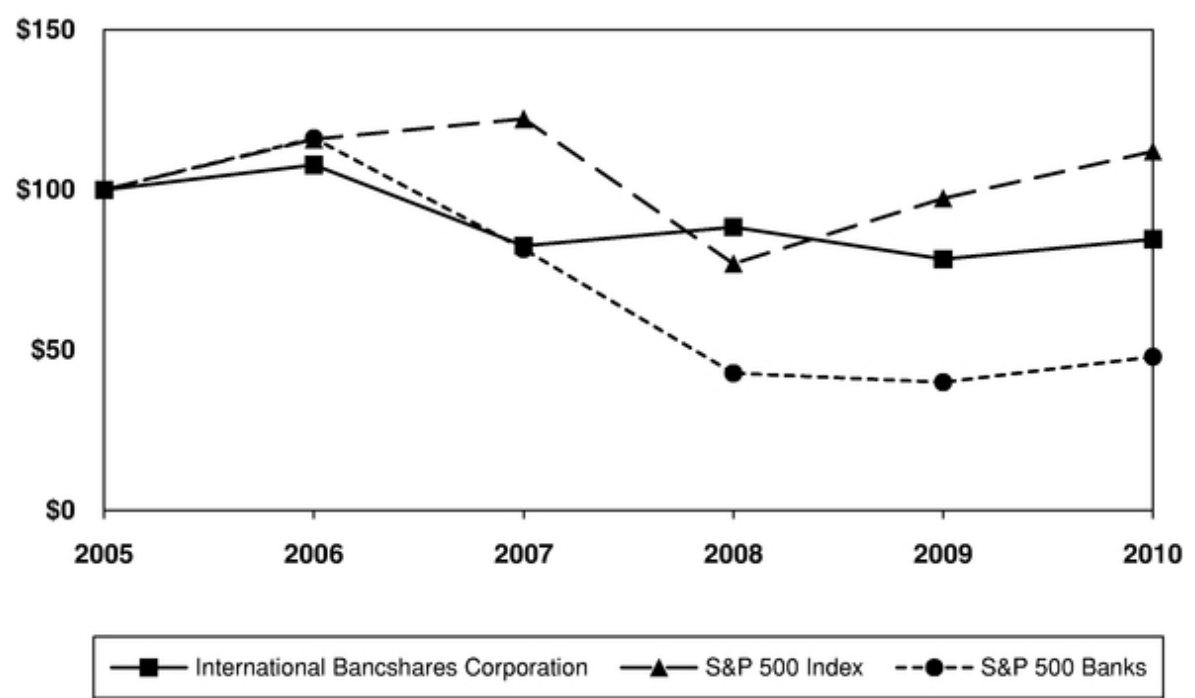
Equity Compensation Plan Information

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	<u>764,982</u>	<u>\$ 20.65</u>	<u>193,197</u>

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)

	<u>2010</u>	<u>2009</u>
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)	<u>5,086,457</u>	<u>4,644,083</u>
Total investment securities	5,088,907	4,646,533
Loans	5,410,003	5,667,262
Less allowance for probable loan losses	<u>(84,482)</u>	<u>(95,393)</u>
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	<u>165,821</u>	<u>123,103</u>
Total assets	<u>\$ 11,943,469</u>	<u>\$ 11,762,543</u>

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)

	<u>2010</u>	<u>2009</u>
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	<u>3,437,640</u>	<u>3,398,656</u>
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	<u>223,527</u>	<u>186,542</u>
Total liabilities	<u>10,484,252</u>	<u>10,355,073</u>
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	<u>28,777</u>	<u>65,878</u>
	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	<u>(250,358)</u>	<u>(243,409)</u>
Total shareholders' equity	<u>1,459,217</u>	<u>1,407,470</u>
Total liabilities and shareholders' equity	<u>\$ 11,943,469</u>	<u>\$ 11,762,543</u>

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)

	<u>2010</u>	<u>2009</u>	<u>2008</u>
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	<u>2,221</u>	<u>607</u>	<u>516</u>
Total interest income	<u>458,769</u>	<u>527,377</u>	<u>564,603</u>
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	<u>—</u>	<u>—</u>	<u>88</u>
Total interest expense	<u>114,036</u>	<u>139,796</u>	<u>231,731</u>
Net interest income	344,733	387,581	332,872
Provision for probable loan losses	<u>22,812</u>	<u>58,833</u>	<u>19,813</u>
Net interest income after provision for probable loan losses	<u>321,921</u>	<u>328,748</u>	<u>313,059</u>
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	<u>11,866</u>	<u>14,084</u>	<u>21,598</u>
Total non-interest income	<u>218,784</u>	<u>201,013</u>	<u>189,809</u>

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)

	<u>2010</u>	<u>2009</u>	<u>2008</u>
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	<u>339,725</u>	<u>309,031</u>	<u>301,226</u>
Income before income taxes	200,980	220,730	201,642
Provision for income taxes	<u>70,957</u>	<u>77,988</u>	<u>69,530</u>
Net income	<u>\$ 130,023</u>	<u>\$ 142,742</u>	<u>\$ 132,112</u>
Preferred stock dividends and discount accretion	<u>13,126</u>	<u>12,984</u>	<u>—</u>
Net income available to common shareholders	<u><u>\$ 116,897</u></u>	<u><u>\$ 129,758</u></u>	<u><u>\$ 132,112</u></u>
Basic earnings per common share:			
Weighted average number of shares outstanding	67,921,353	68,373,732	68,576,654
Net income	<u>\$ 1.72</u>	<u>\$ 1.90</u>	<u>\$ 1.93</u>
Fully diluted earnings per common share:			
Weighted average number of shares outstanding	68,004,441	68,394,624	68,714,390
Net income	<u>\$ 1.72</u>	<u>\$ 1.90</u>	<u>\$ 1.92</u>

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	<u>\$ 92,922</u>	<u>\$ 190,431</u>	<u>\$ 150,136</u>

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	<u>\$ 208,068</u>	<u>95,711</u>	<u>\$ 95,711</u>	<u>\$ 162,276</u>	<u>\$ 1,214,743</u>	<u>\$ 28,777</u>	<u>\$ (250,358)</u>	<u>\$ 1,459,217</u>

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)

	<u>2010</u>	<u>2009</u>	<u>2008</u>
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	<u>127,222</u>	<u>141,767</u>	<u>154,104</u>
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	<u>(235)</u>	<u>(259)</u>	<u>(1,074)</u>
Net cash (used in) provided by investing activities	<u>(204,510)</u>	<u>679,152</u>	<u>(1,251,412)</u>

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)

	<u>2010</u>	<u>2009</u>	<u>2008</u>
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	<u>50,464</u>	<u>(895,001)</u>	<u>1,049,976</u>
Decrease in cash and cash equivalents	(26,824)	(74,082)	(47,332)
Cash and cash equivalents at beginning of year	<u>224,638</u>	<u>298,720</u>	<u>346,052</u>
Cash and cash equivalents at end of year	<u>\$ 197,814</u>	<u>\$ 224,638</u>	<u>\$ 298,720</u>
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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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	<u>\$ 2,450</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 2,450</u>	<u>\$ 2,450</u>

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(2) Investment Securities (Continued)

	Available for Sale				
	Amortized	Gross	Gross	Estimated	Carrying
	cost	unrealized	unrealized	fair	value(1)
		gains	losses	value	
			(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	<u>\$ 5,041,847</u>	<u>\$ 79,241</u>	<u>\$ (34,631)</u>	<u>\$ 5,086,457</u>	<u>\$ 5,086,457</u>

(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	<u>\$ 2,450</u>	<u>\$ 2,450</u>	<u>\$ 5,041,847</u>	<u>\$ 5,086,457</u>

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
Total investment securities	<u>\$ 2,450</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 2,450</u>

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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	<u>\$ 4,541,851</u>	<u>\$ 117,583</u>	<u>\$ (15,351)</u>	<u>\$ 4,644,083</u>	<u>\$ 4,644,083</u>

- (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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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)
	<u>\$ 1,269,409</u>	<u>\$ (23,870)</u>	<u>\$ 46,446</u>	<u>\$ (10,761)</u>	<u>\$ 1,315,855</u>	<u>\$ (34,631)</u>

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)
	<u>\$ 31,491</u>	<u>\$ (238)</u>	<u>\$ 60,187</u>	<u>\$ (15,113)</u>	<u>\$ 91,678</u>	<u>\$ (15,351)</u>

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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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	<u>\$ 8,416</u>

(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	<u>\$ 5,410,003</u>	<u>\$ 5,667,262</u>

(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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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,	<u>\$ 84,482</u>	<u>\$ 95,393</u>	<u>\$ 73,461</u>

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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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	<u>\$ 125,200</u>	<u>\$ 12,171</u>	<u>\$ 5,284,803</u>	<u>\$ 72,311</u>

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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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	<u>\$ 73,694</u>	<u>\$ 76,236</u>	<u>\$ 78,288</u>	<u>\$ 32</u>

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	<u>\$ 118,274</u>	<u>\$ 164,939</u>
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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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	<u>\$ 16,870</u>	<u>\$ 9,434</u>	<u>\$ 88,529</u>	<u>\$ 19,848</u>	<u>\$ 114,833</u>	<u>\$ 5,295,170</u>	<u>\$ 5,410,003</u>

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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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	<u>\$ 4,760,129</u>	<u>\$ 187,119</u>	<u>\$ 92,640</u>	<u>\$ 244,915</u>	<u>\$ 125,200</u>

(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		<u>\$ 468,950</u>	<u>\$ 490,375</u>

(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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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:

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

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:

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

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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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:

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

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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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	<u>\$ 3,437,640</u>

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
	<u>\$ 2,297,173</u>

(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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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	<u>\$ 1,747,043</u>	<u>\$ 1,777,975</u>	<u>\$ 1,433,270</u>	<u>2.97%</u>
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	<u>\$ 1,839,876</u>	<u>\$ 1,891,443</u>	<u>\$ 1,441,817</u>	<u>2.97%</u>

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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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 (in thousands)	Repricing Frequency	Interest Rate	Interest Rate Index(1)	Maturity Date	Optional Redemption Date
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
	<u>\$ 201,117</u>					

(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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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:

	<u>Net Income</u> <u>(Numerator)</u>	<u>Shares</u> <u>(Denominator)</u> (Dollars in Thousands, Except Per Share Amounts)	<u>Per Share</u> <u>Amount</u>
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	<u>\$ 116,897</u>	<u>68,004,441</u>	\$ 1.72
December 31, 2009:			
Basic EPS			
Net income	\$ 129,758	68,373,732	\$ 1.90
Potential dilutive common shares	—	20,892	
Diluted EPS	<u>\$ 129,758</u>	<u>68,394,624</u>	\$ 1.90
December 31, 2008:			
Basic EPS			
Net income	\$ 132,112	68,576,654	\$ 1.93
Potential dilutive common shares	—	137,736	
Diluted EPS	<u>\$ 132,112</u>	<u>68,714,390</u>	\$ 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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(13) International Operations (Continued)

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

	<u>2010</u>	<u>2009</u>
	<u>(Dollars in Thousands)</u>	
Loans:		
Commercial	\$ 195,208	\$ 230,464
Others	<u>50,417</u>	<u>50,021</u>
	245,625	280,485
Less allowance for probable loan losses	<u>(437)</u>	<u>(393)</u>
Net loans	<u>\$ 245,188</u>	<u>\$ 280,092</u>
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:

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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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:

	<u>2010</u>	<u>2009</u>	<u>2008</u>
	(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	<u>\$ 70,957</u>	<u>\$ 77,988</u>	<u>\$ 69,530</u>

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:

	<u>2010</u>	<u>2009</u>
	(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	<u>43,724</u>	<u>41,051</u>
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	<u>(66,238)</u>	<u>(87,619)</u>
Net deferred tax liability	<u>\$ (22,514)</u>	<u>\$ (46,568)</u>

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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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:

<u>Non-vested Options</u>	<u>Options</u>	<u>Weighted average grant-date fair value (\$)</u>
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	<u>377,544</u>	\$ 4.48

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

	<u>Twelve Months Ended December 31,</u>		
	<u>2010</u>	<u>2009</u>	<u>2008</u>
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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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:

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

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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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	<u>\$ 46,028</u>

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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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.

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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	<u>\$ 1,671,061</u>	<u>\$ 1,614,303</u>
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	<u>211,844</u>	<u>206,833</u>
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	<u>(250,358)</u>	<u>(243,409)</u>
Total shareholders' equity	<u>1,459,217</u>	<u>1,407,470</u>
Total liabilities and shareholders' equity	<u>\$ 1,671,061</u>	<u>\$ 1,614,303</u>

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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

INTERNATIONAL BANCSHARES CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements (Continued)

(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)**

	<u>2010</u>	<u>2009</u>	<u>2008</u>
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	<u>54,548</u>	<u>39,798</u>	<u>49,233</u>
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	<u>(5,137)</u>	<u>(144,277)</u>	<u>(59,623)</u>
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	<u>(41,709)</u>	<u>(39,563)</u>	<u>170,564</u>
Increase (decrease) in cash	7,702	(144,042)	160,174
Cash at beginning of year	<u>16,712</u>	<u>160,754</u>	<u>580</u>
Cash at end of year	<u>\$ 24,414</u>	<u>\$ 16,712</u>	<u>\$ 160,754</u>

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	<u>26,564</u>	<u>27,902</u>	<u>29,643</u>	<u>29,927</u>
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	<u>75,305</u>	<u>79,379</u>	<u>79,464</u>	<u>105,577</u>
Income before income taxes	53,324	47,026	51,944	48,686
Income taxes	<u>22,904</u>	<u>13,477</u>	<u>17,936</u>	<u>16,640</u>
Net income	<u>\$ 30,420</u>	<u>\$ 33,549</u>	<u>\$ 34,008</u>	<u>\$ 32,046</u>
Preferred Stock Dividends	<u>3,295</u>	<u>3,286</u>	<u>3,277</u>	<u>3,268</u>
Net income available to common shareholders	<u><u>\$ 27,125</u></u>	<u><u>\$ 30,263</u></u>	<u><u>\$ 30,731</u></u>	<u><u>\$ 28,778</u></u>
Per common share:				
Basic				
Net income	<u><u>\$.40</u></u>	<u><u>\$.45</u></u>	<u><u>\$.45</u></u>	<u><u>\$.42</u></u>
Diluted				
Net income	<u><u>\$.40</u></u>	<u><u>\$.45</u></u>	<u><u>\$.45</u></u>	<u><u>\$.42</u></u>

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	<u>30,818</u>	<u>32,257</u>	<u>34,651</u>	<u>42,070</u>
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	<u>74,878</u>	<u>78,746</u>	<u>85,181</u>	<u>70,226</u>
Income before income taxes	59,113	56,230	47,680	57,707
Income taxes	<u>22,005</u>	<u>19,257</u>	<u>16,547</u>	<u>20,179</u>
Net income	<u>\$ 37,108</u>	<u>\$ 36,973</u>	<u>\$ 31,133</u>	<u>\$ 37,528</u>
Preferred Stock Dividends	<u>3,259</u>	<u>3,250</u>	<u>3,242</u>	<u>3,233</u>
Net income available to common shareholders	<u><u>\$ 33,849</u></u>	<u><u>\$ 33,723</u></u>	<u><u>\$ 27,891</u></u>	<u><u>\$ 34,295</u></u>
Per common share:				
Basic				
Net income	<u><u>\$.50</u></u>	<u><u>\$.49</u></u>	<u><u>\$.41</u></u>	<u><u>\$.50</u></u>
Diluted				
Net income	<u><u>\$.50</u></u>	<u><u>\$.49</u></u>	<u><u>\$.41</u></u>	<u><u>\$.50</u></u>

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.

List of Subsidiaries

Subsidiaries of International Bancshares Corporation

Name	State of Incorporation or Organization	Business	% of Ownership
IBC Subsidiary Corporation	Delaware	Bank Holding Company	100%
IBC Life Insurance Company	Texas	Credit Life Insurance	100%
IBC Trading Company	Texas	Export Trading	100%
IBC Capital Corporation	Texas	Investments	100%
Premier Tierra Holdings, Inc.	Texas	Liquidating Subsidiary	100%

Subsidiaries of IBC Subsidiary Corporation

Name	State of Incorporation or Organization	Business	% of Ownership
International Bank of Commerce	Texas	State Bank	100%
Commerce Bank	Texas	State Bank	100%
International Bank of Commerce, Zapata	Texas	State Bank	100%
International Bank of Commerce, Brownsville	Texas	State Bank	100%
Gulfstar Merchant Banking I, Ltd.	Texas	Investment and Merchant Banking	70%
Gulfstar Merchant Banking II, Ltd.	Texas	Investment Banking	70%
Gulfstar Merchant Banking III, Ltd.	Texas	Merchant Banking	50%

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in Registration Statement (No. 333-128147) on Form S-8 of International Bancshares Corporation of our reports dated February 28, 2011, relating to our audits of the consolidated financial statements and internal control over financial reporting, included in and incorporated by reference in the Annual Report on Form 10-K of International Bancshares Corporation for the year ended December 31, 2010.

/s/ McGladrey & Pullen, LLP

Dallas, Texas
February 28, 2011

Certification

I, Dennis E. Nixon, certify that:

1. I have reviewed this Annual Report on Form 10-K of International Bancshares Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 28, 2011

By: /s/ DENNIS E. NIXON

Dennis E. Nixon
President (Chief Executive Officer)

Certification

I, Imelda Navarro, certify that:

1. I have reviewed this Annual Report on Form 10-K of International Bancshares Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 28, 2011

By: /s/ IMELDA NAVARRO

Imelda Navarro
Treasurer (Chief Financial Officer)

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of International Bancshares Corporation (the "Company") on Form 10-K for the year ended December 31, 2010 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Dennis E. Nixon, President and Principal Executive Officer of the Company, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)), as applicable; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

By: /s/ DENNIS E. NIXON

Dennis E. Nixon
President

Date: February 28, 2011

The foregoing certification is being furnished solely to accompany the Report pursuant to 18 U.S.C. Section 1350, and not being filed for purposes of Section 18 of the Securities Exchange Act, as amended, and is not to be incorporated by reference into any filing of the Company, whether on and before or after the date hereof, regardless of any general incorporation language in such filing.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of International Bancshares Corporation (the "Company") on Form 10-K for the year ended December 31, 2010 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Imelda Navarro, Treasurer and Principal Financial Officer of the Company, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (3) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)), as applicable; and
- (4) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

By: /s/ IMELDA NAVARRO
Imelda Navarro
Treasurer

Date: February 28, 2011

The foregoing certification is being furnished solely to accompany the Report pursuant to 18 U.S.C. Section 1350, and not being filed for purposes of Section 18 of the Securities Exchange Act, as amended, and is not to be incorporated by reference into any filing of the Company, whether on and before or after the date hereof, regardless of any general incorporation language in such filing.

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

**CERTIFICATION PURSUANT TO
31 C.F.R. SECTION 30.15**

**INTERNATIONAL BANCSHARES CORPORATION
UST #136**

I, Dennis E. Nixon, certify, based on my knowledge, that:

(i) The compensation committee of International Bancshares Corporation has discussed, reviewed, and evaluated with senior risk officers at least every six months during any part of the most recently completed fiscal year that was a TARP period, senior executive officer ("SEO") compensation plans and employee compensation plans and the risks these plans pose to International Bancshares Corporation;

(ii) The compensation committee of International Bancshares Corporation has identified and limited during any part of the most recently completed fiscal year that was a TARP period any features of the SEO compensation plans that could lead SEOs to take unnecessary and excessive risks that could threaten the value of International Bancshares Corporation and has identified any features of the employee compensation plans that pose risks to International Bancshares Corporation and has limited those features to ensure that International Bancshares Corporation is not unnecessarily exposed to risks;

(iii) The compensation committee has reviewed, at least every six months during any part of the most recently completed fiscal year that was a TARP period, the terms of each employee compensation plan and identified any features of the plan that could encourage the manipulation of reported earnings of International Bancshares Corporation to enhance the compensation of an employee, and has limited any such features;

(iv) The compensation committee of International Bancshares Corporation will certify to the reviews of the SEO compensation plans and employee compensation plans required under (i) and (iii) above;

(v) The compensation committee of International Bancshares Corporation will provide a narrative description of how it limited during any part of the most recently completed fiscal year that was a TARP period the features in:

- (A) SEO compensation plans that could lead SEOs to take unnecessary and excessive risks that could threaten the value of International Bancshares Corporation;
- (B) Employee compensation plans that unnecessarily expose International Bancshares Corporation to risks; and
- (C) Employee compensation plans that could encourage the manipulation of reported earnings of International Bancshares Corporation to enhance the compensation of an employee;

(vi) International Bancshares Corporation has required that bonus payments to SEOs or any of the next twenty most highly compensated employees, as defined in the regulations and guidance established under section 111 of EESA (bonus payments), be subject to a recovery or "clawback" provision during any part of the most recently completed fiscal year that was a TARP period if the bonus payments were based on materially inaccurate financial statements or any other materially inaccurate performance metric criteria;

(vii) International Bancshares Corporation has prohibited any golden parachute payment, as defined in the regulations and guidance established under section 111 of EESA, to a SEO or any of the next five most highly compensated employees during any part of the most recently completed fiscal year that was a TARP period;

- (viii) International Bancshares Corporation has limited bonus payments to its applicable employees in accordance with section 111 of EESA and the regulations and guidance established thereunder during any part of the most recently completed fiscal year that was a TARP period;
- (ix) International Bancshares Corporation and its employees have complied with the excessive or luxury expenditures policy, as defined in the regulations and guidance established under section 111 of EESA, during any part of the most recently completed fiscal year that was a TARP period; and any expenses that, pursuant to the policy, required approval of the board of directors, a committee of the board of directors, an SEO, or an executive officer with a similar level of responsibility were properly approved;
- (x) International Bancshares Corporation will permit a non-binding shareholder resolution in compliance with any applicable federal securities rules and regulations on the disclosures provided under the federal securities laws related to SEO compensation paid or accrued during any part of the most recently completed fiscal year that was a TARP period;
- (xi) International Bancshares Corporation will disclose the amount, nature, and justification for the offering, during any part of the most recently completed fiscal year that was a TARP period, of any perquisites, as defined in the regulations and guidance established under section 111 of EESA, whose total value exceeds \$25,000 for any employee who is subject to the bonus payment limitations identified in paragraph (viii);
- (xii) International Bancshares Corporation will disclose whether International Bancshares Corporation, the board of directors of International Bancshares Corporation, or the compensation committee of International Bancshares Corporation has engaged during any part of the most recently completed fiscal year that was a TARP period a compensation consultant; and the services the compensation consultant or any affiliate of the compensation consultant provided during this period;
- (xiii) International Bancshares Corporation has prohibited the payment of any gross-ups, as defined in the regulations and guidance established under section 111 of EESA, to the SEOs and the next twenty most highly compensated employees during any part of the most recently completed fiscal year that was a TARP period;
- (xiv) International Bancshares Corporation has substantially complied with all other requirements related to employee compensation that are provided in the agreement between International Bancshares Corporation and Treasury, including any amendments;
- (xv) International Bancshares Corporation has submitted to Treasury a complete and accurate list of the SEOs and the twenty next most highly compensated employees for the current fiscal year, with the non-SEO's ranked in **descending** order of level of annual compensation, and with the name, title, and employer of each SEO and most highly compensated employee identified; and
- (xvi) I understand that a knowing and willful false or fraudulent statement made in connection with this certification may be punished by fine, imprisonment, or both.

By: /s/ DENNIS E. NIXON

 Dennis E. Nixon
 President

Date: February 28, 2011

**CERTIFICATION PURSUANT TO
31 C.F.R. SECTION 30.15**

I, Imelda Navarro, certify, based on my knowledge, that:

(i) The compensation committee of International Bancshares Corporation has discussed, reviewed, and evaluated with senior risk officers at least every six months during any part of the most recently completed fiscal year that was a TARP period, senior executive officer ("SEO") compensation plans and employee compensation plans and the risks these plans pose to International Bancshares Corporation;

(ii) The compensation committee of International Bancshares Corporation has identified and limited during any part of the most recently completed fiscal year that was a TARP period any features of the SEO compensation plans that could lead SEOs to take unnecessary and excessive risks that could threaten the value of International Bancshares Corporation and has identified any features of the employee compensation plans that pose risks to International Bancshares Corporation and has limited those features to ensure that International Bancshares Corporation is not unnecessarily exposed to risks;

(iii) The compensation committee has reviewed, at least every six months during any part of the most recently completed fiscal year that was a TARP period, the terms of each employee compensation plan and identified any features of the plan that could encourage the manipulation of reported earnings of International Bancshares Corporation to enhance the compensation of an employee, and has limited any such features;

(iv) The compensation committee of International Bancshares Corporation will certify to the reviews of the SEO compensation plans and employee compensation plans required under (i) and (iii) above;

(v) The compensation committee of International Bancshares Corporation will provide a narrative description of how it limited during any part of the most recently completed fiscal year that was a TARP period the features in:

- (A) SEO compensation plans that could lead SEOs to take unnecessary and excessive risks that could threaten the value of International Bancshares Corporation;
- (B) Employee compensation plans that unnecessarily expose International Bancshares Corporation to risks; and
- (C) Employee compensation plans that could encourage the manipulation of reported earnings of International Bancshares Corporation to enhance the compensation of an employee;

(vi) International Bancshares Corporation has required that bonus payments to SEOs or any of the next twenty most highly compensated employees, as defined in the regulations and guidance established under section 111 of EESA (bonus payments), be subject to a recovery or "clawback" provision during any part of the most recently completed fiscal year that was a TARP period if the bonus payments were based on materially inaccurate financial statements or any other materially inaccurate performance metric criteria;

(vii) International Bancshares Corporation has prohibited any golden parachute payment, as defined in the regulations and guidance established under section 111 of EESA, to a SEO or any of the next five most highly compensated employees during any part of the most recently completed fiscal year that was a TARP period;

(viii) International Bancshares Corporation has limited bonus payments to its applicable employees in accordance with section 111 of EESA and the regulations and guidance established thereunder during any part of the most recently completed fiscal year that was a TARP period;

(ix) International Bancshares Corporation and its employees have complied with the excessive or luxury expenditures policy, as defined in the regulations and guidance established under section 111 of EESA, during any part of the most recently completed fiscal year that was a TARP period; and any expenses that, pursuant to the policy, required approval of the board of directors, a committee of the board of directors, an SEO, or an executive officer with a similar level of responsibility were properly approved;

(x) International Bancshares Corporation will permit a non-binding shareholder resolution in compliance with any applicable federal securities rules and regulations on the disclosures provided under the federal securities laws related to SEO compensation paid or accrued during any part of the most recently completed fiscal year that was a TARP period;

(xi) International Bancshares Corporation will disclose the amount, nature, and justification for the offering, during any part of the most recently completed fiscal year that was a TARP period, of any perquisites, as defined in the regulations and guidance established under section 111 of EESA, whose total value exceeds \$25,000 for any employee who is subject to the bonus payment limitations identified in paragraph (viii);

(xii) International Bancshares Corporation will disclose whether International Bancshares Corporation, the board of directors of International Bancshares Corporation, or the compensation committee of International Bancshares Corporation has engaged during any part of the most recently completed fiscal year that was a TARP period a compensation consultant; and the services the compensation consultant or any affiliate of the compensation consultant provided during this period;

(xiii) International Bancshares Corporation has prohibited the payment of any gross-ups, as defined in the regulations and guidance established under section 111 of EESA, to the SEOs and the next twenty most highly compensated employees during any part of the most recently completed fiscal year that was a TARP period;

(xiv) International Bancshares Corporation has substantially complied with all other requirements related to employee compensation that are provided in the agreement between International Bancshares Corporation and Treasury, including any amendments;

(xv) International Bancshares Corporation has submitted to Treasury a complete and accurate list of the SEOs and the twenty next most highly compensated employees for the current fiscal year, with the non-SEO ranked in **descending** order of level of annual compensation, and with the name, title, and employer of each SEO and most highly compensated employee identified; and

(xvi) I understand that a knowing and willful false or fraudulent statement made in connection with this certification may be punished by fine, imprisonment, or both.

By: /s/ IMELDA NAVARRO
Imelda Navarro
Treasurer

Date: February 28, 2011
