

**AGREEMENT BY AND BETWEEN
MERCEDES NATIONAL BANK
MERCEDES, TEXAS
AND
THE OFFICE OF THE COMPTROLLER OF THE CURRENCY**

Mercedes National Bank, Mercedes, Texas (“Bank”) and the Comptroller of the Currency of the United States of America (“Comptroller”) wish to protect the interests of the depositors, other customers, and shareholders of the Bank, and, toward that end, wish the Bank to operate safely and soundly and in accordance with all applicable laws, rules and regulations.

The Comptroller, through his National Bank Examiner, has examined the Bank, and his findings are contained in the Report of Examination for the examination that commenced on October 13, 2003 (“ROE”).

In consideration of the above premises, it is agreed, between the Bank, by and through its duly elected and acting Board of Directors (“Board”), and the Comptroller, through his authorized representative, that the Bank shall operate at all times in compliance with the Articles of this Agreement.

Article I-- JURISDICTION

(1) This Agreement shall be construed to be a “written agreement entered into with the agency” within the meaning of 12 U.S.C. § 1818(b)(1).

(2) This Agreement shall be construed to be a “written agreement between such depository institution and such agency” within the meaning of 12 U.S.C. § 1818(e)(1) and 12 U.S.C. § 1818(i)(2).

(3) This Agreement shall be construed to be a “formal written agreement” within the meaning of 12 C.F.R. § 5.51(c)(6)(ii). *See*, 12 U.S.C. § 1831i.

(4) This Agreement shall be construed to be a “written agreement” within the meaning of 12 U.S.C. § 1818(u)(1)(A).

(5) All reports or plans which the Bank or Board has agreed to submit to the Assistant Deputy Comptroller (“ADC”) pursuant to this Agreement shall be forwarded to:

Gerry B. Hagar
Assistant Deputy Comptroller
San Antonio South Field Office
10101 Reunion Place Boulevard, Suite 402
San Antonio, Texas 78216-4165

Article II -- COMPLIANCE COMMITTEE

(1) Within ten (10) days, the Board shall appoint a Compliance Committee of at least five (5) directors, of which no more than two (2) shall be employees of the Bank or any of its affiliates [as the term “affiliate” is defined in 12 U.S.C. § 371c(b)(1)], or a family member of any such person. Upon appointment, the names of the members of the Compliance Committee shall be submitted in writing to the ADC. The Compliance Committee shall be responsible for monitoring and coordinating the Bank's adherence to the provisions of this Agreement.

(2) The Compliance Committee shall meet at least monthly.

(3) Within sixty (60) days of the appointment of the Committee (the first report shall be due March 31, 2004), and quarterly thereafter, the Compliance Committee shall submit a written progress report to the Board setting forth in detail:

- (a) actions taken to comply with each Article of this Agreement; and
- (b) the results of those actions.

(4) The Board shall promptly forward a copy of the Compliance Committee's report, with any additional comments by the Board, to the ADC.

Article III -- **BOARD COOPERATION**

(1) The Board shall immediately adopt a resolution which states that the members of the Board and senior management recognize that they are to act in the best interest of the Bank, and, to that end, they resolve to behave in a businesslike manner and to cooperate in the Board's and the Compliance Committee's efforts to comply with the Articles of this Agreement.

(2) A copy of the resolution shall promptly be forwarded to the ADC.

Article IV -- **MANAGEMENT AND BOARD SUPERVISION STUDY**

(1) Within ninety (90) days, the Compliance Committee shall complete a study of current management and Board supervision presently being provided to the Bank, the Bank's management structure, and its staffing requirements in light of the Bank's present condition. The findings and recommendations shall be set forth in a written report. At a minimum, the report shall contain:

- (a) the identification of present and future management and staffing requirements of each area of the Bank;
- (b) detailed written job descriptions for all executive officers as well as for all other bank employees (i.e., staff employees);
- (c) an evaluation of each officer's and staff employee's qualifications and abilities, and a determination of whether each of these individuals possesses the experience and other qualifications required to perform the present and anticipated duties of his position;

- (d) an evaluation of current lines of authority, reporting responsibilities, and delegation of duties for all officers and staff employees, including identification of any overlapping duties or responsibilities;
- (e) recommendations as to whether management or staffing changes should be made, including the need for additions to or deletions from the current management team and staff complement;
- (f) objectives by which management's and employees' effectiveness will be measured;
- (g) a recommended organization chart that clearly reflects areas of responsibility and lines of authority for all officers, including the Bank's president and chief executive officer, as well as reporting lines for all bank employees;
- (h) an assessment of the Board's strengths and weaknesses, along with a proposal regarding director education programs designed to strengthen identified weaknesses;
- (i) an assessment of whether Board members are receiving adequate information on the operation of the Bank to enable them to fulfill their fiduciary responsibilities and other responsibilities under law;
- (j) recommendations as to whether the scope, frequency, and sufficiency of information provided to the Board by management should be expanded;
- (k) recommendations to correct or eliminate any other deficiencies in the supervision or organizational structure of the Bank.

(2) Within thirty (30) days of completion of this study and report, the Board shall develop, implement, and thereafter ensure Bank adherence to, a written plan, with specific time frames, that will correct any deficiencies which are noted in the report.

(3) Copies of the Board's written plan and of the report shall be forwarded to the ADC. The ADC shall retain the right to determine the adequacy of the report and its compliance with the terms of this Agreement. In the event the written plan, or any portion thereof, is not implemented, the Board shall immediately advise the ADC, in writing, of specific reasons for deviating from the plan.

Article V -- **BOARD'S COMMITTEE STRUCTURE**

(1) Within thirty (30) days, the Compliance Committee shall conduct a review of the Board's committee structure. The review shall include an evaluation of the existing structure and shall include:

- (a) an analysis of the number of Board committees and responsibilities assigned to each;
- (b) an analysis of the composition of each Board committee;
- (c) the creation of a mission statement for each committee;
- (d) a description of specific reports generated by the bank which would be useful to each committee;
- (e) a determination of how often each committee should meet; and,
- (f) specific recommendations to ensure the efficiency and responsiveness of each committee;

(2) Upon completion of the review, a written report setting out the Board's conclusions and recommendations shall be forwarded to the ADC along with a copy of the Board resolution making appropriate adjustments in the committee structure.

Article VI -- **PRODUCTS AND SERVICES - EXISTING OR NEW**

(1) Within sixty (60) days, the Board shall prepare a written analysis of the mortgage lending program which fully assesses the risks and benefits of this line of business. This analysis shall include an assessment of the Bank's controls, procedures, MIS and management of the mortgage lending operation, and shall tie directly to the Bank's strategic plan.

(2) Prior to the Bank's involvement in any new products or services, the Board shall prepare a written analysis of said product or service. The analysis shall, at a minimum, include the following:

- (a) an assessment of the risks and benefits of the product or service to the Bank;
- (b) an explanation of how the product or service is consistent with the Bank's strategic plan;
- (c) an evaluation of the adequacy of the Bank's organizational structure, staffing, MIS, internal controls and written policies and procedures to identify, measure, monitor, and control the risks associated with the product or service; and
- (d) a profitability analysis, including growth projections and interest rate risk.

(3) Upon completion of the analysis, the Board shall promptly forward a copy of it to the ADC.

Article VII -- **CRITICIZED ASSETS**

(1) Within thirty (30) days, the Board shall adopt, implement, and thereafter ensure Bank adherence to, a written program designed to eliminate the basis of criticism of assets criticized in the ROE, in any subsequent Report of Examination, or by any internal or external loan review, or in any list provided to management by the National Bank Examiners during any examination as "doubtful," "substandard," or "special mention." This program shall include, at a minimum:

- (a) an identification of the expected sources of repayment;
- (b) the appraised value of supporting collateral and the position of the Bank's lien on such collateral where applicable;
- (c) an analysis of current and satisfactory credit information, including cash flow analysis where loans are to be repaid from operations; and
- (d) an action plan to eliminate the basis of criticism and the time frame for its accomplishment.

(2) Upon adoption, a copy of the program for all criticized assets equal to or exceeding fifty thousand dollars (\$ 50,000) shall be forwarded to the ADC.

(3) The Board, or a designated committee, shall conduct a review, on at least a quarterly basis, to determine:

- (a) the status of each criticized asset or criticized portion thereof that equals or exceeds fifty thousand dollars (\$50,000);
- (b) management's adherence to the program adopted pursuant to this Article;
- (c) the status and effectiveness of the written program; and
- (d) the need to revise the program or take alternative action.

(4) A copy of each review shall be forwarded to the ADC on a quarterly basis (in a format similar to Appendix A, attached hereto).

(5) The Bank may extend credit, directly or indirectly, including renewals, extensions or capitalization of accrued interest, to a borrower whose loans or other extensions of credit are criticized in the ROE, in any subsequent Report of Examination, in any internal or external loan review, or in any list provided to management by the National Bank Examiners during any examination and whose aggregate loans or other extensions exceed fifty thousand dollars (\$50,000) **only if** each of the following conditions are met:

- (a) the Board or a designated committee finds that the extension of additional credit is necessary to promote the best interests of the Bank, and that prior to renewing, extending or capitalizing any additional credit, a majority of the full Board (or designated committee) approves the credit extension and records, in writing, why such extension is necessary to promote the best interests of the Bank; and,
- (b) a comparison to the written program adopted pursuant to this Article shows that the Board's formal plan to collect or strengthen the criticized asset will not be compromised.

(6) A copy of the approval of the Board or of the designated committee shall be maintained in the file of the affected borrower.

Article VIII-- **OTHER REAL ESTATE OWNED - ACTION PLANS**

(1) Within thirty (30) days, the Board shall adopt, implement, and thereafter ensure Bank adherence to action plans for each parcel of Other Real Estate Owned (“OREO”) to ensure

that these assets are managed in accordance with 12 U.S.C. § 29 and 12 C.F.R. Part 34, Subpart

E. At a minimum, the plans shall:

- (a) identify the Bank officer(s) responsible for managing and authorizing transactions relating to the OREO properties;
 - (b) contain an analysis of each OREO property which compares the cost to carry against the financial benefits of near term sale;
 - (c) detail the marketing strategies for each parcel;
 - (d) identify targeted time frames for disposing of each parcel of OREO;
 - (e) establish targeted write-downs at periodic intervals if marketing strategies are unsuccessful;
 - (f) establish procedures to require periodic market valuations of each property, and the methodology to be used; and
 - (g) provide for reports to the Board on the status of OREO properties on at least a quarterly basis.
- (2) Upon adoption, the Board shall submit a copy of the plans to the ADC.

Article IX -- **CAPITAL POLICY**

(1) By February 15, 2004, the Board shall develop, implement, and thereafter ensure Bank adherence to, a one year capital program. The program shall include:

- (a) specific plans for the maintenance of adequate capital that may in no event be less than the requirements of paragraph (3);
- (b) projections for growth and capital requirements based upon a detailed analysis of the Bank's assets, liabilities, earnings, fixed assets, and off-balance sheet activities;

- (c) projections of the sources and timing of additional capital to meet the Bank's current and future needs;
- (d) the primary source(s) from which the Bank will strengthen its capital structure to meet the Bank's needs;
- (e) contingency plans that identify alternative methods should the primary source(s) under (d) above not be available; and
- (f) a dividend policy that permits the declaration of a dividend only:
 - (i) when the Bank is in compliance with its approved capital program;
 - (ii) when the Bank is in compliance with 12 U.S.C. §§ 56 and 60; and
 - (iii) with the prior determination of no supervisory objection by the ADC.

(2) Upon completion, the Bank's capital program shall be submitted to the ADC for prior determination of no supervisory objection. Upon receiving a determination of no supervisory objection from the ADC, the Bank shall implement and adhere to the capital program. The Board shall review and update the Bank's capital program on an annual basis, or more frequently if necessary. Copies of the reviews and updates shall be submitted to the ADC.

(3) The Bank shall achieve by May 15, 2004, and thereafter maintain the following capital levels (as defined in 12 C.F.R. Part 3):

- (a) Tier 1 capital at least equal to 14 percent (14%) of risk-weighted assets;
- (b) Tier 1 capital at least equal to 8.5 percent (8.5%) of adjusted total assets.¹

¹ Adjusted total assets is defined in 12 C.F.R. § 3.2(a) as the average total asset figure used for Call Report purposes minus end-of-quarter intangible assets. As further noted in 12 C.F.R. § 3.2(a), a bank may be required to compute and maintain its leverage ratio on the basis of actual, rather than average total assets. This language would have to be modified to reflect that change.

(4) The requirement in this Agreement to meet and maintain a specific capital level means that the Bank may not be deemed to be “well capitalized” for purposes of 12 U.S.C. § 1831o and 12 C.F.R. Part 6 pursuant to 12 C.F.R. § 6.4(b)(1)(iv).

Article X -- **STRATEGIC AND PROFIT PLAN**

(1) Within sixty (60) days, the Board shall develop, implement, and thereafter ensure Bank adherence to, a written profit plan to improve and sustain the earnings of the Bank. This plan shall include, at minimum, the following elements:

- (a) identification of the major areas in and means by which the Board will seek to improve the Bank's operating performance;
- (b) realistic and comprehensive budgets, including projected balance sheets and year-end income statements;
- (c) a budget review process to monitor both the Bank's income and expenses, and to compare actual figures with budgetary projections; and
- (d) a description of the operating assumptions that form the basis for major projected income and expense components.

(2) The budgets and related documents required in paragraph (1) above for 2004 shall be submitted to the ADC upon completion. The Board shall submit to the ADC annual budgets as described in paragraph (1) above for each year this Agreement remains in effect. The budget for each year shall be submitted on or before November 30th of the preceding year.

(3) The Board shall forward comparisons of its balance sheet and profit and loss statement, to the profit plan projections to the ADC on a quarterly basis.

Article XI -- ASSET/LIABILITY MANAGEMENT POLICY

(1) Within ninety (90) days, the Board shall adopt, implement, and thereafter ensure Bank adherence to a written liquidity, asset and liability management policy. In formulating this policy, the Board shall refer to the Liquidity booklet, L-L, of the *Comptroller's Handbook*. The policy shall provide for a coordinated asset/liability management strategy and, at a minimum, address:

- (a) adequate management reports that enable the Board and management to monitor the Bank's liquidity position and maintain liquidity at an adequate level;
- (b) development of a liquidity contingency plan;
- (c) guidelines concerning the nature, extent, and purpose of the Bank's use of brokered deposits consistent with the Bank's overall funds management strategies;
- (d) the nature, extent and purpose of Bank borrowings;
- (e) limits on concentrations of funding sources; and
- (f) periodic review of the Bank's adherence to the policy.

(2) Upon adoption, a copy of the written policy shall be forwarded to the ADC for review.

Article XII -- ADMINISTRATIVE APPEALS AND EXTENSIONS OF TIME

(1) If the Board determines that an exception to any provision of this Agreement is in the best interests of the Bank, or requires an extension of any timeframe within this Agreement, the Board shall submit a written request to the ADC asking for relief.

(2) Any written requests submitted pursuant to this Article shall include a statement setting forth in detail the special circumstances that prevent the Bank from complying with any provision, that require the ADC to exempt the Bank from any provision, or that require an extension of any timeframe within this Agreement. All such requests shall be accompanied by relevant supporting documentation.

(3) The ADC's decision in granting the request is final and not subject to further review.

Article XIII -- CLOSING

(1) Although the Board has agreed to submit certain programs and reports to the ADC for review or prior determination of no supervisory objection, the Board has the ultimate responsibility for proper and sound management of the Bank.

(2) The Board shall ensure that the Bank has processes, personnel, and control systems to ensure implementation of and adherence to the policies developed pursuant to this Agreement.

(3) It is expressly and clearly understood that if, at any time, the Comptroller deems it appropriate in fulfilling the responsibilities placed upon him/her by the several laws of the United States of America to undertake any action affecting the Bank, nothing in this Agreement shall in any way inhibit, estop, bar, or otherwise prevent the Comptroller from so doing.

(4) Any time limitations imposed by this Agreement shall begin to run from the effective date of this Agreement. Such time requirements may be extended in writing by the ADC for good cause upon written application by the Board.

(5) The provisions of this Agreement shall be effective upon execution by the parties hereto and its provisions shall continue in full force and effect unless or until such provisions are

amended in writing by mutual consent of the parties to the Agreement or excepted, waived, or terminated in writing by the Comptroller.

(6) This Agreement is intended to be, and shall be construed to be, a supervisory “written agreement entered into with the agency” as contemplated by 12 U.S.C. § 1818(b)(1), and expressly does not form, and may not be construed to form, a contract binding on the OCC or the United States. Notwithstanding the absence of mutuality of obligation, or of consideration, or of a contract, the OCC may enforce any of the commitments or obligations herein undertaken by the Bank under its supervisory powers, including 12 U.S.C. § 1818(b)(1), and not as a matter of contract law. The Bank expressly acknowledges that neither the Bank nor the OCC has any intention to enter into a contract. The Bank also expressly acknowledges that no OCC officer or employee has statutory or other authority to bind the United States, the U.S. Treasury Department, the OCC, or any other federal bank regulatory agency or entity, or any officer or employee of any of those entities to a contract affecting the OCC’s exercise of its supervisory responsibilities. The terms of this Agreement, including this paragraph, are not subject to amendment or modification by any extraneous expression, prior agreements or prior arrangements between the parties, whether oral or written.

IN TESTIMONY WHEREOF, the undersigned, authorized by the Comptroller, has hereunto set his hand on behalf of the Comptroller.

/s/ Gerry B. Hagar
Gerry B. Hagar
Assistant Deputy Comptroller
San Antonio South Field Office

1/26/04
Date

AND IN FURTHER TESTIMONY WHEREOF, the undersigned, as the duly elected and acting Board of Directors of the Bank, have hereunto set their hands on behalf of the Bank.

| NAME: | SIGNATURE: | DATE: |
|------------------|-------------------|--------------|
| Ellen Bartnesky | Signed | 1-26-04 |
| Cheryl Bellamy | Signed | 1-26-04 |
| Nadine Crenshaw | Signed | 1-26-04 |
| Kenneth Eilers | Signed | 1-26-04 |
| Robert Eilers | Signed | 1-26-04 |
| Jean Lauder | Signed | 1/26/04 |
| W.B. Lauder, Jr. | Signed | 1-26-04 |
| Ralph H. Lauder | Signed | 1/26/04 |
| Gail V. Lauder | Signed | 1/26/04 |
| Isaac Rodriguez | | |
| Lloyd Schwarz | Signed | 1/26/04 |

APPENDIX A
MERCEDES NATIONAL BANK
MERCEDES, TEXAS

CRITICIZED ASSET REPORT AS OF: _____

BORROWER(S): _____

ASSET BALANCE(S) AND OCC RATING (SM, SUBSTANDARD, DOUBTFUL OR LOSS):

\$ _____ CRITICISM _____

AMOUNT CHARGED OFF TO DATE _____

FUTURE POTENTIAL CHARGE-OFF _____

PRESENT STATUS (Fully explain any increase in outstanding balance; include past due status, nonperforming, significant progress or deterioration, etc.):

FINANCIAL AND/OR COLLATERAL SUPPORT (include brief summary of most current financial information, appraised value of collateral and/or estimated value and date thereof, bank's lien position and amount of available equity, if any, guarantor(s) info, etc.):

PROPOSED PLAN OF ACTION TO ELIMINATE ASSET CRITICISM(S) AND TIME FRAME FOR ITS ACCOMPLISHMENT:

IDENTIFIED SOURCE OF REPAYMENT AND DEFINED REPAYMENT PROGRAM (repayment program should coincide with source of repayment):

Use this form for reporting each criticized asset that exceeds fifty thousand dollars (\$50,000) and retain the original in the credit file for review by the examiners. Submit your reports quarterly until notified otherwise, in writing, by the Assistant Deputy Comptroller.