



**F. WAYNE WALKER**

EXECUTIVE VICE PRESIDENT & CFO

February 18, 2011

Ms. Jennifer J. Johnson

Secretary

Board of Governors of the Federal Reserve System

20th Street and Constitution Avenue, NW.

Washington, DC 20551

RE: **OUR OPPOSITION** to the Durbin Amendment to Dodd-Frank Bill; Docket No. R-1404

Dear Ms. Johnson:

Much has already been written concerning the negative impact of this legislation on banks, communities and customers. Capital Bank will be impacted in all of the ways already presented....negative pressure on earnings forcing us to either raise other fees, develop new fees or cut services. None of these options will be a positive for our customers. Anyone that believes merchants will use their lower cost for processing transactions to reduce cost to consumers is living in a fantasy world. Our politicians have looked at billion dollar income amounts that banks receive from interchange fees and decided banks are making too much from this service. It appears very little attention has been paid to the cost of providing these services in the real world.

Most banks, other than large regional or national banks, find that the most efficient way to acquire the expertise and access to card networks is through a third party processor. Capital Bank uses such a processor to drive our ATM network and process/settle for card transactions. We pay for our customers using other ATMs and we receive fees when non-Capital Bank customers use our ATMs. We pay for the cost to process transactions our customers conduct at merchants and we receive interchange income to help reimburse our bank for all the costs associated with this process.

Perhaps it will be beneficial to break this down to the impact on a single institution. Capital Bank has assets of slightly over \$250 million and has served communities in the Houston area for over 45 years. We are a for-profit institution and if regulations such as the Durbin Amendment place unrealistic caps on a reasonable source of income we will be forced to raise fees in other areas or cut back on services. To illustrate, provided below are a few key statistics for 2010 to illustrate how limiting interchange fees will impact our bank:

- Gross interchange fees as a % of Total Revenue = .21%
- Gross interchange fees as a % of Net Revenue = .87%
- Gross interchange fees as a % of Total non-interest income = 1.24%

- Fraud losses from debit card operations for our bank in 2009 were \$7,916.74. Losses in 2010 were \$4,321.88. There is no reason to believe these losses will not continue to be significant, especially since the majority of the burden for card fraud is placed on the issuing bank with merchants having very little responsibility for trying to reduce fraud.

Our attachment shows a few statistics which I would like to share with you. We expect a 70% reduction in our interchange fees which will reduce our income by .61%! That, coupled with the reduction of NSF fee income and increased interest expense due to Reg Q, we anticipate a total reduction of net income in the amount of \$1.1 million! That's a 54.01% total reduction in net income! I repeat: A potential **54.01% reduction in our net income!** Given this worst case scenario, this equates to a potential loss that **cannot** be made up in the local economy. Community Banks like ours only increase Equity Capital through retained net income. If net income is reduced, so is our capital growth. That leads to less lending by banks. While we are a healthy bank, there will be a far greater impact on banks that aren't as healthy as we are. Banks will have to ration capital which will lead to an unintended capital crunch. Is this what the Federal Reserve, Congress, and Regulators really wanted?

Furthermore, let me illustrate an example of an issue that occurs frequently. In speaking with our debit card processor, we were informed that one of our customers rented a car from Hertz and signed the authorization form showing a smaller amount since the final amount is not known at the time of the initial transaction. Hertz used an authorization code to charge the smaller amount, which the customer was paying weekly. When the customer stopped making payments to Hertz, they re-ran the same authorization code and charged the debit card with the full amount.

Merchants like Hertz are protected under the Travel and Expense Rule and we, as the card issuer, must bear all the risk. We could not dispute the charge due the T&E Rule. Our bank lost over \$1,700 on this one transaction. If our interchange revenue is expected to be cut by 70%, we cannot afford such losses. This was just ONE customer! Yet another unintended consequence of why this Amendment must be repealed. Please stop or delay implementation of this Amendment.

There appears to be little evidence of how this Amendment will positively impact the banking industry, customers or the economy. Sources of income cannot be taken away from any business segment without weakening that segment or forcing other sources of income to be developed. In summary, I urge you to stop the far-reaching negative implications for the banking industry, consumers and the economy at large.

Sincerely,



F. Wayne Walker  
Executive Vice President and  
Chief Financial Officer

cc: American Bankers Association  
Texas Bankers Association

<b>Capital Bank</b>
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	YTD 2010	% Non-Int Inc	% Revenue	% PBT
Interest Income	\$12,406,600			
Interest Expense	\$1,833,300			
<b>NET INTEREST INCOME</b>	<b>\$10,573,300</b>			
Provision for Loan Losses	\$464,500			
<b>NET INT INCOME AFTER PLLL</b>	<b>\$10,108,800</b>			
Interchange Income	\$26,000	1.24%	0.21%	0.87%
NSF Fee Income	\$1,178,300	56.17%	9.30%	39.51%
Other Non-Interest Income	\$893,500			
<b>TOTAL NON-INTEREST INCOME</b>	<b>\$2,097,800</b>			
<b>TOTAL NON-INTEREST EXPENSE</b>	<b>\$9,292,300</b>			
<b>Non-recurring Income</b>	<b>\$68,000</b>			
<b>PROFIT BEFORE FIT</b>	<b>\$2,982,300</b>			
Federal Income Tax	\$1,021,700			
<b>NET INCOME</b>	<b>\$1,960,600</b>			

**Capital Bank**

<b>Reduction in Interchange of:</b>	<b>30%</b>	<b>50%</b>	<b>70%</b>
<i>Reduction in net income of:</i>	\$5,000	\$8,000	\$12,000
Percentage reduction in net income:	0.26%	0.41%	0.61%
Current tier 1 capital ratio:	8.66%	8.66%	8.66%
<i>Reduction in funds available to lend:</i>	\$58,000	\$92,000	\$139,000

<b>Reduction in NSF Fee Income of:</b>	<b>30%</b>	<b>50%</b>	<b>70%</b>
Reduction in net income of:	\$230,000	\$383,000	\$536,000
Percentage reduction in net income:	11.73%	19.53%	27.34%
Current tier 1 capital ratio:	8.66%	8.66%	8.66%
Reduction in funds available to lend:	\$2,656,000	\$4,423,000	\$6,189,000

<b>Increase Interest Expense from Reg Q Repeal:</b>			
Average collected balance:	\$39,283,490	\$39,283,490	\$39,283,490
Average rate paid:	0.25%	1.00%	2.00%
Reduction in net income of:	\$64,000	\$255,000	\$511,000
Percentage reduction in net income:	3.26%	13.01%	26.06%
Current tier 1 capital ratio:	8.66%	8.66%	8.66%
Reduction in funds available to lend:	\$739,000	\$2,945,000	\$5,901,000

<b>Combined Impact of All Three:</b>			
<i>Reduction in net income of:</i>	\$299,000	\$646,000	<b>\$1,059,000</b>
<i>Percentage reduction in net income:</i>	15.25%	32.95%	<b>54.01%</b>
Current tier 1 capital ratio:	8.66%	8.66%	8.66%
Reduction in funds available to lend:	\$3,453,000	\$7,460,000	<b>\$12,229,000</b>

<b>FUNDS NOT AVAILABLE TO LEND ANNUALLY:</b>	<b>\$3,453,000</b>	<b>\$7,460,000</b>	<b>\$12,229,000</b>
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Capital Bank is headquartered in Jacinto City, Texas  
 As of January 31, 2011, Total assets were: \$256.7 Million  
[www.capitalbanktx.com](http://www.capitalbanktx.com)  
 Contact: F. Wayne Walker at 713-672-1498