FIRST FINANCIAL BANKSHARES

J. Bruce Hildebrand
Executive Vice President
and Chief Financial Officer

September 6, 2012

Comptroller of the Currency
Administrator of National Banks
Washington, DC 20219

email: regs.comments@occ.treas.gov

RE: Basel III OCC Docket ID OCC-2012-0008, 0009, and 0010

Federal Deposit Insurance Corporation
Executive Secretary Section
550 17th Street, N. W.
Washington, DC 20429

email: comments@FDIC.gov

RE: Basel III FDIC RIN 3064-AD95, RIN 3064-AD96, and RIN 3064-D97

Board of Governors of the
Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

email: regs.comments@federalreserve.gov

RE: Basel III docket No. 1442

Gentlemen:

First Financial Bankshares, Inc. is a $4.3 billion bank holding company, which owns eleven separately charted community banks in West and Central Texas. We are publicly traded on NASDAQ under the symbol FFIN with a market capitalization of approximately $1.0 billion. Our banks are extremely community focused with local management and heavy community involvement. Our capital is strong with a 10.36% leverage ratio, a 17.23% risked based capital ratio and an 18.48% total risked capital ratio as of June 30, 2012 under today's regulations. We were voted the #2 ranked bank by Bank Director Magazine in the $1 to $5 billion category of publicly traded banks, and have been ranked #1 or #2 for the past four years.

We are writing to you to express our strong concerns over the new Basel III capital proposals. In summary, while we believe strong capital is paramount in banking and certainly community banking, we do not believe that Basel III was intended to be implemented at the community bank

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level and the changes and complexity required under Basel III will be a large detriment to community banks, which could force many community banks to close (if they cannot raise additional capital) and add significant costs to the operations of banks that could force community banks to reduce important products and services for its customers, thus greatly hurting consumers and the United States economy. Basel III is not needed because you as the industry regulators are already making sure banks have adequate capital to operate in a safe and sound manner.

We will address six (6) areas of the Basel III proposals, that we believe directly impact community banks. The Basel III proposal is extremely complex and we are not saying these are the only provisions of Basel III that negatively impact community banks, but with these six areas you can clearly see how community banks are adversely affected.

1. Background: The proposal requires that all unrealized gains and losses in available for sale securities (AFS) must "flow through" to common equity tier 1 (CET1), a new term. Gains and losses in AFS portfolios occur primarily as a result of interest rate movements as opposed to changes in credit risk. Interest rates in debt securities can fluctuate frequently (often daily), and the proposed rules will cause significant volatility in capital calculations.

   Our eleven banks have $1.96 billion in AFS securities at June 30, 2012. As interest rates rise (and they ultimately will), our capital ratios will be adversely affected. We would likely have to change our investment strategy to stay very short in the market to minimize volatility. Should we limit our investments in longer duration assets? How will this affect local governments and the housing markets that depend on community banks to purchase longer term municipal bonds and mortgage backed securities. We are concerned about how this proposal might impact our asset/liability function and our liquidity, contingency funding plans and earnings.

   We are a community bank and, as such, should not be forced into the "mark-to-market" frenzy that has consumed other segments of the financial services industry.

   In addition, this proposal will cause an increase in employee time to monitor our AFS portfolio. This may also require us to purchase software to stay in compliance. Both of these will add costs and lead to less time and service for our customers.

2. Background: The Dodd-Frank Act grandfathers Trust Preferred Securities (TruPs) for banks between $500 million and $415 billion. The Basel III proposal requires a complete phase out of TruPs. 90% of carrying value is allowed in 2013, with an annual decrease of 10% thereafter.

   While our banks do not have outstanding TruPs, community banks sold TruPs and put the capital in the banks based on the encouragement of the regulators and in full compliance with the regulations. To now disallow the TruPs under the Basel III proposal, community banks would have to decide how to replace the capital, which would not be easy to do in today's economy. Another alternative is to shrink the bank and reduce assets. This would mean less loans available for customers, less people hired by the community banks and, overall, a very negative impact for the consumer and our economy.

3. Background: The proposal assigns increased risk weights for residential home mortgages based on whether they are "traditional mortgages" in Category 1 or "riskier" in Category 2.

   Banks will be required to re-assess a mortgage after a restructuring or modification, except for HAMP loans. The proposal also does not recognize private mortgage insurance and there are no grandfather clauses. Banks will have to re-examine all loans on the books to determine if they come under the appropriate category and loan-to-value (LTV) for each mortgage. Risk weighting of these loans could double under the Basel III proposal.

   Our eleven banks have approximately 25% of our assets in mortgage assets. In addition, we originate approximately $170 million in mortgage loans that are sold to upstream banks in the secondary market.

   The most likely result of this proposal is that the availability of mortgages in the communities where we offer loans will be reduced.

In addition, our capital ratios will be negatively impacted from higher risk weighting resulting in the potential for us to have to raise additional capital. For certain, the regulatory burden, in additional to all the Dodd-Frank Act regulatory changes, will significantly increase the costs to originate mortgage loans and discourage community banks from being in the business. Obviously this will hurt the home building industry and stymie the economy recovery.

4. Background: The proposal defines "High Volatility Commercial Real Estate" (HVCRE) as acquisition, development and construction (ADC) commercial real estate loans except:

    1. One-to- four family residential ADC loans; or
    2. Commercial real estate ADC loans that meet LTV requirements, the borrowers' cash in the project is at least 15% of the "appraised as completed" value prior to the advancement of funds by the bank and the borrower is required to remain in the project until the credit facility is converted to permanent financing, sold or paid in full.

    HVCRE loans are assigned a 150% risk weight compared to current risk weighting of 100%.

    Community banks are very active in financing construction projects in our market. By increasing the risk weighting to 150% or higher, our bank's capital will have to be bolstered and the cost of our loans will increase which will result in less construction projects, job losses and very negative effect on the economy.

    In addition, the definitions and rules in this area are very complex, difficult to understand, and will likely result in additional labor and software costs to comply.

5. Background: The proposed rules will not allow banks to count as part of their common equity tier 1 (CET1) any mortgage servicing assets (net of deferred tax liabilities) that exceed 10% of their CET1. When aggregated with deferred tax assets and investments in common stock of an unconsolidated financial entity, all of that together may not exceed 15%.

While our banks do not have mortgage servicing rights on our balance sheet, many community banks do and if they are to continue servicing mortgages, will have to raise capital, something that is not easy for a community bank.

If community banks discontinue these services, customers will be harmed and so will earnings.

When you combine this proposal with the increased risk weighting for mortgage assets (see #3 above) that is also in Basel III, this will have a significant negative impact on the mortgage industry and our economy.

6. Background: The Basel III proposal will require all banks to collect new and often granular information in order to calculate risk weighted assets. New information will have to be obtained, maintained and reported in order to satisfy underwriting features as well as LTV features to satisfy due diligence requirements. Existing loans are not grandfathered. Information will have to be reported in different ways and with greater frequency. Monitoring capital with the new AFS requirements will also be time consuming.

   Our bank has approximately 950 employees. We are already laboring in an environment involving increased regulatory scrutiny in compliance exams and the new burdens being placed on us by the Dodd-Frank Act. Our compliance costs alone have increased significantly in the last 3 years and we have more than doubled our compliance staff.

   It appears that as proposed, Basel III will require us to change our internal reporting systems and provide additional employee training. More than likely we will have to hire additional employees. The complexity of the data requests most likely means that we will also have to install new software systems and/or look for third parties to provide them. The compliance costs will pull money out of capital and earnings rather than help our borrowers.

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As can be seen from just these six examples, Basel III will have a very negative impact on community banks that we believe was never intended. We have closely followed the evolution of Basel III over the years and its objective has primarily centered on money centered, very large banks, including international. These banks have complex operations, including investment banking operations and derivative trading, that Basel III was focused on addressing.

We therefore recommend and request that a size and complexity of operations scope be established that would exclude community banks from the provisions of Basel III.

Thank you for allowing us to share our opinions on Basel III.

Sincerely,

J. Bruce Hildebrand
Executive Vice President
and Chief Financial Officer

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