TEXAS CAPITAL BANCSHARES INC/TX
Form 10-Q
July 23, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

ý Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

For the quarterly period ended June 30, 2015

.. Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

For the transition period from to
Commission file number 001-34657

TEXAS CAPITAL BANCSHARES, INC.
(Exact Name of Registrant as Specified in Its Charter)

Delaware	75-2679109
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
2000 McKinney Avenue, Suite 700, Dallas, Texas, U.S.A.	75201
(Address of principal executive officers)	(Zip Code)

214/932-6600
(Registrant's telephone number, including area code)
N/A
(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act 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 ý No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, 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 ý ¨ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of “large accelerated filer” and “accelerated filer” Rule 12b-2 of the Exchange Act.

Large Accelerated Filer	ý	Accelerated Filer	¨
Non-Accelerated Filer	¨	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 ý

APPLICABLE ONLY TO CORPORATE ISSUERS:

On July 21, 2015, the number of shares set forth below was outstanding with respect to each of the issuer’s classes of common stock:

Common Stock, par value $0.01 per share 45,819,304

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PART I – FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS
TEXAS CAPITAL BANCSHARES, INC.
CONSOLIDATED BALANCE SHEETS
(In thousands except share data)

	June 30, 2015 (Unaudited)	December 31, 2014
Assets		
Cash and due from banks	$117,387	$96,524
Interest-bearing deposits	1,321,064	1,233,990
Federal funds sold and securities purchased under resale agreements	16,300	—
Securities, available-for-sale	35,361	41,719
Loans held for investment, mortgage finance	4,906,415	4,102,125
Loans held for investment (net of unearned income)	11,123,325	10,154,887
Less: Allowance for loan losses	118,770	100,954
Loans held for investment, net	15,910,970	14,156,058
Premises and equipment, net	17,951	17,368
Accrued interest receivable and other assets	378,068	333,699
Goodwill and intangible assets, net	20,237	20,588
Total assets	$17,817,338	$15,899,946
Liabilities and Stockholders' Equity		
Liabilities:		
Deposits:		
Non-interest-bearing	$6,479,073	$5,011,619
Interest-bearing	7,502,937	7,348,972
Interest-bearing in foreign branches	206,266	312,709
Total deposits	14,188,276	12,673,300
Accrued interest payable	4,905	4,747
Other liabilities	161,215	145,622
Federal funds purchased and repurchase agreements	109,007	92,676
Other borrowings	1,400,000	1,100,005
Subordinated notes	286,000	286,000
Trust preferred subordinated debentures	113,406	113,406
Total liabilities	16,262,809	14,415,756
Stockholders' equity:		
Preferred stock, $.01 par value, $1,000 liquidation value:		
Authorized shares – 10,000,000		
Issued shares – 6,000,000 shares issued at June 30, 2015 and December 31, 2014	150,000	150,000
Common stock, $.01 par value:		
Authorized shares – 100,000,000		
Issued shares – 45,813,388 and 45,735,424 at June 30, 2015 and December 31, 2014, respectively	458	457
Additional paid-in capital	712,222	709,738
Retained earnings	690,826	622,714
Treasury stock (shares at cost: 417 at June 30, 2015 and December 31, 2014)	(8)	(8)
Accumulated other comprehensive income, net of taxes	1,031	1,289
Total stockholders' equity	1,554,529	1,484,190
Total liabilities and stockholders' equity	$17,817,338	$15,899,946

See accompanying notes to consolidated financial statements.

TEXAS CAPITAL BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF INCOME AND OTHER COMPREHENSIVE INCOME – UNAUDITED
(In thousands except per share data)

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Interest income				
Interest and fees on loans	$151,606	$124,234	$290,780	$240,106
Securities	323	471	681	1,011
Federal funds sold and securities purchased under resale agreements	118	8	234	48
Deposits in other banks	1,327	100	2,587	259
Total interest income	153,374	124,813	294,282	241,424
Interest expense				
Deposits	5,642	4,246	11,270	8,276
Federal funds purchased	93	115	161	210
Repurchase agreements	4	4	8	8
Other borrowings	528	181	918	253
Subordinated notes	4,191	4,241	8,382	7,720
Trust preferred subordinated debentures	631	619	1,249	1,235
Total interest expense	11,089	9,406	21,988	17,702
Net interest income	142,285	115,407	272,294	223,722
Provision for credit losses	14,500	4,000	25,500	9,000
Net interest income after provision for credit losses	127,785	111,407	246,794	214,722
Non-interest income				
Service charges on deposit accounts	2,149	1,764	4,243	3,460
Trust fee income	1,287	1,242	2,487	2,524
Bank owned life insurance (BOLI) income	476	521	960	1,030
Brokered loan fees	5,277	3,357	9,509	6,181
Swap fees	1,035	410	3,021	1,634
Other	2,547	3,239	4,818	6,060
Total non-interest income	12,771	10,533	25,038	20,889
Non-interest expense				
Salaries and employee benefits	48,200	39,896	94,028	81,952
Net occupancy expense	5,808	5,073	11,499	9,841
Marketing	3,925	3,795	8,143	7,554
Legal and professional	5,618	7,181	9,666	12,583
Communications and technology	5,647	4,361	10,725	8,285
FDIC insurance assessment	4,211	2,544	8,001	5,269
Allowance and other carrying costs for OREO	6	11	15	56
Other	7,861	6,904	15,716	13,542
Total non-interest expense	81,276	69,765	157,793	139,082
Income before income taxes	59,280	52,175	114,039	96,529
Income tax expense	21,343	18,754	41,052	34,843
Net income	37,937	33,421	72,987	61,686
Preferred stock dividends	2,437	2,437	4,875	4,875
Net income available to common stockholders	$35,500	$30,984	$68,112	$56,811
Other comprehensive income (loss)				
Change in net unrealized gain on available-for-sale securities arising during period, before-tax	$(321)	$43	$(397)	$(118)

Income tax expense (benefit) related to net unrealized gain on available-for-sale securities	(112)	15	(139)	(41)
Other comprehensive income (loss), net of tax	(209)	28	(258)	(77)
Comprehensive income	$37,728	$33,449	$72,729	$61,609
Basic earnings per common share	$0.78	$0.72	$1.49	$1.33
Diluted earnings per common share	$0.76	$0.71	$1.47	$1.30

See accompanying notes to consolidated financial statements.

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TEXAS CAPITAL BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY - UNAUDITED
(In thousands except share data)

	Preferred Stock		Common Stock				Treasury Stock			
	Shares	Amount	Shares	Amount	Additional Paid-in Capital	Retained Earnings	Shares	Amount	Accumulated Other Comprehensive Income (Loss), Net of Taxes	Total
Balance at December 31, 2013	6,000,000	$150,000	41,036,787	$410	$448,208	$496,112	(417)	$(8)	$1,628	$1,096,350
Comprehensive income:										
Net income	—	—	—	—	—	61,686	—	—	—	61,686
Change in unrealized gain on available-for-sale securities, net of taxes of $41	—	—	—	—	—	—	—	—	(77)	(77)
Total comprehensive income										61,609
Tax benefit related to exercise of stock-based awards	—	—	—	—	1,479	—	—	—	—	1,479
Stock-based compensation expense recognized in earnings	—	—	—	—	2,528	—	—	—	—	2,528
Issuance of preferred stock	—	—	—	—	—	—	—	—	—	—
Preferred stock dividend	—	—	—	—	—	(4,875)	—	—	—	(4,875)
Issuance of stock related to stock-based awards	—	—	94,845	1	(824)	—	—	—	—	(823)
Issuance of common stock	—	—	1,875,000	19	106,529	—	—	—	—	106,548
Issuance of common stock related to warrants	—	—	99,229	1	(1)	—	—	—	—	—
	6,000,000	$150,000	43,105,861	$431	$557,919	$552,923	(417)	$(8)	$1,551	$1,262,816

Balance at June 30, 2014										
Balance at December 31, 2014	6,000,000	$150,000	45,735,424	$457	$709,738	$622,714	(417)	$(8)	$1,289	$1,484,190
Comprehensive income:										
Net income	—	—	—	—	—	72,987	—	—	—	72,987
Change in unrealized gain on available-for-sale securities, net of taxes of $139	—	—	—	—	—	—	—	—	(258)	(258)
Total comprehensive income										72,729
Tax benefit related to exercise of stock-based awards	—	—	—	—	736	—	—	—	—	736
Stock-based compensation expense recognized in earnings	—	—	—	—	2,103	—	—	—	—	2,103
Preferred stock dividend	—	—	—	—	—	(4,875)	—	—	—	(4,875)
Issuance of stock related to stock-based awards	—	—	77,964	1	(355)	—	—	—	—	(354)
Balance at June 30, 2015	6,000,000	$150,000	45,813,388	$458	$712,222	$690,826	(417)	$(8)	$1,031	$1,554,529

See accompanying notes to consolidated financial statements.

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TEXAS CAPITAL BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS—UNAUDITED
(In thousands)

	Six months ended June 30, 2015	2014
Operating activities		
Net income from continuing operations	$72,987	$61,686
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	25,500	9,000
Depreciation and amortization	8,289	6,693
Amortization and accretion on securities	—	—
Bank owned life insurance (BOLI) income	(960)	(1,030)
Stock-based compensation expense	6,641	7,233
Excess tax expense from stock-based compensation arrangements	(779)	(1,479)
Gain on sale of assets	24	(709)
Changes in operating assets and liabilities:		
Accrued interest receivable and other assets	(50,485)	(51,854)
Accrued interest payable and other liabilities	12,090	(1,324)
Net cash provided by operating activities	73,307	28,216
Investing activities		
Maturities and calls of available-for-sale securities	1,950	8,474
Principal payments received on available-for-sale securities	4,011	5,292
Originations of mortgage finance loans	(45,359,254)	(23,694,564)
Proceeds from pay-offs of mortgage finance loans	44,554,964	22,778,580
Net increase in loans held for investment, excluding mortgage finance loans	(976,122)	(671,896)
Purchase (disposal) of premises and equipment, net	(2,635)	(6,193)
Proceeds from sale of foreclosed assets	1,164	5,763
Net cash used in investing activities	(1,775,922)	(1,574,544)
Financing activities		
Net increase in deposits	1,514,976	1,499,937
Net expense from issuance of stock related to stock-based awards	(354)	(823)
Net proceeds from issuance of common stock	—	106,548
Preferred dividends paid	(4,875)	(4,875)
Net increase (decrease) in other borrowings	299,995	(149,473)
Excess tax benefits from stock-based compensation arrangements	779	1,479
Net increase in Federal funds purchased and repurchase agreements	16,331	124,391
Net proceeds from issuance of subordinated notes	—	172,375
Net cash provided by financing activities	1,826,852	1,749,559
Net increase in cash and cash equivalents	124,237	203,231
Cash and cash equivalents at beginning of period	1,330,514	153,911
Cash and cash equivalents at end of period	$1,454,751	$357,142
Supplemental disclosures of cash flow information:		
Cash paid during the period for interest	$21,830	$13,780
Cash paid during the period for income taxes	42,934	33,702
Transfers from loans/leases to OREO and other repossessed assets	1,177	851

See accompanying notes to consolidated financial statements.

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TEXAS CAPITAL BANCSHARES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—UNAUDITED
(1) OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES
Organization and Nature of Business
Texas Capital Bancshares, Inc. (the “Company”), a Delaware corporation, was incorporated in November 1996 and commenced banking operations in December 1998. The consolidated financial statements of the Company include the accounts of Texas Capital Bancshares, Inc. and its wholly owned subsidiary, Texas Capital Bank, National Association (the “Bank”). We serve the needs of commercial businesses and successful professionals and entrepreneurs located in Texas as well as operate several lines of business serving a regional or national clientele of commercial borrowers. We are primarily a secured lender, with our greatest concentration of loans in Texas.
Basis of Presentation
Our accounting and reporting policies conform to accounting principles generally accepted in the United States (“GAAP”) and to generally accepted practices within the banking industry. Certain prior period balances have been reclassified to conform to the current period presentation.
The consolidated interim financial statements have been prepared without audit. Certain information and footnote disclosures presented in accordance with GAAP have been condensed or omitted. In the opinion of management, the interim financial statements include all normal and recurring adjustments and the disclosures made are adequate to make the interim financial information not misleading. The consolidated financial statements have been prepared in accordance with GAAP for interim financial information and the instructions to Form 10-Q adopted by the Securities and Exchange Commission (“SEC”). Accordingly, the financial statements do not include all of the information and footnotes required by GAAP for complete financial statements and should be read in conjunction with our consolidated financial statements, and notes thereto, for the year ended December 31, 2014, included in our Annual Report on Form 10-K filed with the SEC on February 19, 2015 (the “2014 Form 10-K”). Operating results for the interim periods disclosed herein are not necessarily indicative of the results that may be expected for a full year or any future period.
Use of Estimates
The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Actual results could differ from those estimates. The allowance for loan losses, the fair value of stock-based compensation awards, the fair values of financial instruments and the status of contingencies are particularly susceptible to significant change in the near term.

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(2) EARNINGS PER COMMON SHARE

The following table presents the computation of basic and diluted earnings per share (in thousands except per share data):

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Numerator:				
Net income	$37,937	$33,421	$72,987	$61,686
Preferred stock dividends	2,437	2,437	4,875	4,875
Net income available to common stockholders	35,500	30,984	$68,112	56,811
Denominator:				
Denominator for basic earnings per share— weighted average shares	45,790,093	43,075,213	45,774,461	42,735,580
Effect of employee stock-based awards(1)	229,378	336,993	219,448	359,794
Effect of warrants to purchase common stock	423,942	432,809	411,281	486,113
Denominator for dilutive earnings per share—adjusted weighted average shares and assumed conversions	46,443,413	43,845,015	46,405,190	43,581,487
Basic earnings per common share	$0.78	$0.72	$1.49	$1.33
Diluted earnings per common share	$0.76	$0.71	$1.47	$1.30

(1) Stock options, SARs and RSUs outstanding of 173,382 at June 30, 2015 and 46,000 at June 30, 2014 have not been included in diluted earnings per share because to do so would have been anti-dilutive for the periods presented.

(3) SECURITIES

Securities are identified as either held-to-maturity or available-for-sale based upon various factors, including asset/liability management strategies, liquidity and profitability objectives and regulatory requirements.
Held-to-maturity securities are carried at cost, adjusted for amortization of premiums or accretion of discounts.
Available-for-sale securities are securities that may be sold prior to maturity based upon asset/liability management decisions. Securities identified as available-for-sale are carried at fair value. Unrealized gains or losses on available-for-sale securities are recorded as accumulated other comprehensive income in stockholders’ equity, net of taxes. Amortization of premiums or accretion of discounts on mortgage-backed securities is periodically adjusted for estimated prepayments. Realized gains and losses and declines in value judged to be other-than-temporary are included in gain (loss) on sale of securities. The cost of securities sold is based on the specific identification method.
At June 30, 2015, our net unrealized gain on the available-for-sale securities portfolio was $1.6 million compared to $2.0 million at December 31, 2014. As a percent of outstanding balances, the unrealized gain was 4.70% and 4.99% at June 30, 2015, and December 31, 2014, respectively. The decrease in the unrealized gain percentage at June 30, 2015 is related to the reduction in the portfolio balance due to paydowns and maturities.

The following is a summary of available-for-sale securities (in thousands):

	June 30, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale securities:				
Residential mortgage-backed securities	$24,945	$1,781	$—	$26,726
Municipals	1,308	5	—	1,313
Equity securities(1)	7,522	12	(212)	7,322
	$33,775	$1,798	$(212)	$35,361

	December 31, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale securities:				
Residential mortgage-backed securities	$28,957	$2,108	$—	$31,065
Municipals	3,257	10	—	3,267
Equity securities(1)	7,522	16	(151)	7,387
	$39,736	$2,134	$(151)	$41,719

(1) Equity securities consist of Community Reinvestment Act funds.

The amortized cost and estimated fair value of available-for-sale securities are presented below by contractual maturity (in thousands, except percentage data):

	June 30, 2015				
	Less Than One Year	After One Through Five Years	After Five Through Ten Years	After Ten Years	Total
Available-for-sale:					
Residential mortgage-backed securities:(1)					
Amortized cost	$71	$6,800	$4,890	$13,184	$24,945
Estimated fair value	72	7,105	5,479	14,070	26,726
Weighted average yield(3)	5.53 %	4.77 %	5.54 %	2.40 %	3.67 %
Municipals:(2)					
Amortized cost	745	563	—	—	1,308
Estimated fair value	747	566	—	—	1,313
Weighted average yield(3)	5.51 %	5.69 %	—	—	5.59 %
Equity securities:(4)					
Amortized cost	7,522	—	—	—	7,522
Estimated fair value	7,322	—	—	—	7,322
Total available-for-sale securities:					
Amortized cost					$33,775
Estimated fair value					$35,361

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	December 31, 2014				
	Less Than One Year	After One Through Five Years	After Five Through Ten Years	After Ten Years	Total
Available-for-sale:					
Residential mortgage-backed securities:(1)					
Amortized cost	$1	$9,151	$5,661	$14,144	$28,957
Estimated fair value	1	9,662	6,333	15,069	31,065
Weighted average yield(3)	6.50 %	4.79 %	5.54 %	2.36 %	3.75 %
Municipals:(2)					
Amortized cost	1,669	1,588	—	—	3,257
Estimated fair value	1,674	1,593	—	—	3,267
Weighted average yield(3)	5.78 %	5.79 %	—	—	5.79 %
Equity securities:(4)					
Amortized cost	7,522	—	—	—	7,522
Estimated fair value	7,387	—	—	—	7,387
Total available-for-sale securities:					
Amortized cost					$39,736
Estimated fair value					$41,719

(1) Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without prepayment penalties.
(2) Yields have been adjusted to a tax equivalent basis assuming a 35% federal tax rate.
(3) Yields are calculated based on amortized cost.
(4) These equity securities do not have a stated maturity.

Securities with carrying values of approximately $25.5 million were pledged to secure certain borrowings and deposits at June 30, 2015. Of the pledged securities at June 30, 2015, approximately $8.4 million were pledged for certain deposits, and approximately $17.1 million were pledged for repurchase agreements.

The following table discloses, as of June 30, 2015 and December 31, 2014, our investment securities that have been in a continuous unrealized loss position for less than 12 months and those that have been in a continuous unrealized loss position for 12 or more months (in thousands):

June 30, 2015	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Equity securities	$—	$—	$6,288	$(212)	$6,288	$(212)

December 31, 2014	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Equity securities	$—	$—	$6,349	$(151)	$6,349	$(151)

At June 30, 2015, we owned one security with an unrealized loss position. This security is a publicly traded equity fund and is subject to market pricing volatility. We do not believe this unrealized loss is “other than temporary”. We have evaluated the near-term prospects of the investment in relation to the severity and duration of the impairment and based on that evaluation have the ability and intent to hold the investment until recovery of fair value.

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(4) LOANS AND ALLOWANCE FOR LOAN LOSSES

At June 30, 2015 and December 31, 2014, loans were as follows (in thousands):

	June 30, 2015	December 31, 2014
Commercial	$6,388,707	$5,869,219
Mortgage finance	4,906,415	4,102,125
Construction	1,837,532	1,416,405
Real estate	2,834,005	2,807,127
Consumer	23,789	19,699
Leases	97,025	99,495
Gross loans held for investment	16,087,473	14,314,070
Deferred income (net of direct origination costs)	(57,733)	(57,058)
Allowance for loan losses	(118,770)	(100,954)
Total	$15,910,970	$14,156,058

Commercial Loans and Leases. Our commercial loan and lease portfolio is comprised of lines of credit for working capital and term loans and leases to finance equipment and other business assets. Our energy production loans are generally collateralized with proven reserves based on appropriate valuation standards and take into account the risk of oil and gas price volatility. Our commercial loans and leases are underwritten after carefully evaluating and understanding the borrower's ability to operate profitably. Our underwriting standards are designed to promote relationship banking rather than to make loans on a transactional basis. Our lines of credit typically are limited to a percentage of the value of the assets securing the line. Lines of credit and term loans typically are reviewed annually and are supported by accounts receivable, inventory, equipment and other assets of our clients' businesses.

Mortgage Finance Loans. Our mortgage finance loans consist of ownership interests purchased in single-family residential mortgages funded through our mortgage finance group. These interests are typically on our balance sheet for 10 to 20 days. We have agreements with mortgage lenders and purchase interests in individual loans they originate. All loans are underwritten consistent with established programs for permanent financing with financially sound investors. Substantially all loans are conforming loans. Balances as of June 30, 2015 and December 31, 2014 are stated net of $541.0 million and $358.3 million participations sold, respectively.

Construction Loans. Our construction loan portfolio consists primarily of single- and multi-family residential properties and commercial projects used in manufacturing, warehousing, service or retail businesses. Our construction loans generally have terms of one to three years. We typically make construction loans to developers, builders and contractors that have an established record of successful project completion and loan repayment and have a substantial equity investment in the borrowers. Loan amounts are derived primarily from the bank's evaluation of expected cash flows available to service debt from stabilized projects under hypothetically stressed conditions. Construction loans are also based in part upon estimates of costs and value associated with the completed project. Sources of repayment for these types of loans may be pre-committed permanent loans from other lenders, sales of developed property or an interim loan commitment from us until permanent financing is obtained. The nature of these loans makes ultimate repayment sensitive to overall economic conditions. Borrowers may not be able to correct conditions of default in loans, increasing risk of exposure to classification, non-performing status, reserve allocation and actual credit loss and foreclosure. These loans typically have floating rates and commitment fees.

Real Estate Loans. A portion of our real estate loan portfolio is comprised of loans secured by properties other than market risk or investment-type real estate. Market risk loans are real estate loans where the primary source of repayment is expected to come from the sale, permanent financing or lease of the real property collateral. We generally provide temporary financing for commercial and residential property. These loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Our real estate loans generally have maximum terms of five to seven years, and we provide loans with both floating and fixed rates. We generally avoid long-term loans for commercial real estate held for investment. Real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy. Appraised values may be highly variable due to market conditions, the impact of the inability of potential purchasers and lessees to obtain financing and a lack of transactions at comparable values.

At June 30, 2015 and December 31, 2014, we had a blanket floating lien on certain real estate-secured loans, mortgage finance loans and certain securities used as collateral for Federal Home Loan Bank ("FHLB") borrowings.

Portfolio Geographic Concentration

As of June 30, 2015, a substantial majority of our loans held for investment, excluding our mortgage finance loans and other national lines of business, were to businesses with headquarters and operations in Texas. This geographic concentration subjects the loan portfolio to the general economic conditions within this area. Additionally, we may make loans to these businesses and individuals secured by assets located outside of Texas. The risks created by this concentration have been considered by management in the determination of the appropriateness of the allowance for loan losses. Management believes the allowance for loan losses is appropriate to cover probable losses inherent in the loan portfolio at each balance sheet date.

Summary of Loan Loss Experience

The reserve for loan losses is comprised of specific reserves for impaired loans and an estimate of losses inherent in the portfolio at the balance sheet date, but not yet identified with specified loans. We regularly evaluate our reserve for loan losses to maintain an appropriate level to absorb estimated loan losses inherent in the loan portfolio. Factors contributing to the determination of reserves include the credit-worthiness of the borrower, changes in the value of pledged collateral and general economic conditions. All loan commitments rated substandard or worse and greater than $500,000 are specifically reviewed for loss potential. For loans deemed to be impaired, a specific allocation is assigned based on the losses expected to be realized from those loans. For purposes of determining the general reserve, the portfolio is segregated by product types to recognize differing risk profiles among categories, and then further segregated by credit grades. Credit grades are assigned to all loans. Each credit grade is assigned a risk factor, or reserve allocation percentage. These risk factors are multiplied by the outstanding principal balance and risk-weighted by product type to calculate the required reserve. A similar process is employed to calculate a reserve assigned to off-balance sheet commitments, specifically unfunded loan commitments and letters of credit, and any needed reserve is recorded in other liabilities. Even though portions of the allowance may be allocated to specific loans, the entire allowance is available for any credit that, in management's judgment, should be charged off.

We have several pass credit grades that are assigned to loans based on varying levels of risk, ranging from credits that are secured by cash or marketable securities, to watch credits which have all the characteristics of an acceptable credit risk but warrant more than the normal level of monitoring. Within our criticized/classified credit grades are special mention, substandard and doubtful. Special mention loans are those that are currently protected by the current sound worth and paying capacity of the borrower, but that are potentially weak and constitute an additional credit risk. The loan has the potential to deteriorate to a substandard grade due to the existence of financial or administrative deficiencies. Substandard loans have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that we will sustain some loss if the deficiencies are not corrected. Some substandard loans are insufficiently protected by the current sound worth and paying capacity of the borrower and of the collateral pledged and may be considered impaired. Substandard loans can be accruing or can be on non-accrual depending on the circumstances of the individual loans. Loans classified as doubtful have all the weaknesses inherent in substandard loans with the added characteristics that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. The possibility of loss is extremely high. All doubtful loans are on non-accrual.

The reserve allocation percentages assigned to each credit grade have been developed based primarily on an analysis of our historical loss rates. The allocations are adjusted for certain qualitative factors for such things as general economic conditions and changes in credit policies and lending standards. Changes in the trend and severity of problem loans can cause the estimation of losses to differ from past experience. In addition, the reserve reflects the results of reviews performed by the Company's independent Credit Review function as reflected in their confirmations of assigned credit grades within the portfolio. The Credit Review function reports to the Credit Risk Committee of the Company's board of directors with administrative oversight from the Company's Chief Risk Officer. The portion of the allowance that is not derived by the allowance allocation percentages compensates for the uncertainty and complexity in estimating loan and lease losses including factors and conditions that may not be fully reflected in the determination and application of the allowance allocation percentages. Examples of risks that support the Company's maintaining an unallocated reserve include the possibility of precipitous negative changes in economic conditions and borrowers' submission of financial statements or certifications of collateral value that subsequently prove to be materially inaccurate for reason of either misstatement or omission of critical information. These situations, while not common, do not necessarily correlate well with the general risk profile presented by assigned credit grade and product type categories. We evaluate many factors and conditions in determining the unallocated portion of the allowance, including amount and frequency of losses attributable to issues not specifically addressed or included in the determination and application of the allowance allocation percentages. We consider the allowance to be appropriate, given management’s assessment of probable losses within the portfolio as of the evaluation date, the significant growth in the loan and lease portfolio, current economic conditions in the Company’s market areas and other factors.

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The methodology used in the periodic review of reserve appropriateness, which is performed at least quarterly, is designed to be dynamic and responsive to changes in portfolio credit quality. The changes are reflected in the general reserve and in specific reserves as the collectability of larger classified loans is evaluated with new information. As our portfolio has matured, historical loss ratios have been closely monitored, and our reserve appropriateness relies primarily on our loss history. The review of the reserve appropriateness is performed by executive management and presented to a committee of our board of directors for their review. The committee reports to the board as part of the board's review on a quarterly basis of the Company's consolidated financial statements.

The following tables summarize the credit risk profile of our loan portfolio by internally assigned grades and non-accrual status as of June 30, 2015 and December 31, 2014 (in thousands):

June 30, 2015

	Commercial	Mortgage Finance	Construction	Real Estate	Consumer	Leases	Total
Grade:							
Pass	$6,142,326	$4,906,415	$1,819,735	$2,804,448	$23,568	$89,990	$15,786,482
Special mention	100,638	—	—	20,330	7	505	121,480
Substandard-accruing	53,678	—	1,048	1,558	214	93	56,591
Non-accrual	92,065	—	16,749	7,669	—	6,437	122,920
Total loans held for investment	$6,388,707	$4,906,415	$1,837,532	$2,834,005	$23,789	$97,025	$16,087,473

December 31, 2014

	Commercial	Mortgage Finance	Construction	Real Estate	Consumer	Leases	Total
Grade:							
Pass	$5,738,474	$4,102,125	$1,414,671	$2,785,804	$19,579	$91,044	$14,151,697
Special mention	53,839	—	1,734	8,723	11	4,363	68,670
Substandard-accruing	43,784	—	—	2,653	47	3,915	50,399
Non-accrual	33,122	—	—	9,947	62	173	43,304
Total loans held for investment	$5,869,219	$4,102,125	$1,416,405	$2,807,127	$19,699	$99,495	$14,314,070

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The following table details activity in the reserve for loan losses by portfolio segment for the six months ended June 30, 2015 and June 30, 2014. Allocation of a portion of the reserve to one category of loans does not preclude its availability to absorb losses in other categories.

June 30, 2015

(in thousands)	Commercial	Mortgage Finance	Construction	Real Estate	Consumer	Leases	Unallocated	Total
Beginning balance	$ 70,654	$—	$ 7,935	$15,582	$240	$1,141	$ 5,402	$100,954
Provision for loan losses	37,666	—	(4,066)	(6,509)	144	(831)	(1,778)	24,626
Charge-offs	8,520	—	—	346	62	—	—	8,928
Recoveries	1,710	—	355	20	10	23	—	2,118
Net charge-offs (recoveries)	6,810	—	(355)	326	52	(23)	—	6,810
Ending balance	$ 101,510	$—	$ 4,224	$8,747	$332	$333	$ 3,624	$118,770
Period end amount allocated to:								
Loans individually evaluated for impairment	$ 13,717	$—	$ —	$337	$—	$1	$ —	$14,055
Loans collectively evaluated for impairment	87,793	—	4,224	8,410	332	332	3,624	104,715
Ending balance	$ 101,510	$—	$ 4,224	$8,747	$332	$333	$ 3,624	$118,770

June 30, 2014

(in thousands)	Commercial	Mortgage Finance	Construction	Real Estate	Consumer	Leases	Unallocated	Total
Beginning balance	$ 39,868	$—	$ 14,553	$24,210	$149	$3,105	$ 5,719	$87,604
Provision for loan losses	13,714	—	199	(3,891)	114	(1,930)	(139)	8,067
Charge-offs	7,526	—	—	296	101	—	—	7,923
Recoveries	2,239	—	—	47	31	1,049	—	3,366
Net charge-offs (recoveries)	5,287	—	—	249	70	(1,049)	—	4,557
Ending balance	$ 48,295	$—	$ 14,752	$20,070	$193	$2,224	$ 5,580	$91,114
Period end amount allocated to:								
Loans individually evaluated for impairment	$ 6,293	$—	$ —	$722	$—	$3	$ —	$7,018
Loans collectively evaluated for impairment	42,002	—	14,752	19,348	193	2,221	5,580	84,096
Ending balance	$ 48,295	$—	$ 14,752	$20,070	$193	$2,224	$ 5,580	$91,114

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Our recorded investment in loans as of June 30, 2015, December 31, 2014 and June 30, 2014 related to each balance in the allowance for loan losses by portfolio segment and disaggregated on the basis of our impairment methodology was as follows (in thousands):

June 30, 2015

	Commercial	Mortgage Finance	Construction	Real Estate	Consumer	Leases	Total
Loans individually evaluated for impairment	$93,944	$—	$16,749	$10,565	$—	$6,437	$127,695
Loans collectively evaluated for impairment	6,294,763	4,906,415	1,820,783	2,823,440	23,789	90,588	15,959,778
Total	$6,388,707	$4,906,415	$1,837,532	$2,834,005	$23,789	$97,025	$16,087,473

December 31, 2014

	Commercial	Mortgage Finance	Construction	Real Estate	Consumer	Leases	Total
Loans individually evaluated for impairment	$35,165	$—	$—	$13,880	$62	$173	$49,280
Loans collectively evaluated for impairment	5,834,054	4,102,125	1,416,405	2,793,247	19,637	99,322	14,264,790
Total	$5,869,219	$4,102,125	$1,416,405	$2,807,127	$19,699	$99,495	$14,314,070

June 30, 2014

	Commercial	Mortgage Finance	Construction	Real Estate	Consumer	Leases	Total
Loans individually evaluated for impairment	$27,679	$—	$—	$19,790	$—	$22	$47,491
Loans collectively evaluated for impairment	5,267,689	3,700,253	1,567,667	2,212,130	15,847	95,892	12,859,478
Total	$5,295,368	$3,700,253	$1,567,667	$2,231,920	$15,847	$95,914	$12,906,969

We have traditionally maintained an unallocated reserve component to compensate for the uncertainty and complexity in estimating loan and lease losses including factors and conditions that may not be fully reflected in the determination and application of the allowance allocation percentages. We believe the level of unallocated reserves at June 30, 2015 is warranted due to the continued uncertain economic environment which has produced losses, including those resulting from borrowers' misstatement of financial information or inaccurate certification of collateral values. Such losses are not necessarily correlated with historical loss trends or general economic conditions. Our methodology used to calculate the allowance considers historical losses; however, the historical loss rates for specific product types or credit risk grades may not fully incorporate the effects of continued weakness in the economy.

Generally we place loans on non-accrual when there is a clear indication that the borrower’s cash flow may not be sufficient to meet payments as they become due, which is generally when a loan is 90 days past due. When a loan is placed on non-accrual status, all previously accrued and unpaid interest is reversed. Interest income is subsequently recognized on a cash basis as long as the remaining unpaid principal amount of the loan is deemed to be fully collectible. If collectability is questionable, then cash payments are applied to principal. As of June 30, 2015,

$904,100 of our non-accrual loans were earning on a cash basis compared to $310,000 at December 31, 2014. A loan is placed back on accrual status when both principal and interest are current and it is probable that we will be able to collect all amounts due (both principal and interest) according to the terms of the loan agreement.

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A loan held for investment is considered impaired when, based on current information and events, it is probable that we will be unable to collect all amounts due (both principal and interest) according to the terms of the loan agreement. In accordance with ASC 310 Receivables ("ASC 310"), we have also included all restructured loans in our impaired loan totals. The following tables detail our impaired loans, by portfolio class, as of June 30, 2015 and December 31, 2014 (in thousands):

June 30, 2015

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial					
Business loans	$11,557	$15,805	$—	$20,736	$—
Energy	37,938	37,938	—	6,956	28
Construction					
Market risk	16,749	16,749	—	2,792	—
Real estate					
Market risk	3,639	3,639	—	3,696	—
Commercial	2,951	2,951	—	3,732	—
Secured by 1-4 family	—	—	—	—	—
Consumer	—	—	—	—	—
Leases	6,432	6,432	—	1,072	—
Total impaired loans with no allowance recorded	$79,266	$83,514	$—	$38,984	$28
With an allowance recorded:					
Commercial					
Business loans	$44,153	$47,153	$13,672	$29,602	$—
Energy	296	296	45	702	—
Construction					
Market risk	—	—	—	—	—
Real estate					
Market risk	1,920	1,920	46	2,693	—
Commercial	436	436	65	466	—
Secured by 1-4 family	1,619	1,619	226	1,757	—
Consumer	—	—	—	21	—
Leases	5	5	1	145	—
Total impaired loans with an allowance recorded	$48,429	$51,429	$14,055	$35,386	$—
Combined:					
Commercial					
Business loans	$55,710	$62,958	$13,672	$50,338	$—
Energy	38,234	38,234	45	7,658	28
Construction					
Market risk	16,749	16,749	—	2,792	—
Real estate					
Market risk	5,559	5,559	46	6,389	—
Commercial	3,387	3,387	65	4,198	—
Secured by 1-4 family	1,619	1,619	226	1,757	—
Consumer	—	—	—	21	—
Leases	6,437	6,437	1	1,217	—

Total impaired loans	$127,695	$134,943	$14,055	$74,370	$28

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December 31, 2014

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial					
Business loans	$9,608	$11,857	$—	$7,334	$—
Energy	—	—	—	375	25
Construction					
Market risk	—	—	—	118	—
Real estate					
Market risk	3,735	3,735	—	7,970	—
Commercial	3,521	3,521	—	2,795	—
Secured by 1-4 family	—	—	—	1,210	—
Consumer	—	—	—	—	—
Leases	—	—	—	—	—
Total impaired loans with no allowance recorded	$16,864	$19,113	$—	$19,802	$25
With an allowance recorded:					
Commercial					
Business loans	$24,553	$25,553	$7,433	$17,705	$—
Energy	1,004	1,004	272	991	—
Construction					
Market risk	—	—	—	—	—
Real estate					
Market risk	4,203	4,203	317	5,064	—
Commercial	526	526	79	705	—
Secured by 1-4 family	1,895	1,895	240	2,119	—
Consumer	62	62	9	16	—
Leases	173	173	26	41	—
Total impaired loans with an allowance recorded	$32,416	$33,416	$8,376	$26,641	$—
Combined:					
Commercial					
Business loans	$34,161	$37,410	$7,433	$25,039	$—
Energy	1,004	1,004	272	1,366	25
Construction					
Market risk	—	—	—	118	—
Real estate					
Market risk	7,938	7,938	317	13,034	—
Commercial	4,047	4,047	79	3,500	—
Secured by 1-4 family	1,895	1,895	240	3,329	—
Consumer	62	62	9	16	—
Leases	173	173	26	41	—
Total impaired loans	$49,280	$52,529	$8,376	$46,443	$25

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Average impaired loans outstanding during the six months ended June 30, 2015 and 2014 totaled $74.4 million and $46.3 million, respectively.
The table below provides an age analysis of our past due loans that are still accruing and non-accrual loans, by portfolio class, as of June 30, 2015 (in thousands):

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days and Accruing(1)	Total Past Due	Non-accrual	Current	Total
Commercial							
Business loans	$ 16,670	$ 29,520	$ 5,460	$ 51,650	$ 53,831	$ 5,179,526	$ 5,285,007
Energy	—	—	22	22	38,234	1,065,444	1,103,700
Mortgage finance loans	—	—	—	—	—	4,906,415	4,906,415
Construction							
Market risk	—	—	—	—	16,749	1,803,414	1,820,163
Secured by 1-4 family	—	—	—	—	—	17,369	17,369
Real estate							
Market risk	2,300	—	—	2,300	3,779	2,197,463	2,203,542
Commercial	—	—	—	—	3,387	522,498	525,885
Secured by 1-4 family	500	—	—	500	503	103,575	104,578
Consumer	184	25	—	209	—	23,580	23,789
Leases	235	—	—	235	6,437	90,353	97,025
Total loans held for investment	$ 19,889	$ 29,545	$ 5,482	$ 54,916	$ 122,920	$ 15,909,637	$ 16,087,473

(1) Loans past due 90 days and still accruing includes premium finance loans of $4.8 million. These loans are generally secured by obligations of insurance carriers to refund premiums on canceled insurance policies. The refund of premiums from the insurance carriers can take 180 days or longer from the cancellation date.

Restructured loans are loans on which, due to the borrower’s financial difficulties, we have granted a concession that we would not otherwise consider for borrowers of similar credit quality. This may include a transfer of real estate or other assets from the borrower, a modification of loan terms, or a combination of the two. Modifications of terms that could potentially qualify as a restructuring include reduction of contractual interest rate, extension of the maturity date at a contractual interest rate lower than the current rate for new debt with similar risk, a reduction of the face amount of debt or forgiveness of either principal or accrued interest. As of June 30, 2015 and December 31, 2014, we had $249,000 and $1.8 million, respectively, in loans considered restructured that are not on non-accrual. These loans did not have unfunded commitments at June 30, 2015 or December 31, 2014. Of the non-accrual loans at June 30, 2015 and December 31, 2014, $28.2 million and $12.1 million, respectively, met the criteria for restructured. These loans had no unfunded commitments at their respective balance sheet dates. A loan continues to qualify as restructured until a consistent payment history or change in borrower’s financial condition has been evidenced, generally no less than twelve months. Assuming that the restructuring agreement specifies an interest rate at the time of the restructuring that is greater than or equal to the rate that we are willing to accept for a new extension of credit with comparable risk, then the loan no longer has to be considered a restructuring if it is in compliance with modified terms in calendar years after the year of the restructure.

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The following tables summarize, for the six months ended June 30, 2015 and 2014, loans that were restructured during 2015 and 2014 (in thousands):

June 30, 2015

	Number of Restructured Loans	Pre-Restructuring Outstanding Recorded Investment	Post-Restructuring Outstanding Recorded Investment
Commercial business loans	4	$18,329	$16,960
Total new restructured loans in 2015	4	$18,329	$16,960

June 30, 2014

	Number of Restructured Loans	Pre-Restructuring Outstanding Recorded Investment	Post-Restructuring Outstanding Recorded Investment
Real estate—commercial	1	$1,441	$1,430
Total new restructured loans in 2014	1	$1,441	$1,430

The restructured loans generally include terms to temporarily place loans on interest only, extend the payment terms or reduce the interest rate. We did not forgive any principal on the above loans. The restructuring of the loans did not have a significant impact on our allowance for loan losses at June 30, 2015 or 2014.

The following table provides information on how restructured loans were modified during the six months ended June 30, 2015 and 2014 (in thousands):

	Six months ended June 30,	
	2015	2014
Extended maturity	$—	$1,430
Combination of maturity extension and payment schedule adjustment	16,960	—
Total	$16,960	$1,430

As of June 30, 2015 and 2014, we did not have any loans that were restructured within the last 12 months that subsequently defaulted.

(5) OREO AND VALUATION ALLOWANCE FOR LOSSES ON OREO

The table below presents a summary of the activity related to OREO (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Beginning balance	$605	$2,420	$568	$5,110
Additions	85	—	1,177	851
Sales	(81)	(1,735)	(1,136)	(5,276)
Valuation allowance for OREO	—	—	—	—
Direct write-downs	—	—	—	—
Ending balance	$609	$685	$609	$685

(6) FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK

The Bank is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit which involve varying degrees of credit risk in excess of the amount recognized in the consolidated balance sheets. The Bank's exposure to credit loss in the event of non-performance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of these instruments. The Bank uses the

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same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. The amount of collateral obtained, if deemed necessary, is based on management's credit evaluation of the borrower. 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 or other termination clauses and may require payment of a fee. Since many of the commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's credit-worthiness on a case-by-case basis.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

The table below summarizes our off-balance sheet financial instruments whose contract amounts represented credit risk (in thousands):

	June 30, 2015	December 31, 2014
Commitments to extend credit	$5,256,986	$5,324,460
Standby letters of credit	186,483	177,808

(7) REGULATORY MATTERS

The Company and the Bank 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 and the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of the Company's and the Bank's assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The Company's and the Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

In July 2013, the Federal Reserve published final rules for the adoption of the Basel III regulatory capital framework (the "Basel III Capital Rules"). The Basel III Capital Rules, among other things, (i) introduce a new capital measure called "Common Equity Tier 1" ("CET1"), (ii) specify that Tier 1 capital consist of Common Equity Tier 1 and "Additional Tier 1 Capital" instruments meeting specified requirements, (iii) define Common Equity Tier 1 narrowly by requiring that most deductions/adjustments to regulatory capital measures be made to Common Equity Tier 1 and not to the other components of capital and (iv) expand the scope of the deductions/adjustments as compared to existing regulations. The Basel III Capital Rules became effective for us on January 1, 2015 with certain transition provisions fully phased in on January 1, 2019.

Quantitative measures established by these regulations to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios CET1, Tier 1 and Total capital to risk-weighted assets, and of Tier 1 capital to average assets, each as defined in the regulations. Management believes, as of June 30, 2015, that the Company and the Bank met all capital adequacy requirements to which they are subject.

Financial institutions are categorized as well capitalized or adequately capitalized, based on minimum total risk-based, Tier 1 risk-based, CET1 and Tier 1 leverage ratios. As shown in the table below, the Company's capital ratios exceeded the regulatory definition of adequately capitalized as of June 30, 2015, and December 31, 2014. Based upon the information in its most recently filed call report, the Bank met the capital ratios necessary to be well capitalized. The regulatory authorities can apply changes in classification of assets and such changes may retroactively subject the Company to changes in capital ratios. Any such changes could result in reducing one or more capital ratios below well-capitalized status. In addition, a change may result in imposition of additional assessments by the FDIC or could result in regulatory actions that could have a material adverse effect on our financial condition and results of operations.

Because our bank had less than $15.0 billion in total consolidated assets as of December 31, 2009, we are allowed to continue to classify our trust preferred securities, all of which were issued prior to May 19, 2010, as Tier 1 capital.

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The table below summarizes our capital ratios:

	June 30, 2015		December 31, 2014	
Company				
Risk-based capital:				
CET1(1)	7.43	%	7.89	%
Tier 1 capital	8.82	%	9.46	%
Total capital	11.03	%	11.83	%
Leverage	9.03	%	10.76	%

(1) December 31, 2014 ratio is unaudited.

Our mortgage finance loan volumes can increase significantly at month-end, causing a meaningful difference between ending balance and average balance for any period. At June 30, 2015, our total mortgage finance loans were $4.9 billion compared to the average for the quarter ended June 30, 2015 of $4.6 billion. As CET1, Tier 1 and total capital ratios are calculated using ending risk-weighted assets and our mortgage finance loans are 100% risk-weighted, the quarter-end fluctuation in these balances can significantly impact our reported ratios. Due to the risk profile and liquidity of this asset class, we manage capital allocated to mortgage finance loans based on changing trends in average balances and do not believe that the quarter-end balance is representative of risk characteristics that would justify higher allocations. However, we will continue to monitor our capital allocation to confirm that all capital levels remain above well-capitalized levels.

Dividends that may be paid by subsidiary banks are routinely restricted by various regulatory authorities. The amount that can be paid in any calendar year without prior approval of the Bank’s regulatory agencies cannot exceed the lesser of the net profits (as defined) for that year plus the net profits for the preceding two calendar years, or retained earnings. The Basel III Capital Rules further limit the amount of dividends that may be paid by our bank. No dividends were declared or paid on common stock during the three and six months ended June 30, 2015 or 2014.

(8) STOCK-BASED COMPENSATION

On May 19, 2015, the Company's stockholders approved the Texas Capital Bancshares, Inc. 2015 Long-Term Incentive Plan (the "2015 Plan"), which provides for the issuance of up to 2,550,000 shares of common stock for compensation to the Company's key employees, certain key contractors and non-employee directors, subject to increase by up to approximately 751,887 shares underlying outstanding stock-settled awards granted pursuant to prior plans that may be forfeited, expire or may be canceled and available for reuse in the future pursuant to the terms of the 2015 Plan.

The fair value of our stock option and stock appreciation right (“SAR”) grants are estimated at the date of grant using the Black-Scholes option pricing model. The Black-Scholes option pricing model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because our employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management’s opinion, the existing models do not necessarily provide the best single measure of the fair value of our employee stock options.

Stock-based compensation consists of SARs and RSUs granted from 2009 through June 30, 2015.

	Three months ended June 30,		Six months ended June 30,	
(in thousands)	2015	2014	2015	2014
Stock- based compensation expense recognized:				
SARs	$93	$148	$197	$291
RSUs	1,019	1,118	1,906	2,237
Total compensation expense recognized	$1,112	$1,266	$2,103	$2,528

	June 30, 2015	
(in thousands)	Options	SARs and RSUs
Unrecognized compensation expense related to unvested awards	$—	$13,839
Weighted average period over which expense is expected to be recognized, in years	N/A	3.4

In connection with the 2010 Long-term Incentive Plan, the Company has issued cash-based performance units. A summary of the compensation cost for these units is as follows (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Cash-based performance units	$3,172	$1,312	$4,538	$4,705

(9) FAIR VALUE DISCLOSURES

ASC 820, Fair Value Measurements and Disclosures ("ASC 820"), defines fair value, establishes a framework for measuring fair value under GAAP and requires enhanced disclosures about fair value measurements. Fair value is defined under ASC 820 as the price that would be received for an asset or paid to transfer a liability (an exit price) in the principal market for the asset or liability in an orderly transaction between market participants on the measurement date.

We determine the fair market values of our assets and liabilities measured at fair value on a recurring and nonrecurring basis using the fair value hierarchy as prescribed in ASC 820. The standard describes three levels of inputs that may be used to measure fair value as provided below.

Level 1	Quoted prices in active markets for identical assets or liabilities.
Level 2	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 2 assets include U.S. government and agency mortgage-backed debt securities, municipal bonds, and Community Reinvestment Act funds. This category includes derivative assets and liabilities where values are obtained from independent pricing services.
Level 3	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 similar techniques, as well as instruments for which the determination of fair values requires significant management judgment or estimation. This category includes impaired loans and OREO where collateral values have been based on third party appraisals; however, due to current economic conditions, comparative sales data typically used in appraisals may be unavailable or more subjective due to lack of market activity.

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Assets and liabilities measured at fair value at June 30, 2015 and December 31, 2014 are as follows (in thousands):

	Fair Value Measurements Using		
June 30, 2015	Level 1	Level 2	Level 3
Available for sale securities:(1)			
Residential mortgage-backed securities	$—	$26,726	$—
Municipals	—	1,313	—
Equity securities(2)	—	7,322	—
Loans(3) (5)	—	—	52,389
OREO(4) (5)	—	—	609
Derivative assets(6)	—	33,576	—
Derivative liabilities(6)	—	33,576	—
December 31, 2014			
Available for sale securities:(1)			
Residential mortgage-backed securities	$—	$31,065	$—
Municipals	—	3,267	—
Equity securities(2)	—	7,387	—
Loans(3) (5)	—	—	23,536
OREO(4) (5)	—	—	568
Derivative assets(6)	—	31,176	—
Derivative liabilities(6)	—	31,176	—

(1) Securities are measured at fair value on a recurring basis, generally monthly.
(2) Equity securities consist of Community Reinvestment Act funds.
(3) Includes impaired loans that have been measured for impairment at the fair value of the loan’s collateral.
(4) OREO is transferred from loans to OREO at fair value less selling costs.
(5) Fair value of loans and OREO is measured on a nonrecurring basis, generally annually or more often as warranted by market and economic conditions.
(6) Derivative assets and liabilities are measured at fair value on a recurring basis, generally quarterly.

Level 3 Valuations

Financial instruments are considered Level 3 when their values are determined using pricing models, discounted cash flow methodologies or similar techniques and at least one significant model assumption or input is unobservable. Level 3 financial instruments also include those for which the determination of fair value requires significant management judgment or estimation. Currently, we measure fair value for certain loans and OREO on a nonrecurring basis as described below.

Loans

During six months ended June 30, 2015 and the year ended December 31, 2014, certain impaired loans were re-evaluated and reported at fair value through a specific allocation of the allowance for loan losses based upon the fair value of the underlying collateral. The $52.4 million reported fair value above includes impaired loans at June 30, 2015 with a carrying value of $58.6 million that were reduced by specific allowance allocations totaling $6.2 million based on collateral valuations utilizing Level 3 valuation inputs. The $23.5 million reported fair value above includes impaired loans at December 31, 2014 with a carrying value of $29.2 million that were reduced by specific valuation allowance allocations totaling $5.7 million based on collateral valuations utilizing Level 3 valuation inputs. Fair values were based on third party appraisals.

OREO

Certain foreclosed assets, upon initial recognition, are valued based on third party appraisals less estimated selling costs. At June 30, 2015 and December 31, 2014, OREO had a carrying value of $609,000 and $568,000, respectively, with no specific valuation allowance. The fair value of OREO was computed based on third party appraisals, which are Level 3 valuation inputs.

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Fair Value of Financial Instruments

Generally accepted accounting principles require disclosure of fair value information about financial instruments, whether or not recognized on the balance sheet, for which it is practical to estimate that value. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. This disclosure does not and is not intended to represent the fair value of the Company.

A summary of the carrying amounts and estimated fair values of financial instruments is as follows (in thousands):

	June 30, 2015		December 31, 2014	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Cash and cash equivalents	$1,454,751	$1,454,751	$1,330,514	$1,330,514
Securities, available-for-sale	35,361	35,361	41,719	41,719
Loans held for investment, net	15,910,970	15,912,316	14,156,058	14,161,484
Derivative assets	33,576	33,576	31,176	31,176
Deposits	14,188,276	14,188,818	12,673,300	12,673,607
Federal funds purchased	79,088	79,088	66,971	66,971
Customer repurchase agreements	29,919	29,919	25,705	25,705
Other borrowings	1,400,000	1,400,000	1,100,005	1,100,005
Subordinated notes	286,000	287,807	286,000	289,947
Trust preferred subordinated debentures	113,406	113,406	113,406	113,406
Derivative liabilities	33,576	33,576	31,176	31,176

The following methods and assumptions were used by the Company in estimating fair value disclosures for its financial instruments:

Cash and cash equivalents

The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents approximate their fair value, which is characterized as a Level 1 asset in the fair value hierarchy

Securities

The fair value of investment securities is based on prices obtained from independent pricing services which are based on quoted market prices for the same or similar securities, which is characterized as a Level 2 asset in the fair value hierarchy. We have obtained documentation from the primary pricing service we use about their processes and controls over pricing. In addition, on a quarterly basis we independently verify the prices that we receive from the service provider using two additional independent pricing sources. Any significant differences are investigated and resolved.

Loans held for investment, net

Loans are characterized as Level 3 assets in the fair value hierarchy. For variable-rate loans that reprice frequently with no significant change in credit risk, fair values are generally based on carrying values. The fair value for all other loans is estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality.

Derivatives

The estimated fair value of interest rate swaps and caps are obtained from independent pricing services based on quoted market prices for the same or similar derivative contracts and are characterized as a Level 2 asset in the fair value hierarchy. On a quarterly basis, we independently verify the fair value using an additional independent pricing source.

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Deposits

Deposits are characterized as Level 3 liabilities in the fair value hierarchy. The carrying amounts for variable-rate money market accounts approximate their fair value. Fixed-term certificate of deposit fair values are estimated using a discounted cash flow calculation that applies interest rates currently being offered on similar certificates to a schedule of aggregated expected monthly maturities.

Federal funds purchased, customer repurchase agreements, other borrowings, subordinated notes and trust preferred subordinated debentures

The carrying values reported in the consolidated balance sheets for Federal funds purchased, customer repurchase agreements and other short-term, floating rate borrowings approximate their fair values, which are characterized as Level 2 assets in the fair value hierarchy. The fair values of any fixed rate short-term borrowings and trust preferred subordinated debentures are estimated using a discounted cash flow calculation that applies interest rates currently being offered on similar borrowings, which are characterized as Level 3 liabilities in the fair value hierarchy. The subordinated notes are publicly traded and are valued based on market prices, which are characterized as Level 2 liabilities in the fair value hierarchy.

(10) DERIVATIVE FINANCIAL INSTRUMENTS

The fair value of derivative positions outstanding is included in accrued interest receivable and other assets and other liabilities in the accompanying consolidated balance sheets on a net basis when a right of offset exists, based on transactions with a single counterparty that are subject to a legally enforceable master netting agreement.

During three months ended June 30, 2015 and 2014, we entered into certain interest rate derivative positions that are not designated as hedging instruments. These derivative positions relate to transactions in which we enter into an interest rate swap, cap and/or floor with a customer while at the same time entering into an offsetting interest rate swap, cap and/or floor with another financial institution. In connection with each swap transaction, we agree to pay interest to the customer on a notional amount at a variable interest rate and receive interest from the customer on a similar notional amount at a fixed interest rate. At the same time, we agree to pay another financial institution the same fixed interest rate on the same notional amount and receive the same variable interest rate on the same notional amount. The transaction allows our customer to effectively convert a variable rate loan to a fixed rate. Because we act as an intermediary for our customer, changes in the fair value of the underlying derivative contracts substantially offset each other and do not have a material impact on our results of operations.

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The notional amounts and estimated fair values of interest rate derivative positions outstanding at June 30, 2015 and December 31, 2014 are presented in the following tables (in thousands):

	June 30, 2015			December 31, 2014		
		Estimated Fair Value			Estimated Fair Value	
	Notional Amount	Asset Derivative	Liability Derivative	Notional Amount	Asset Derivative	Liability Derivative
Non-hedging interest rate derivatives:						
Financial institution counterparties:						
Commercial loan/lease interest rate swaps	$1,016,251	$212	$31,162	$866,432	$361	$30,162
Commercial loan/lease interest rate caps	223,828	2,414	—	63,414	1,014	—
Customer counterparties:						
Commercial loan/lease interest rate swaps	1,016,251	31,162	212	866,432	30,162	361
Commercial loan/lease interest rate caps	223,828	—	2,414	63,414	—	1,014
Gross derivatives		33,788	33,788		31,537	31,537
Offsetting derivative assets/liabilities		(212)	(212)		(361)	(361)
Net derivatives included in the consolidated balance sheets		$33,576	$33,576		$31,176	$31,176

The weighted-average receive and pay interest rates for interest rate swaps outstanding at June 30, 2015 were as follows:

	June 30, 2015		December 31, 2014	
	Weighted-Average Interest Rate		Weighted-Average Interest Rate	
	Received	Paid	Received	Paid
Non-hedging interest rate swaps	2.81%	4.74%	2.79%	4.82%

The weighted-average strike rate for outstanding interest rate caps was 2.25% at June 30, 2015 and 1.44% at December 31, 2014.

Our credit exposure on interest rate swaps and caps is limited to the net favorable value and interest payments of all swaps and caps by each counterparty. In such cases collateral may be required from the counterparties involved if the net value of the swaps and caps exceeds a nominal amount considered to be immaterial. Our credit exposure, net of any collateral pledged, relating to interest rate swaps and caps was approximately $33.6 million at June 30, 2015 and approximately $31.2 million at December 31, 2014, all of which relates to bank customers. Collateral levels are monitored and adjusted on a regular basis for changes in interest rate swap and cap values. At June 30, 2015 and December 31, 2014, we had $31.6 million and $30.2 million, respectively, in cash collateral pledged for these derivatives included in interest-bearing deposits.

(11) NEW ACCOUNTING PRONOUNCEMENTS

ASU 2014-09 "Revenue from Contracts with Customers (Topic 606)" ("ASU 2014-09") implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 establishes a five-step model which entities must follow to recognize revenue and removes inconsistencies and weaknesses in existing guidance. ASU 2014-09 is effective for annual and interim periods beginning after December 15, 2017 and is not expected to have a significant impact on our consolidated financial statements.

ASU 2014-12 "Compensation - Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period" ("ASU

2014-12") requires that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. ASU 2014-12 is intended to resolve the diverse accounting treatments of these types of awards in practice and is effective for annual and interim periods beginning after December 15, 2015. It is not expected to have a significant impact on our consolidated financial statements.

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QUARTERLY FINANCIAL SUMMARIES – UNAUDITED
Consolidated Daily Average Balances, Average Yields and Rates
(In thousands)

	For the three months ended June 30, 2015				For the three months ended June 30, 2014			
	Average Balance	Revenue/ Expense(1)	Yield/ Rate		Average Balance	Revenue/ Expense(1)	Yield/ Rate	
Assets								
Securities – taxable	$35,081	$311	3.56	%	$44,216	$410	3.72	%
Securities – non-taxable(2)	1,427	18	5.06	%	6,271	94	6.01	%
Federal funds sold	200,690	118	0.24	%	14,997	8	0.21	%
Deposits in other banks	2,103,732	1,327	0.25	%	183,061	100	0.22	%
Loans held for investment, mortgage finance loans	4,573,478	33,773	2.96	%	2,822,560	23,231	3.30	%
Loans held for investment	10,941,029	117,833	4.32	%	8,984,521	101,003	4.51	%
Less reserve for loan losses	109,086	—	—		90,105	—	—	
Loans, net of reserve	15,405,421	151,606	3.95	%	11,716,976	124,234	4.25	%
Total earning assets	17,746,351	153,380	3.47	%	11,965,521	124,846	4.18	%
Cash and other assets	493,034				396,938			
Total assets	$18,239,385				$12,362,459			
Liabilities and Stockholders’ Equity								
Transaction deposits	$1,404,521	$458	0.13	%	$895,827	$170	0.08	%
Savings deposits	5,610,277	4,332	0.31	%	4,679,140	3,395	0.29	%
Time deposits	516,582	657	0.51	%	401,024	390	0.39	%
Deposits in foreign branches	246,035	195	0.32	%	350,043	291	0.33	%
Total interest bearing deposits	7,777,415	5,642	0.29	%	6,326,034	4,246	0.27	%
Other borrowings	1,565,874	625	0.16	%	666,696	300	0.18	%
Subordinated notes	286,000	4,191	5.88	%	286,000	4,241	5.95	%
Trust preferred subordinated debentures	113,406	631	2.23	%	113,406	619	2.19	%
Total interest bearing liabilities	9,742,695	11,089	0.46	%	7,392,136	9,406	0.51	%
Demand deposits	6,804,994				3,629,941			
Other liabilities	161,614				98,595			
Stockholders’ equity	1,530,082				1,241,787			
Total liabilities and stockholders’ equity	$18,239,385				$12,362,459			
Net interest income(2)		$142,291				$115,440		
Net interest margin			3.22	%			3.87	%
Net interest spread			3.01	%			3.67	%
Loan spread			3.79	%			4.08	%

(1) The loan averages include loans on which the accrual of interest has been discontinued and are stated net of unearned income.
(2) Taxable equivalent rates used where applicable.

	For the six months ended June 30, 2015	For the six months ended June 30, 2014

	Average Balance	Revenue/ Expense(1)	Yield/ Rate		Average Balance	Revenue/ Expense(1)	Yield/ Rate	
Assets								
Securities – taxable	$36,107	$643	3.59	%	$45,614	$852	3.77	%
Securities – non-taxable(2)	2,102	58	5.56	%	8,401	245	5.88	%
Federal funds sold	196,019	234	0.24	%	44,209	48	0.22	%
Deposits in other banks	2,061,882	2,587	0.25	%	206,548	259	0.25	%
Loans held for investment, mortgage finance loans	4,162,491	61,404	2.97	%	2,427,109	40,013	3.32	%
Loans held for investment	10,722,813	229,376	4.31	%	8,852,127	200,093	4.56	%
Less reserve for loan losses	105,086	—	—		88,902	—	—	
Loans, net of reserve	14,780,218	290,780	3.97	%	11,190,334	240,106	4.33	%
Total earning assets	17,076,328	294,302	3.48	%	11,495,106	241,510	4.24	%
Cash and other assets	476,126				389,608			
Total assets	$17,552,454				$11,884,714			
Liabilities and Stockholders' Equity								
Transaction deposits	$1,403,081	$902	0.13	%	$839,378	$250	0.06	%
Savings deposits	5,750,034	8,752	0.31	%	4,635,559	6,699	0.29	%
Time deposits	482,322	1,163	0.49	%	388,364	741	0.38	%
Deposits in foreign branches	274,969	453	0.33	%	352,934	586	0.33	%
Total interest bearing deposits	7,910,406	11,270	0.29	%	6,216,235	8,276	0.27	%
Other borrowings	1,370,361	1,087	0.16	%	481,032	471	0.20	%
Subordinated notes	286,000	8,382	5.91	%	256,995	7,720	6.06	%
Trust preferred subordinated debentures	113,406	1,249	2.22	%	113,406	1,235	2.20	%
Total interest bearing liabilities	9,680,173	21,988	0.46	%	7,067,668	17,702	0.51	%
Demand deposits	6,201,909				3,506,407			
Other liabilities	157,151				101,040			
Stockholders' equity	1,513,221				1,209,599			
Total liabilities and stockholders' equity	$17,552,454				$11,884,714			
Net interest income(2)		$272,314				$223,808		
Net interest margin			3.22	%			3.93	%
Net interest spread			3.02	%			3.73	%
Loan spread			3.81	%			4.16	%

(1) The loan averages include loans on which the accrual of interest has been discontinued and are stated net of unearned income.

(2) Taxable equivalent rates used where applicable.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

Statements and financial analysis contained in this report that are not historical facts are forward-looking statements made pursuant to the safe harbor provisions of federal securities laws. Forward-looking statements may also be contained in our future filings with SEC, in press releases and in oral and written statements made by us or with our approval that are not statements of historical fact. Forward-looking statements describe our future plans, strategies and expectations and are based on certain assumptions. Words such as “believes”, “expects,” “estimates,” “anticipates”, “plans”, “goals”, “objectives”, “expects”, “intends”, “seeks”, “likely”, “targeted”, “continue”, “remain”, “will”, “should”, “may” and ot expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements. Forward-looking statements may include, among other things, statements about our confidence in our strategies and our expectations about financial performance, market growth, market and regulatory trends and developments, acquisitions and divestitures, new technologies, services and opportunities and earnings.

Forward-looking statements are subject to various risks and uncertainties, which change over time, are based on management’s expectations and assumptions at the time the statements are made and are not guarantees of future results. Important factors that could cause actual results to differ materially from the forward-looking statements include, but are not limited to, the following:

- Deterioration of the credit quality of our loan portfolio, increased default rates and loan losses or adverse changes in the industry concentrations of our loan portfolio.
- Developments adversely affecting our commercial, entrepreneurial and professional customers.
- Changes in the U.S. economy in general or the Texas economy specifically resulting in deterioration of credit quality or reduced demand for credit or other financial services we offer, including declines and volatility in oil and gas prices.
- Changes in the value of commercial and residential real estate securing our loans or in the demand for credit to support the purchase and ownership of such assets.
- The failure of assumptions supporting our allowance for loan losses causing it to become inadequate as loan quality decreases and losses and charge-offs increase.
- A failure to effectively manage our interest rate risk resulting from unexpectedly large or sudden changes in interest rates or rate or maturity imbalances in our assets and liabilities.
- Failure to execute our business strategy, including any inability to expand into new markets and lines of business in Texas, regionally and nationally.
- Loss of access to capital market transactions and other sources of funding, or a failure to effectively balance our funding sources with cash demands by depositors and borrowers.
- Failure to successfully develop and launch new lines of business and new products and services within the expected time frames and budgets, or failure to anticipate and appropriately manage the associated risks.
- The failure to attract and retain key personnel or the loss of key individuals or groups of employees.
- Legislative and regulatory changes imposing further restrictions and costs on our business, a failure to remain well capitalized or well managed or regulatory enforcement actions against us.
- An increase in the incidence or severity of fraud, illegal payments, security breaches and other illegal acts impacting our bank and our customers.
- Structural changes in the markets for origination, sale and servicing of residential mortgages.
- Increased or more effective competition from banks and other financial service providers in our markets.
- Material failures of our accounting estimates and risk management processes based on management judgment, or the supporting analytical and forecasting models.
- Unavailability of funds obtained from capital transactions or from our bank to fund our obligations.
- Failures of counterparties or third party vendors to perform their obligations.
- Failures or breaches of our information systems that are not effectively managed.

- Severe weather, natural disasters, acts of war or terrorism and other external events.

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- Incurrence of material costs and liabilities associated with legal and regulatory proceedings and related matters with respect to the financial services industry, including those directly involving us or our bank.
- Failure of our risk management strategies and procedures, including failure or circumvention of our controls.

Actual outcomes and results may differ materially from what is expressed in our forward-looking statements and from our historical financial results due to the factors discussed elsewhere in this report or disclosed in our other SEC filings. Forward-looking statements included herein should not be relied upon as representing our expectations or beliefs as of any date subsequent to the date of this report. Except as required by law, we undertake no obligation to revise any forward-looking statements contained in this report, whether as a result of new information, future events or otherwise. The factors discussed herein are not intended to be a complete summary of all risks and uncertainties that may affect our businesses. Though we strive to monitor and mitigate risk, we cannot anticipate all potential economic, operational and financial developments that may adversely impact our operations and our financial results. Forward-looking statements should not be viewed as predictions and should not be the primary basis upon which investors evaluate an investment in our securities.

Overview of Our Business Operations

We commenced our banking operations in December 1998. An important aspect of our growth strategy has been our ability to service and effectively manage a large number of loans and deposit accounts in multiple markets in Texas, as well as several lines of business serving a regional or national clientèle of commercial borrowers. Accordingly, we have created an operations infrastructure sufficient to support our lending and banking operations that we continue to build out as needed to serve a larger customer base and specialized industries.

The following discussion and analysis presents the significant factors affecting our financial condition as of June 30, 2015 and December 31, 2014 and results of operations for three and six months in the periods ended June 30, 2015 and 2014. This discussion should be read in conjunction with our consolidated financial statements and notes to the financial statements appearing in Part I, Item 1 of this report.

Results of Operations

Summary of Performance

We reported net income of $37.9 million and net income available to common stockholders of $35.5 million, or $0.76 per diluted common share, for the second quarter of 2015 compared to net income of $33.4 million and net income available to common stockholders of $31.0 million, or $0.71 per diluted common share, for the second quarter of 2014. Return on average common equity (“ROE”) was 10.32% and return on average assets ("ROA") was .83% for the second quarter of 2015, compared to 11.38% and 1.08%, respectively, for the second quarter of 2014. Net income and net income available to common stockholders for the six months ended June 30, 2015, totaled $73.0 million and $68.1 million, respectively, or $1.47 per diluted common share, compared to net income and net income available to common stockholders of $61.7 million and $56.8 million, respectively, or $1.30 per diluted common share, for the same period in 2014. ROE was 10.08% and ROA was .84% for the six months ended June 30, 2015 compared to 10.81% and 1.05%, respectively, for the six months ended June 30, 2014. The ROE decrease resulted from an increase in average common equity for the three and six months ended June 30, 2015, as compared to the same periods in 2014, related to the equity offering completed in the fourth quarter of 2014. The offering increased total equity by $149.7 million, and also had a dilutive effect on earnings per common share for the three and six months ended June 30, 2015 as compared to the same periods in 2014. The ROA decrease resulted from a combination of reduced yields on loans and an increase in average liquidity assets during the three and six months ended June 30, 2015 compared to the same periods of 2014.

Net income increased $4.5 million, or 14%, for the three months ended June 30, 2015, as compared to the same period in 2014. The increase was primarily the result of a $26.9 million increase in net interest income and a $2.2 million increase in non-interest income, offset by a $10.5 million increase in the provision for credit losses, a, $11.5 million increase in non-interest expense and a $2.6 million increase in income tax expense. Net income increased $11.3 million, or 18%, during the six months ended June 30, 2015, primarily as the result of a $48.6 million increase in net interest income and a $4.1 million increase in non-interest income, offset by a $16.5 million increase in the provision for credit losses, an $18.7 million increase in non-interest expense and a $6.2 million increase in income tax expense.

Details of the changes in the various components of net income are further discussed below.

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Net Interest Income

Net interest income was $142.3 million for the second quarter of 2015, compared to $115.4 million for the second quarter of 2014. The increase was due to an increase in average earning assets of $5.8 billion as compared to the second quarter of 2014. The increase in average earning assets included a $3.7 billion increase in average net loans and a $2.1 billion increase in average liquidity assets, offset by a $14.0 million decrease in average securities. For the quarter ended June 30, 2015, average net loans, liquidity assets and securities represented approximately 87%, 13% and less than 1%, respectively, of average earning assets compared to 98%, 2% and less than 1% for the same quarter of 2014.

Average interest-bearing liabilities for the quarter ended June 30, 2015 increased $2.4 billion from the second quarter of 2014, which included a $1.5 billion increase in interest-bearing deposits and an $899.5 million increase in other borrowings. Average demand deposits increased from $3.6 billion at June 30, 2014 to $6.8 billion at June 30, 2015. The average cost of total deposits and borrowed funds declined slightly to .16% for the second quarter of 2015 compared to .17% for the same period of 2014. The cost of interest-bearing liabilities decreased from .51% for the quarter ended June 30, 2014 to .46% for the same period of 2015.

Net interest income was $272.3 million for the six months ended June 30, 2015, compared to $223.7 million for the same period in 2014. The increase was due to an increase in average earning assets of $5.6 billion as compared to the six months ended June 30, 2014. The increase in average earning assets included a $3.6 billion increase in average net loans and a $2.0 billion increase in average liquidity assets, offset by a $15.8 million decrease in average securities. For the six months ended June 30, 2015, average net loans, liquidity assets and securities represented approximately 87%, 13% and less than 1%, respectively, of average earning assets compared to 97%, 2% and less than 1% for the same quarter of 2014.

Average interest-bearing liabilities for the six months ended June 30, 2015 increased $2.6 billion from the six months of 2014, which included a $1.7 billion increase in interest-bearing deposits, a, $889.3 million increase in other borrowings and a $29.0 million increase in long-term debt as a result of the Bank’s issuance of subordinated notes in January 2014. Average demand deposits increased from $3.5 billion at June 30, 2014 to $6.2 billion at June 30, 2015. The average cost of total deposits and borrowed funds declined slightly to .16% for the six months ended June 30, 2015 compared to .17% for the same period in 2014. The cost of interest-bearing liabilities decreased from .51% for the six months ended June 30, 2015 to .46% for the same period of 2015.

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The following table (in thousands) presents changes in taxable-equivalent net interest income between the first quarter of 2014 and the first quarter of 2015 and identifies the changes due to differences in the average volume of earning assets and interest-bearing liabilities and changes due to changes in the average interest rate on those assets and liabilities.

	Three months ended June 30, 2015/2014			Six months ended June 30, 2015/2014		
	Net	Change Due To(1)		Net	Change Due To(1)	
	Change	Volume	Yield/Rate	Change	Volume	Yield/Rate
Interest income:						
Securities(2)	$(175)	$(158)	$(17)	$(396)	$(362)	$(34)
Loans held for investment, mortgage finance loans	10,542	14,411	(3,869)	21,391	28,609	(7,218)
Loans held for investment	16,830	21,995	(5,165)	29,283	42,285	(13,002)
Federal funds sold	110	99	11	186	165	21
Deposits in other banks	1,227	1,049	178	2,328	2,326	2
Total	28,534	37,396	(8,862)	52,792	73,023	(20,231)
Interest expense:						
Transaction deposits	288	97	191	652	168	484
Savings deposits	937	676	261	2,053	1,611	442
Time deposits	267	112	155	422	179	243
Deposits in foreign branches	(96)	(86)	(10)	(133)	(129)	(4)
Borrowed funds	325	405	(80)	616	871	(255)
Long-term debt	(38)	—	(38)	676	871	(195)
Total	1,683	1,204	479	4,286	3,571	715
Net interest income	$26,851	$36,192	$(9,341)	$48,506	$69,452	$(20,946)

(1) Changes attributable to both volume and yield/rate are allocated to both volume and yield/rate on an equal basis.
(2) Taxable equivalent rates used where applicable and assume a 35% tax rate.

Net interest margin, which is defined as the ratio of net interest income to average earning assets, was 3.22% for the second quarter of 2015 compared to 3.87% for the second quarter of 2014. The year-over-year decrease was due to the growth in loans with lower yields, and the $2.1 billion increase in average balances of liquidity assets, which includes Federal funds sold and deposits in other banks. The cost of total deposits and borrowed funds decreased to .16% for the second quarter of 2015 compared to .17% for the second quarter of 2014. The spread on total earning assets, net of the cost of deposits and borrowed funds, was 3.31% for the second quarter of 2015 compared to 4.01% for the second quarter of 2014. The decrease resulted from the significant increase in liquidity assets coupled with a reduction in yields on total loans, primarily due to the increased proportion of mortgage finance loans to total loans. Total funding costs, including all deposits, long-term debt and stockholders' equity, decreased to .24% for the second quarter of 2015 compared to .31% for the second quarter of 2014. The average interest rate on long-term debt for the second quarter of 2015 was 4.84% compared to 4.88% for the same period of 2014.

Non-interest Income

The components of non-interest income were as follows (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Service charges on deposit accounts	$2,149	$1,764	$4,243	$3,460
Trust fee income	1,287	1,242	2,487	2,524
Bank owned life insurance (BOLI) income	476	521	960	1,030
Brokered loan fees	5,277	3,357	9,509	6,181
Swap fees	1,035	410	3,021	1,634

Other	2,547	3,239	4,818	6,060
Total non-interest income	$12,771	$10,533	$25,038	$20,889

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Non-interest income increased $2.2 million during the three months ended June 30, 2015 compared to the same period of 2014. This increase was primarily due to a $1.9 million increase in brokered loan fees as a result of an increase in mortgage finance volumes during the second quarter of 2015. Swap fees increased $625,000 during the three months ended June 30, 2015 compared to the same period of 2014. These fees fluctuate from quarter to quarter based on the number and volume of transactions closed during the quarter. Swap fees are fees related to customer swap transactions and are received from the institution that is our counterparty on the transaction. Service charges increased $385,000 during the three months ended June 30, 2015 compared to the same period of 2014 as a result of an increase in deposit balances year-over-year. Offsetting these increases was a $692,000 decrease in other non-interest income. Other non-interest income includes such items as letter of credit fees and other general operating income, none of which account for 1% or more of total interest income and non-interest income.

Non-interest income increased $4.1 million during the six months ended June 30, 2015 compared to the same period of 2014. This increase was primarily due to a $3.3 million increase in brokered loan fees as a result of an increase in mortgage finance volumes during the first six months of 2015. Swap fee income increased $1.4 million during the six months ended June 30, 2015 compared to the same period of 2014. These fees fluctuate from quarter to quarter based on the number and volume of transactions closed during the quarter. Swap fees are fees related to customer swap transactions and are received from the institution that is our counterparty on the transaction. Service charges increased $783,000 during the six months ended June 30, 2015 compared to the same period of 2014 as a result of an increase in deposit balances year-over-year. Offsetting these increases was a $1.2 million decrease in other non-interest income. Other non-interest income includes such items as letter of credit fees and other general operating income, none of which account for 1% or more of total interest income and non-interest income.

While management expects continued growth in certain components of non-interest income, the future rate of growth could be affected by increased competition from nationwide and regional financial institutions. In order to achieve growth in non-interest income, we may need to introduce new products or enter into new lines of business or expand existing lines of business. Any new product introduction or new market entry could place additional demands on capital and managerial resources.

Non-interest Expense

The components of non-interest expense were as follows (in thousands):

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Salaries and employee benefits	$48,200	$39,896	$94,028	$81,952
Net occupancy expense	5,808	5,073	11,499	9,841
Marketing	3,925	3,795	8,143	7,554
Legal and professional	5,618	7,181	9,666	12,583
Communications and technology	5,647	4,361	10,725	8,285
FDIC insurance assessment	4,211	2,544	8,001	5,269
Allowance and other carrying costs for OREO	6	11	15	56
Other(1)	7,861	6,904	15,716	13,542
Total non-interest expense	$81,276	$69,765	$157,793	$139,082

(1) Other expense includes such items as courier expenses, regulatory assessments other than FDIC insurance, due from bank charges and other general operating expenses, none of which account for 1% or more of total interest income and non-interest income.

Non-interest expense for the second quarter of 2015 increased $11.5 million, or 16%, to $81.3 million from $69.8 million in the second quarter of 2014. The increase is primarily attributable to an $8.3 million increase in salaries and employee benefits expense due to general business growth and as we respond to continued regulatory changes and strategic initiatives.

Net occupancy expense for the three months ended June 30, 2015 increased $735,000 as a result of general business growth and continued build-out needed to support that growth.

Legal and professional expense for three months ended June 30, 2015 decreased $1.6 million compared to the same quarter of 2014. Our legal and professional expense will continue to fluctuate and could increase in the future due to general business growth and as we respond to continued regulatory changes and strategic initiatives.

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Communications and technology expense for the three months ended June 30, 2015 increased $1.3 million as a result of general business and customer growth and continued build-out needed to support that growth.
FDIC insurance assessment expense for the three months ended June 30, 2015 increased $1.7 million compared to the same quarter in 2014 as a result of the increase in total assets from June 30, 2014 to June 30, 2015.
Non-interest expense for the six months ended June 30, 2015 increased $18.7 million, or 13%, to $157.8 million from $139.1 million compared to the same period in 2014. The increase is primarily attributable to a $12.1 million increase in salaries and employee benefits expense due to general business growth and as we respond to continued regulatory changes and strategic initiatives.
Net occupancy expense for the six months ended June 30, 2015 increased $1.7 million as a result of general business growth and continued build-out needed to support that growth.
Legal and professional expense for six months ended June 30, 2015 decreased $2.9 million compared to the same quarter of 2014. Our legal and professional expense will continue to fluctuate and could increase in the future due to general business growth and as we respond to continued regulatory changes and strategic initiatives.
Communications and technology expense for the six months ended June 30, 2015 increased $2.4 million as a result of general business and customer growth and continued build-out needed to support that growth.
FDIC insurance assessment expense for the six months ended June 30, 2015 increased $2.7 million compared to the same quarter in 2014 as a result of the increase in total assets from June 30, 2014 to June 30, 2015.

Analysis of Financial Condition

Loan Portfolio

Loans were as follows as of the dates indicated (in thousands):

	June 30, 2015	December 31, 2014
Commercial	$6,388,707	$5,869,219
Mortgage finance	4,906,415	4,102,125
Construction	1,837,532	1,416,405
Real estate	2,834,005	2,807,127
Consumer	23,789	19,699
Leases	97,025	99,495
Gross loans held for investment	16,087,473	14,314,070
Deferred income (net of direct origination costs)	(57,733)	(57,058)
Allowance for loan losses	(118,770)	(100,954)
Total loans held for investment, net	$15,910,970	$14,156,058

Total loans net of allowance for loan losses at June 30, 2015 increased $1.8 billion from December 31, 2014 to $15.9 billion. Our business plan focuses primarily on lending to middle market businesses and successful professionals and entrepreneurs, and as such, commercial, real estate and construction loans have comprised a majority of our loan portfolio. Consumer loans generally have represented 1% or less of the portfolio. Mortgage finance loans relate to our mortgage warehouse lending operations in which we invest in mortgage loan ownership interests that are typically sold within 10 to 20 days. Volumes fluctuate based on the level of market demand for the product and the number of days between purchase and sale of the loans as well as overall market interest rates and tend to peak at the end of each month.
We originate a substantial majority of all loans held for investment (excluding mortgage finance loans). We also participate in syndicated loan relationships, both as a participant and as an agent. As of June 30, 2015, we had $1.7 billion in syndicated loans, $347.3 million of which we administer as agent. All syndicated loans, whether we act as agent or participant, are underwritten to the same standards as all other loans we originate. As of June 30, 2015, $58.6 million of our syndicated loans were on non-accrual.

Portfolio Geographic Concentration

As of June 30, 2015, a substantial majority of our loans held for investment, excluding our mortgage finance loans and other national lines of business, were to businesses with headquarters and operations in Texas. This geographic concentration subjects the loan portfolio to the general economic conditions within this area. Additionally, we may make loans to these businesses and individuals, secured by assets located outside of Texas. The risks created by this concentration have been considered by management in the determination of the adequacy of the allowance for loan losses. Management believes the allowance for loan losses is appropriate to cover estimated losses on loans at each balance sheet date.

Summary of Loan Loss Experience

The provision for credit losses is a charge to earnings to maintain the reserve for loan losses at a level consistent with management’s assessment of the loan portfolio in light of current economic conditions and market trends. We recorded a provision of $14.5 million during the second quarter of 2015 compared to $11.0 million in the first quarter of 2014 and $4.0 million in the second quarter of 2014. The provision was driven by the application of our methodology. The increase was primarily related to the growth in traditional loans held for investment, excluding mortgage finance loans, as well as a change in applied risk weights which are based in part on historical loss experience as well as changes in the composition of our pass-rated loan portfolio.

We continue to maintain an unallocated reserve component to compensate for the uncertainty and complexity in estimating loan and lease losses, including factors and conditions that may not be fully reflected in the determination and application of the allowance allocation percentages. We believe the level of unallocated reserves at June 30, 2015 is warranted due to the continued uncertain economic environment which has produced losses, including those resulting from borrowers' misstatement of financial information or inaccurate certification of collateral values. Such losses are not necessarily correlated with historical loss trends or general economic conditions. Our methodology used to calculate the allowance considers historical losses; however, the historical loss rates for specific product types or credit risk grades may not fully incorporate the effects of continued weakness in the economy.

The reserve for loan losses is comprised of specific reserves for impaired loans and an estimate of losses inherent in the portfolio at the balance sheet date, but not yet identified with specified loans. We regularly evaluate our reserve for loan losses to maintain an appropriate level to absorb estimated loan losses inherent in the loan portfolio. Factors contributing to the determination of reserves include the creditworthiness of the borrower, changes in the value of pledged collateral, and general economic conditions. All loan commitments rated substandard or worse and greater than $500,000 are specifically reviewed for loss potential. For loans deemed to be impaired, a specific allocation is assigned based on the losses expected to be realized from those loans. For purposes of determining the general reserve, the portfolio is segregated by credit grades, and then further segregated by product types to recognize differing risk profiles among categories. Credit grades are assigned to all loans. Each credit grade is assigned a risk factor, or reserve allocation percentage. These risk factors are multiplied by the outstanding principal balance and risk-weighted by product type to calculate the required reserve. A similar process is employed to calculate a reserve assigned to off-balance sheet commitments, specifically unfunded loan commitments and letters of credit. Even though portions of the allowance may be allocated to specific loans, the entire allowance is available for any credit that, in management’s judgment, should be charged off.

The reserve allocation percentages assigned to each credit grade have been developed based primarily on an analysis of our historical loss rates. The allocations are adjusted for certain qualitative factors, including general economic conditions, changes in credit policies and lending standards. Changes in the trend and severity of problem loans can cause the estimation of losses to differ from past experience. In addition, the reserve reflects the results of reviews performed by the Company's independent Credit Review function as reflected in their confirmations of assigned credit grades within the portfolio. The Credit Review function reports to the Credit Risk Committee of the Company's board of directors with administrative oversight from the Company's Chief Risk Officer. The portion of the allowance that is not derived by the allowance allocation percentages compensates for the uncertainty and complexity in estimating loan and lease losses including factors and conditions that may not be fully reflected in the determination and application of the allowance allocation percentages. Examples of risks that support the Company's maintaining an unallocated reserve include the possibility of precipitous negative changes in economic conditions and borrowers' submission of financial statements or certifications of collateral value that subsequently prove to be materially inaccurate for reason of either misstatement or omission of critical information. These situations, while not common, do not necessarily correlate well with the general risk profile presented by assigned credit grade and product type categories. We evaluate many such factors and conditions in determining the unallocated portion of the allowance, including the amount and frequency of losses attributable to issues not specifically addressed or included in the determination and application of the allowance allocation percentages. We believe the allowance is appropriate, given management’s assessment of potential losses

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within the portfolio as of the evaluation date, the significant growth in the loan and lease portfolio, current economic conditions in the Company's market areas and other factors.

The methodology used in the periodic review of reserve adequacy, which is performed at least quarterly, is designed to be dynamic and responsive to changes in portfolio credit quality. The changes are reflected in the general reserve and in specific reserves as the collectability of larger classified loans is evaluated with new information. As our portfolio has matured, historical loss ratios have been closely monitored, and our reserve adequacy relies primarily on our loss history. The review of the reserve adequacy is performed by executive management and presented to a committee of our board of directors for their review. The committee reports to the board as part of the board's review on a quarterly basis of the Company's consolidated financial statements.

The combined reserve for credit losses, which includes a liability for losses on unfunded commitments, totaled $126.7 million at June 30, 2015, $108.0 million at December 31, 2014 and $96.7 million at June 30, 2014. The total reserve percentage increased to 1.14% at June 30, 2015 from 1.06% and 1.06% of loans excluding mortgage finance loans at December 31, 2014 and June 30, 2014, respectively.

At June 30, 2015, we believe the reserve is sufficient to cover all expected losses in the portfolio and has been derived from consistent application of the methodology described above.

Should any of the factors considered by management in evaluating the adequacy of the allowance for loan losses change, our estimate of expected losses in the portfolio could also change, which would affect the level of future provisions for loan losses.

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Activity in the reserve for loan losses is presented in the following table (in thousands, except percentage data and ratios):

	Six months ended June 30, 2015	Year ended December 31, 2014	Six months ended June 30, 2014
Reserve for loan losses:			
Beginning balance	$100,954	$87,604	$87,604
Loans charged-off:			
Commercial	8,520	9,803	7,526
Real estate	346	296	296
Consumer	62	266	101
Total charge-offs	8,928	10,365	7,923
Recoveries:			
Commercial	1,710	2,762	2,243
Real estate	20	79	43
Construction	355	—	—
Consumer	10	162	31
Leases	23	1,082	1,049
Total recoveries	2,118	4,085	3,366
Net charge-offs	6,810	6,280	4,557
Provision for loan losses	24,626	19,630	8,067
Ending balance	$118,770	$100,954	$91,114
Reserve for off-balance sheet credit losses:			
Beginning balance	$7,060	$4,690	$4,690
Provision for off-balance sheet credit losses	874	2,370	933
Ending balance	$7,934	$7,060	$5,623
Total reserve for credit losses	$126,704	$108,014	$96,737
Total provision for credit losses	$25,500	$22,000	$9,000
Reserve for loan losses to loans	0.74 %	0.71 %	0.71 %
Reserve for loan losses to loans excluding mortgage finance loans	1.07 %	0.99 %	1.00 %
Net charge-offs to average loans(1)	0.09 %	0.05 %	0.08 %
Net charge-offs to average loans excluding mortgage finance loans(1)	0.13 %	0.07 %	0.10 %
Total provision for credit losses to average loans	0.35 %	0.18 %	0.16 %
Total provision for credit losses to average loans excluding mortgage finance loans	0.48 %	0.24 %	0.21 %
Recoveries to total charge-offs	23.72 %	39.41 %	42.48 %
Reserve for off-balance sheet credit losses to off-balance sheet credit commitments	0.15 %	0.13 %	0.12 %
Combined reserves for credit losses to loans held for investment	0.79 %	0.76 %	0.75 %
Combined reserves for credit losses to loans held for investment excluding mortgage finance loans	1.14 %	1.06 %	1.06 %
Non-performing assets:			
Non-accrual loans(4)	$122,920	$43,304	$41,565
OREO(3)	609	568	685
Total	$123,529	$43,872	$42,250
Restructured loans	$249	$1,806	$249
Loans past due 90 days and still accruing(2)	5,482	5,274	4,793

Reserve for loan losses to non-accrual loans	1.0x	2.3x	2.2x

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(1) Interim period ratios are annualized.

(2) At June 30, 2015, December 31, 2014 and June 30, 2014, loans past due 90 days and still accruing include premium finance loans of $4.8 million, $3.7 million and $4.6 million, respectively. These loans are generally secured by obligations of insurance carriers to refund premiums on cancelled insurance policies. The refund of premiums from the insurance carriers can take 180 days or longer from the cancellation date.

(3) We did not have a valuation allowance recorded against the OREO balance at June 30, 2015, December 31, 2014 or June 30, 2014.

(4) As of June 30, 2015, December 31, 2014 and June 30, 2014, non-accrual loans included $28.2 million, $12.1 million and $16.2 million, respectively, in loans that met the criteria for restructured.

Non-performing Assets

Non-performing assets include non-accrual loans and leases and repossessed assets. The table below summarizes our non-accrual loans by type and OREO (in thousands):

	June 30, 2015	December 31, 2014	June 30, 2014
Commercial	$92,065	$33,122	$25,545
Construction	16,749	—	—
Real estate	7,669	9,947	15,998
Consumer	—	62	—
Leases	6,437	173	22
Total non-accrual loans	122,920	43,304	41,565
Repossessed assets:			
OREO	609	568	685
Total non-performing assets	$123,529	$43,872	$42,250

The table below summarizes the non-accrual loans as segregated by loan type and type of property securing the credit as of June 30, 2015 (in thousands):

Non-accrual loans:	
Commercial	
Lines of credit secured by the following:	
Oil and gas properties	$37,984
Assets of the borrowers	53,206
Other	875
Total commercial	92,065
Construction	
Unimproved land and/or undeveloped lots	16,749
Real estate	
Secured by:	
Commercial property	2,951
Unimproved land and/or undeveloped residential lots	3,639
Other	1,079
Total real estate	7,669
Leases (commercial leases primarily secured by assets of the lessor)	6,437
Total non-accrual loans	$122,920

Generally, we place loans on non-accrual when there is a clear indication that the borrower's cash flow may not be sufficient to meet payments as they become due, which is generally when a loan is 90 days past due. When a loan is placed on non-accrual status, all previously accrued and unpaid interest is reversed. Interest income is subsequently recognized on a cash basis as long

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as the remaining unpaid principal amount of the loan is deemed to be fully collectible. If collectability is questionable, then cash payments are applied to principal. A loan is placed back on accrual status when both principal and interest are current and it is probable that we will be able to collect all amounts due (both principal and interest) according to the terms of the loan agreement.

Potential problem loans consist of loans that are performing in accordance with contractual terms but for which we have concerns about the borrower's ability to comply with repayment terms because of the borrower's potential financial difficulties. We monitor these loans closely and review their performance on a regular basis. At June 30, 2015 and December 31, 2014, we had $15.2 million and $16.3 million, respectively, in loans of this type which were not included in either non-accrual or 90 days past due categories.

The following table summarizes the assets held in OREO at June 30, 2015 (in thousands):

Undeveloped land and residential lots	$487
Other	122
Total OREO	$609

When foreclosure occurs, fair value, which is generally based on appraised values, may result in partial charge-off of a loan upon taking the collateral, and so long as the collateral is retained, subsequent reductions in appraised values will result in valuation adjustments taken as non-interest expense. In addition, if the decline in value is believed to be permanent and not just driven by market conditions, a direct write-down to the OREO balance may be taken. We generally pursue sales of OREO when conditions warrant, but we may choose to hold certain properties for a longer term, which can result in additional exposure related to the appraised values during that holding period. We did not record a valuation expense during the three or six months ended June 30, 2015 or June 30, 2014.

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Liquidity and Capital Resources

In general terms, liquidity is a measurement of our ability to meet our cash needs. Our objective in managing our liquidity is to maintain our ability to meet loan commitments, purchase securities or repay deposits and other liabilities in accordance with their terms, without an adverse impact on our current or future earnings. Our liquidity strategy is guided by policies, which are formulated and monitored by our senior management and our Balance Sheet Management Committee ("BSMC"), and which take into account the demonstrated marketability of assets, the sources and stability of funding and the level of unfunded commitments. We regularly evaluate all of our various funding sources with an emphasis on accessibility, stability, reliability and cost effectiveness. For the year ended December 31, 2014 and for the six months ended June 30, 2015 our principal source of funding has been our customer deposits, supplemented by our borrowings, primarily short-term Federal funds purchased and FHLB borrowings used to fund mortgage finance assets.

Our liquidity needs for support of growth in loans held for investment have been fulfilled through growth in our core customer deposits. Our goal is to obtain as much of our funding for loans held for investment and other earning assets as possible from deposits of these core customers. These deposits are generated principally through development of long-term relationships with customers, with a significant focus on treasury management products. In addition to deposits from our core customers, we also have access to deposits through brokered customer relationships. For regulatory purposes, these relationship brokered deposits are categorized as brokered deposits; however, since these deposits arise from a customer relationship, which involves extensive treasury services, we consider these deposits to be core deposits for our reporting purposes. We also have access to incremental deposits through brokered retail certificates of deposit, or CDs. These traditional brokered deposits are generally of short maturities, 30 to 90 days, and are used to supplement temporary differences in the growth in loans, compared to customer deposits. The following table summarizes our period-end and average year-to-date core customer deposits and brokered deposits (in millions):

	June 30, 2015		December 31, 2014		June 30, 2014	
Deposits from core customers	$12,623.2		$10,900.0		$8,642.9	
Deposits from core customers as a percent of total deposits	89.0	%	86.0	%	80.4	%
Relationship brokered deposits	$1,565.1		$1,773.3		$1,863.0	
Relationship brokered deposits as a percent of total deposits	11.0	%	14.0	%	17.3	%
Traditional brokered deposits	$—		$—		$251.4	
Traditional brokered deposits as a percent of total deposits	—	%	—	%	2.3	%
Average deposits from core customers(1)	$12,467.9		$9,135.0		$8,062.9	
Average deposits from core customers as a percent of total quarterly average deposits(1)	88.3	%	84.1	%	83.0	%
Average relationship brokered deposits(1)	$1,644.4		$1,709.8		$1,618.0	
Average relationship brokered deposits as a percent of total quarterly average deposits(1)	11.7	%	15.7	%	16.6	%
Average traditional brokered deposits(1)	$—		$20.7		$41.7	
Average traditional brokered deposits as a percent of total quarterly average deposits(1)	—	%	0.2	%	0.4	%

(1) Annual averages presented for December 31, 2014.

We have access to sources of brokered deposits that we estimate to be $3.5 billion. Based on our internal guidelines, we may choose to limit our use of these sources to a lesser amount. Customer deposits (total deposits, including relationship brokered deposits, minus brokered CDs) at June 30, 2015 increased by $1.5 billion from December 31, 2014 and increased $3.9 billion from June 30, 2014.

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Additionally, we have short-term borrowing sources available to supplement deposits and meet our funding needs. Such borrowings are generally used to fund our mortgage finance assets, due to their liquidity, short duration and interest spreads available. These borrowing sources typically include Federal funds purchased from our downstream correspondent bank relationships (which consist of banks that are smaller than our bank) and from our upstream correspondent bank relationships (which consist of banks that are larger than our bank), customer repurchase agreements, treasury, tax and loan notes and advances from the FHLB and the Federal Reserve. The following table summarizes our short-term borrowings as of June 30, 2015 (in thousands):

Federal funds purchased	$79,088
Repurchase agreements	29,919
FHLB borrowings	1,400,000
Total short-term borrowings	$1,509,007
Maximum short-term borrowings outstanding at any month-end during the year	$1,986,214

The following table summarizes our other borrowing capacities in excess of balances outstanding at June 30, 2015 (in thousands):

FHLB borrowing capacity relating to loans	$4,118,100
FHLB borrowing capacity relating to securities	1,523
Total FHLB borrowing capacity	$4,119,623
Unused Federal funds lines available from commercial banks	$1,280,000

The following table summarizes our long-term borrowings as of June 30, 2015 (in thousands):

Subordinated notes	$286,000
Trust preferred subordinated debentures	113,406
Total long-term borrowings	$399,406

At June 30, 2015, we had a revolving, non-amortizing line of credit with $100.0 million of unused capacity. This line of credit matures on December 22, 2015. The loan proceeds may be used for general corporate purposes including funding regulatory capital infusions into the Bank. The loan agreement contains customary financial covenants and restrictions. At June 30, 2015 and December 31, 2014, no borrowings were outstanding.

Our equity capital, including $150 million in preferred stock, averaged $1.5 billion for the six months ended June 30, 2015, as compared to $1.2 billion for the same period in 2014. We have not paid any cash dividends on our common stock since we commenced operations and have no plans to do so in the foreseeable future.

As of June 30, 2015 our capital ratios were above the levels required to be well capitalized. We believe that our earnings, periodic capital raising transactions, and the addition of loan and deposit relationships, will allow us to continue to grow organically.

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Commitments and Contractual Obligations

The following table presents significant fixed and determinable contractual payment obligations to third parties by payment date. Payments for borrowings do not include interest. Payments related to leases are based on actual payments specified in the underlying contracts. As of June 30, 2015, our significant fixed and determinable contractual obligations to third parties, excluding interest, were as follows (in thousands):

	Within One Year	After One but Within Three Years	After Three but Within Five Years	After Five Years	Total
Deposits without a stated maturity	$13,437,098	$—	$ —	$—	$13,437,098
Time deposits	725,373	20,126	5,679	—	751,178
Federal funds purchased and customer repurchase agreements	109,007	—	—	—	109,007
FHLB borrowings	1,400,000	—	—	—	1,400,000
Operating lease obligations(1)	15,764	31,582	30,890	47,031	125,267
Subordinated notes	—	—	—	286,000	286,000
Trust preferred subordinated debentures	—	—	—	113,406	113,406
Total contractual obligations	$15,687,242	$51,708	$ 36,569	$446,437	$16,221,956

(1) Non-balance sheet item.

Critical Accounting Policies

SEC guidance requires disclosure of “critical accounting policies.” The SEC defines “critical accounting policies” as those that are most important to the presentation of a company’s financial condition and results, and require management’s most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

We follow financial accounting and reporting policies that are in accordance with accounting principles generally accepted in the United States. The more significant of these policies are summarized in Note 1 to the consolidated financial statements. Not all these significant accounting policies require management to make difficult, subjective or complex judgments. However, we believe the policy described below meets the SEC’s definition of a critical accounting policy.

Management considers the policies related to the allowance for loan losses as the most critical to the financial statement presentation. The total allowance for loan losses includes activity related to allowances calculated in accordance with ASC 310, Receivables, and ASC 450, Contingencies. The allowance for loan losses is established through a provision for loan losses charged to current earnings. The amount maintained in the allowance reflects management’s continuing evaluation of the loan losses inherent in the loan portfolio. The allowance for loan losses is comprised of specific reserves assigned to certain classified loans and general reserves. Factors contributing to the determination of specific reserves include the creditworthiness of the borrower, and more specifically, changes in the expected future receipt of principal and interest payments and/or in the value of pledged collateral. A reserve is recorded when the carrying amount of the loan exceeds the discounted estimated cash flows using the loan’s initial effective interest rate or the fair value of the collateral for certain collateral dependent loans. For purposes of determining the general reserve, the portfolio is segregated by product types in order to recognize differing risk profiles among categories, and then further segregated by credit grades. See “Summary of Loan Loss Experience” and Note 4 – Loans and Allowance for Loan Losses in the accompanying notes to the consolidated financial statements included elsewhere in this report for further discussion of the risk factors considered by management in establishing the allowance for loan losses.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is a broad term for the risk of economic loss due to adverse changes in the fair value of a financial instrument. These changes may be the result of various factors, including interest rates, foreign exchange rates, commodity prices, or equity prices. Additionally, the financial instruments subject to market risk can be classified either as held for trading purposes or held for other than trading.

We are subject to market risk primarily through the effect of changes in interest rates on our portfolio of assets held for purposes other than trading. Additionally, we have some market risk relative to commodity prices through our energy lending activities. Petroleum and natural gas commodity prices declined substantially during 2014. Such declines in commodity prices, if sustained or continued, could negatively impact our energy clients' ability to perform on their loan obligations. Management does not expect the current decline in petroleum and natural gas commodity prices to have a material adverse effect on our financial position. Foreign exchange rates, commodity prices and/or equity prices do not pose significant market risk to us.

The responsibility for managing market risk rests with the BSMC, which operates under policy guidelines established by our board of directors. The negative acceptable variation in net interest revenue due to a 200 basis point increase or decrease in interest rates is generally limited by these guidelines to +/- 5%. These guidelines also establish maximum levels for short-term borrowings, short-term assets and public and brokered deposits. They also establish minimum levels for unpledged assets, among other things. Compliance with these guidelines is the ongoing responsibility of the BSMC, with exceptions reported to our board of directors on a quarterly basis. Additionally, the Credit Policy Committee ("CPC") specifically manages risk relative to commodity price market risks. The CPC establishes maximum portfolio concentration levels for energy loans as well as maximum advance rates for energy collateral.

Interest Rate Risk Management

Our interest rate sensitivity is illustrated in the following table. The table reflects rate-sensitive positions as of June 30, 2015, and is not necessarily indicative of positions on other dates. The balances of interest rate sensitive assets and liabilities are presented in the periods in which they next reprice to market rates or mature and are aggregated to show the interest rate sensitivity gap. The mismatch between repricings or maturities within a time period is commonly referred to as the “gap” for that period. A positive gap (asset sensitive), where interest rate sensitive assets exceed interest rate sensitive liabilities, generally will result in the net interest margin increasing in a rising rate environment and decreasing in a falling rate environment. A negative gap (liability sensitive) will generally have the opposite results on the net interest margin. To reflect anticipated prepayments, certain asset and liability categories are shown in the table using estimated cash flows rather than contractual cash flows. The Company employs interest rate floors in certain variable rate loans to enhance the yield on those loans at times when market interest rates are extraordinarily low. The degree of asset sensitivity, spreads on loans and net interest margin may be reduced until rates increase by an amount sufficient to eliminate the effects of floors. The adverse effect of floors as market rates increase may also be offset by the positive gap, the extent to which rates on deposits and other funding sources lag increasing market rates and changes in composition of funding.

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Interest Rate Sensitivity Gap Analysis
June 30, 2015
(In thousands)

	0-3 mo Balance	4-12 mo Balance	1-3 yr Balance	3+ yr Balance	Total Balance
Assets:					
Securities(1)	$8,084	$12,127	5,994	$9,156	$35,361
Total variable loans	13,973,310	84,080	11,422	15,435	14,084,247
Total fixed loans	377,917	1,026,855	327,944	270,510	2,003,226
Total loans(2)	14,351,227	1,110,935	339,366	285,945	16,087,473
Total interest sensitive assets	$14,359,311	$1,123,062	$345,360	$295,101	$16,122,834
Liabilities:					
Interest-bearing customer deposits	$7,164,291	$—	$—	$—	$7,164,291
CDs & IRAs	212,785	306,322	20,126	5,679	544,912
Traditional brokered deposits	—	—	—	—	—
Total interest-bearing deposits	7,377,076	306,322	20,126	5,679	7,709,203
Repurchase agreements, Federal funds purchased, FHLB borrowings	1,509,007	—	—	—	1,509,007
Subordinated notes	—	—	—	286,000	286,000
Trust preferred subordinated debentures	—	—	—	113,406	113,406
Total borrowings	1,509,007	—	—	399,406	1,908,413
Total interest sensitive liabilities	$8,886,083	$306,322	$20,126	$405,085	$9,617,616
Gap	$5,473,228	$816,740	$325,234	$(109,984)	$—
Cumulative Gap	5,473,228	6,289,968	6,615,202	6,505,218	6,505,218
Demand deposits					$6,479,073
Stockholders' equity					1,554,529
Total					$8,033,602

(1) Securities based on fair market value.
(2) Loans are stated at gross.

The table above sets forth the balances as of June 30, 2015 for interest bearing assets, interest bearing liabilities, and the total of non-interest bearing deposits and stockholders' equity. While a gap interest table is useful in analyzing interest rate sensitivity, an interest rate sensitivity simulation provides a better illustration of the sensitivity of earnings to changes in interest rates. Earnings are also affected by the effects of changing interest rates on the value of funding derived from demand deposits and stockholders' equity. We perform a sensitivity analysis to identify interest rate risk exposure on net interest income. We quantify and measure interest rate risk exposure using a model to dynamically simulate the effect of changes in net interest income relative to changes in interest rates and loan and deposit account balances over the next twelve months based on three interest rate scenarios. These are a "most likely" rate scenario and two "shock test" scenarios.

The "most likely" rate scenario is based on the consensus forecast of future interest rates published by independent sources. These forecasts incorporate future spot rates and relevant spreads of instruments that are actively traded in the open market. The Federal Reserve's Federal funds target affects short-term borrowing rates; the prime lending rate and LIBOR are the basis for most of our variable-rate loan pricing. The 10-year mortgage rate is also monitored because of its effect on prepayment speeds for mortgage-backed securities. We believe these are our primary interest rate exposures. We are not currently using derivatives to manage our interest rate exposure.

The two “shock test” scenarios assume a sustained parallel 100 and 200 basis point increase in interest rates. As short-term rates have remained low through 2014 and the first six months of 2015, we do not believe that analysis of an assumed decrease in interest rates would provide meaningful results. We will continue to evaluate these scenarios as interest rates change, until short-term rates rise above 3.0%, at which point we will resume evaluations of shock scenarios in which interest rates decrease.

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Our interest rate risk exposure model incorporates assumptions regarding the level of interest rate or balance changes on indeterminable maturity deposits (demand deposits, interest-bearing transaction accounts and savings accounts) for a given level of market rate changes. These assumptions have been developed through a combination of historical analysis and future expected pricing behavior. Changes in prepayment behavior of mortgage-backed securities and residential and commercial mortgage loans in each rate environment are captured using industry estimates of prepayment speeds for various coupon segments of the portfolio. The impact of planned growth and new business activities is factored into the simulation model. This modeling indicated interest rate sensitivity as follows (in thousands):

	Anticipated Impact Over the Next Twelve Months as Compared to Most Likely Scenario		Anticipated Impact Over the Next Twelve Months as Compared to Most Likely Scenario	
	100 bp Increase	200 bp Increase	100 bp Increase	200 bp Increase
	June 30, 2015		June 30, 2014	
Change in net interest income	$ 84,883	$ 178,313	$ 54,031	$ 119,028

The simulations used to manage market risk are based on numerous assumptions regarding the effect of changes in interest rates on the timing and extent of repricing characteristics, future cash flows and customer behavior. These assumptions are inherently uncertain and, as a result, the model cannot precisely estimate net interest income or precisely predict the impact of higher or lower interest rates on net interest income. Actual results may differ from simulated results due to timing, magnitude and frequency of interest rate changes as well as changes in market conditions and management strategies, among other factors.

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ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the supervision and participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based upon that evaluation, we have concluded that, as of the end of such period, our disclosure controls and procedures were effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports that we file or submit under the Exchange Act and were effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to the Company’s management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II—OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are subject to various claims and legal actions related to operating activities that arise in the ordinary course of business. Management does not currently expect the ultimate disposition of these matters to have a material adverse impact on our financial statements.

ITEM 1A. RISK FACTORS

There have been no material changes in the risk factors previously disclosed in the Company’s 2014 Form 10-K for the fiscal year ended December 31, 2014.

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ITEM 6. EXHIBITS

(a) Exhibits

10.1*	Texas Capital Bancshares, Inc. 2015 Long-Term Incentive Plan (included as Exhibit 10.1 to the Company's Current Report on Form 8-K filed with the SEC on May 21, 2015, and incorporated herein by reference.
10.2*	Form of Restricted Stock Unit Award Agreement for Directors, filed herewith.
10.3*	Form of Restricted Stock Unit Award Agreement for the Executive Officers, filed herewith.
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, filed herewith.
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, filed herewith.
32.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(b) of the Exchange Act and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, furnished herewith.
32.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(b) of the Exchange Act and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, furnished herewith.
101	The following materials from Texas Capital Bancshares, Inc.'s Quarterly Report on Form 10-Q for the quarter ended June 30, 2015, formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Statements of Income, (ii) Consolidated Balance Sheets, (iii) Consolidated Statements of Cash Flows, and (iv) Notes to Consolidated Financial Statements

*Denotes management contract or compensatory plan.

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SIGNATURES
Pursuant to the requirements 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.
TEXAS CAPITAL BANCSHARES, INC.
Date: July 23, 2015
/s/ Peter B. Bartholow
Peter B. Bartholow
Chief Financial Officer
(Duly authorized officer and principal financial officer)

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