

TEXAS CAPITAL BANCSHARES INC/TX

Form 10-K

February 17, 2017

Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2016

¨ 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, \_\_\_\_\_ 75201

Dallas, Texas, U.S.A.

(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)

Securities registered under Section 12(b) of the Exchange Act:

Common stock, par value \$0.01 per share

(Title of class)

6.50% Non-Cumulative Perpetual Preferred Stock Series A, par value \$0.01 per share

(Title of class)

Warrants to Purchase Common Stock (expiring January 16, 2019), par value \$0.01 per share

(Title of class)

The Nasdaq Stock Market LLC

(Name of Exchange on Which Registered)

Securities registered under Section 12(g) of the Exchange Act: NONE

Indicate by check mark if the issuer is a well-known seasoned issuer pursuant to Section 13 or Section 15(d) of the Securities Act. Yes  No

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of “large accelerated filer,” “accelerated filer” and “smaller reporting company”

Edgar Filing: TEXAS CAPITAL BANCSHARES INC/TX - Form 10-K

in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer  Accelerated Filer  Non-Accelerated Filer  Non-Accelerated Filer

(Do not check if a 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

As of June 30, 2016, the last business day of the registrant's most recently completed second fiscal quarter, the aggregate market value of the shares of common stock held by non-affiliates, based on the closing price per share of the registrant's common stock as reported on The Nasdaq Global Select Market, was approximately \$2,125,503,000. There were 49,518,387 shares of the registrant's common stock outstanding on February 15, 2017.

Documents Incorporated by Reference

Portions of the registrant's Proxy Statement relating to the 2016 Annual Meeting of Stockholders, which will be filed no later than April 7, 2016, are incorporated by reference into Part III of this Form 10-K.

---

Table of Contents

TABLE OF CONTENTS

PART I

Item 1. <u>Business</u>	<u>3</u>
Item 1A. <u>Risk Factors</u>	<u>11</u>
Item 1B. <u>Unresolved Staff Comments</u>	<u>23</u>
Item 2. <u>Properties</u>	<u>23</u>
Item 3. <u>Legal Proceedings</u>	<u>23</u>
Item 4. <u>Mine Safety Disclosures</u>	<u>23</u>

PART II

Item 5. <u>Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	<u>23</u>
Item 6. <u>Selected Consolidated Financial Data</u>	<u>26</u>
Item 7. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>29</u>
Item 7A. <u>Quantitative and Qualitative Disclosure About Market Risk</u>	<u>49</u>
Item 8. <u>Financial Statements and Supplementary Data</u>	<u>52</u>
Item 9. <u>Changes in and Disagreements With Accountants on Accounting and Financial Disclosures</u>	<u>96</u>
Item 9A. <u>Controls and Procedures</u>	<u>96</u>
Item 9B. <u>Other Information</u>	<u>98</u>

PART III

Item 10. <u>Directors, Executive Officers and Corporate Governance</u>	<u>98</u>
Item 11. <u>Executive Compensation</u>	<u>98</u>
Item 12. <u>Security Ownership of Certain Beneficial Owners and Management And Related Stockholder Matters</u>	<u>98</u>
Item 13. <u>Certain Relationships and Related Transactions, and Director Independence</u>	<u>98</u>
Item 14. <u>Principal Accounting Fees and Services</u>	<u>98</u>

PART IV

Item 15. <u>Exhibits, Financial Statement Schedules</u>	<u>98</u>
---	-----------

Table of Contents

## ITEM 1. BUSINESS

## Background

The disclosures set forth in this item are qualified by Item 1A. Risk Factors and the section captioned “Forward-Looking Statements” in Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations of this report and other cautionary statements set forth elsewhere in this report.

Texas Capital Bancshares, Inc. (“we”, “us” or the “Company”), a Delaware corporation organized in 1996, is the parent of Texas Capital Bank, National Association (the “Bank”). The Company is a registered bank holding company and a financial holding company.

The Bank is headquartered in Dallas, with primary banking offices in Austin, Dallas, Fort Worth, Houston and San Antonio, the five largest metropolitan areas of Texas. Substantially all of our business activities are conducted through the Bank. We have focused on organic growth, maintenance of credit quality and recruiting and retaining experienced bankers with strong personal and professional relationships in their communities.

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 a majority of our loans being made to businesses headquartered or with operations in Texas. At the same time our national lines of business continue to provide specialized lending products to businesses throughout the United States. We have benefitted from the success of our business model since inception, producing strong loan and deposit growth and favorable loss experience amidst a challenging environment for banking nationally.

## Growth History

We have grown substantially in both size and profitability since our formation. The table below sets forth data regarding the growth of key areas of our business from 2012 through 2016 (in thousands):

	December 31,				
	2016	2015	2014	2013	2012
Loans held for sale	\$968,929	\$ 86,075	\$ —	—\$	—\$ —
Loans held for investment, mortgage finance	4,497,338	4,966,276	4,102,125	2,784,265	3,175,272
Loans held for investment, net	13,001,011	11,745,674	10,154,887	8,486,603	6,785,837
Assets	21,697,134	18,903,821	15,900,034	11,717,174	10,537,853
Demand deposits	7,994,201	6,386,911	5,011,619	3,347,567	2,535,375
Total deposits	17,016,831	15,084,619	12,673,300	9,257,379	7,440,804
Stockholders’ equity	2,009,557	1,623,533	1,484,190	1,096,350	836,242

The following table provides information about the growth of our loans held for investment (“LHI”) portfolio by type of loan from 2012 through 2016 (in thousands):

	December 31,				
	2016	2015	2014	2013	2012
Commercial	\$7,291,545	\$6,672,631	\$5,869,219	\$5,020,565	\$4,106,419
Total real estate	5,560,909	4,990,914	4,223,532	3,409,427	2,630,390
Construction	2,098,706	1,851,717	1,416,405	1,262,905	737,637
Real estate term	3,462,203	3,139,197	2,807,127	2,146,522	1,892,753
Mortgage finance	4,497,338	4,966,276	4,102,125	2,784,265	3,175,272
Equipment leases	185,529	113,996	99,495	93,160	69,470
Consumer	34,587	25,323	19,699	15,350	19,493

## Table of Contents

### The Texas Market

The Texas market for banking services is highly competitive. Texas' largest banking organizations are headquartered outside of Texas and are controlled by out-of-state organizations. We also compete with other providers of financial services, such as savings and loan associations, credit unions, consumer finance companies, securities firms, insurance companies, commercial finance and leasing companies, full service brokerage firms and discount brokerage firms. We believe that many middle market companies and successful professionals and entrepreneurs are interested in banking with a company headquartered in, and with decision-making authority based in, Texas and with established Texas bankers who have the expertise to act as trusted advisors to customers with regard to their banking needs.

Our banking centers in our target markets are served by experienced bankers with lending expertise in the specific industries found in their market areas and established community ties. We believe our Bank can offer customers more responsive and personalized service than our competitors. If we provide effective service to these customers, we believe we will be able to establish long-term relationships and provide multiple products to our customers, thereby enhancing our profitability.

### National Lines of Business

While the Texas market continues to be central to the growth and success of our company, we have developed several lines of business, including mortgage finance, mortgage correspondent aggregation, homebuilder finance, insurance premium finance, lender finance, public finance and asset-based lending, that offer specialized loan and deposit products to businesses, municipalities and governmental and tax-exempt entities regionally and throughout the country. We believe this helps us mitigate our geographic concentration risk in Texas. We seek opportunities to develop additional lines of business that leverage our capabilities and are consistent with our business strategy. We launched our mortgage correspondent aggregation ("MCA") business in 2015 and asset-based lending and public finance businesses in 2016.

### Business Strategy

Drawing on the business and community ties of our management and their banking experience, our strategy is to continue growing an independent bank that focuses primarily on middle market business customers and successful professionals and entrepreneurs in each of the five major metropolitan markets of Texas as well as our national lines of business. To achieve this, we seek to implement the following strategies:

- targeting middle market businesses and successful professionals and entrepreneurs;
- growing our loan and deposit base in our existing markets by hiring additional experienced bankers in our different lines of business;
- developing lines of business that leverage our strengths and complement our existing lines of business;
- continuing our emphasis on credit policy to maintain credit quality consistent with long-term objectives;
  - leveraging our existing infrastructure to support a larger volume of business;
- maintaining stringent internal approval processes for capital and operating expenditures;
- continuing our extensive use of outsourcing to provide cost-effective operational support and service levels consistent with large-bank operations; and
- extending our reach within our target markets and lines of business through service innovation and service excellence.

### Products and Services

We offer a variety of loan, deposit account and other financial products and services to our customers.

**Business Customers.** We offer a full range of products and services oriented to the needs of our business customers, including:

- commercial loans for general corporate purposes including financing for working capital, internal growth, acquisitions and financing for business insurance premiums;
- real estate term and construction loans;
- mortgage finance lending;
- mortgage correspondent aggregation;
- equipment leasing;
- medium- and long-term tax-exempt loans for municipalities and other governmental and tax-exempt entities;

treasury management services;  
wealth management and trust services; and  
letters of credit.

4

---

## Table of Contents

Individual Customers. We also provide complete banking services for our individual customers, including:

personal wealth management and trust services;

certificates of deposit;

interest-bearing and non-interest-bearing checking accounts with optional features such as Visa® debit/ATM cards and overdraft protection;

traditional money market and savings accounts;

loans, both secured and unsecured; and

Internet banking.

### Lending Activities

We target our lending to middle market businesses and successful professionals and entrepreneurs that meet our credit standards. The credit standards are set by our standing Credit Policy Committee with the assistance of our Bank's Chief Credit Officer, who is charged with ensuring that credit standards are met by loans in our portfolio. Our Credit Policy Committee is comprised of senior Bank officers including our Bank's Chief Executive Officer and President, our Texas President/Chief Lending Officer, our Bank's Chief Risk Officer and our Bank's Chief Credit Officer, and is subject to oversight by the Credit Risk Committee of the Company's board of directors. We believe we maintain an appropriately diversified loan portfolio. Credit policies and underwriting guidelines are tailored to address the unique risks associated with each industry represented in the portfolio.

Our credit standards for commercial borrowers reference numerous criteria with respect to the borrower, including historical and projected financial information, strength of management, acceptable collateral and associated advance rates, and market conditions and trends in the borrower's industry. In addition, prospective loans are also analyzed based on current industry concentrations in our loan portfolio to prevent an unacceptable concentration of loans in any particular industry. We believe our credit standards are consistent with achieving our business objectives in the markets we serve and are an important part of our risk mitigation. We believe that our Bank is differentiated from its competitors by its focus on and targeted marketing to our core customers and by its ability to fit its products to the individual needs of our customers.

We generally extend variable rate loans in which the interest rate fluctuates with a specified reference rate such as the United States prime rate or the London Interbank Offered Rate (LIBOR) and frequently provide for a minimum floor rate. Our use of variable rate loans is designed to protect us from risks associated with interest rate fluctuations since the rates of interest earned will automatically reflect such fluctuations.

### Deposit Products

We offer a variety of deposit products and services to our core customers upon terms, including interest rates, which are competitive with other banks. Our business deposit products include commercial checking accounts, lockbox accounts, cash concentration accounts and other treasury management services, including on-line data and server access. Our treasury management on-line system offers information services, wire transfer initiation, ACH initiation, account transfer and service integration. Our consumer deposit products include checking accounts, savings accounts, money market accounts and certificates of deposit. We also allow our consumer deposit customers to access their accounts, transfer funds, pay bills and perform other account functions over the Internet and through ATM machines.

### Wealth Management and Trust

Our wealth management and trust services include investment management, personal trust and estate services, custodial services, retirement accounts and related services. Our investment management professionals work with our clients to define objectives, goals and strategies for their investment portfolios. We assist the customer with the selection of an investment manager and work with the client to tailor the investment program accordingly. We also offer retirement products such as individual retirement accounts and administrative services for retirement vehicles such as pension and profit sharing plans.

### Employees

As of December 31, 2016, we had 1,442 full-time employees. None of our employees is represented by a collective bargaining agreement and we consider our relations with our employees to be good.

### Regulation and Supervision

General. We and our Bank are subject to extensive federal and state laws and regulations that impose specific requirements on us and provide regulatory oversight of virtually all aspects of our operations. These laws and regulations generally are intended for the protection of depositors, the deposit insurance fund of the Federal Deposit Insurance Corporation (“FDIC”) and the stability of the U.S. banking system as a whole, rather than for the protection of our stockholders and creditors.

5

---



## Table of Contents

The following discussion summarizes certain laws and regulations to which we and our Bank are subject. It does not address all applicable laws and regulations that affect us currently or might affect us in the future. This discussion is qualified in its entirety by reference to the full texts of the laws, regulations and policies described.

The Company's activities are governed by the Bank Holding Company Act of 1956, as amended ("BHCA"). We are subject to regulation, supervision and examination by the Board of Governors of the Federal Reserve System (the "Federal Reserve") pursuant to the BHCA. We file quarterly reports and other information with the Federal Reserve. We file reports with the Securities and Exchange Commission ("SEC") and are subject to its regulation with respect to our securities, reporting and certain governance matters, including matters submitted for stockholder approval. Our securities are listed on the Nasdaq Global Select Market, and we are subject to Nasdaq rules for listed companies. Our Bank is organized as a national banking association under the National Bank Act, and is subject to regulation, supervision and examination by the Office of the Comptroller of the Currency (the "OCC"), the FDIC and the Consumer Financial Protection Bureau ("CFPB") as well as being subject to regulation by certain other federal and state agencies. The OCC has primary supervisory responsibility for our Bank and performs a continuous program of examinations concerning safety and soundness, the quality of management and directors, information technology and compliance with applicable laws and regulations. Our Bank files quarterly reports of condition and income with the FDIC, which provides insurance for certain of our Bank's deposits. The CFPB has regulation, supervision and examination authority over our Bank with respect to substantially all federal statutes protecting the interests of consumers of financial services.

**Bank Holding Company Regulation.** The BHCA limits our business to banking, managing or controlling banks and other activities that the Federal Reserve has determined to be closely related to banking. We have elected to register with the Federal Reserve as a financial holding company. This authorizes us to engage in any activity that is either (i) financial in nature or incidental to such financial activity, as determined by the Federal Reserve, or (ii) complementary to a financial activity, so long as the activity does not pose a substantial risk to the safety and soundness of our Bank or the financial system generally, as determined by the Federal Reserve. Examples of non-banking activities that are financial in nature include securities underwriting and dealing, insurance underwriting and making merchant banking investments.

We are not at this time exercising this authority at the parent company level. We, through our Bank, engage in traditional banking activities that are deemed financial in nature. In order for us to undertake new activities permitted by the BHCA, we and our Bank must be considered "well capitalized" (as defined below) and well managed, our Bank must have received a rating of at least satisfactory in its most recent examination under the Community Reinvestment Act and we would be required to notify the Federal Reserve within thirty days of engaging in the new activity.

Under Federal Reserve policy, now codified by the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"), we are expected to act as a source of financial and managerial strength to our Bank and commit resources to its support. Such support may be required at times when, absent this Federal Reserve policy, a holding company may not be inclined to provide it. We could in certain circumstances be required to guarantee the capital plan of our Bank if it became undercapitalized.

It is the policy of the Federal Reserve that financial holding companies may pay cash dividends on common stock only out of income available over the past year and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. The policy provides that financial holding companies may not pay cash dividends in an amount that would undermine the holding company's ability to serve as a source of strength to its banking subsidiary.

With certain limited exceptions, the BHCA prohibits a person or company or a group of persons deemed to be "acting in concert" from, directly or indirectly, acquiring more than 10% (5% if the acquirer is a bank holding company) of any class of our voting stock or obtaining the ability to control in any manner the election of a majority of our directors or otherwise direct the management or policies of our company without prior notice or application to and the approval of the Federal Reserve.

If, in the opinion of the applicable federal bank regulatory authorities, a depository institution or holding company is engaged in or is about to engage in an unsafe or unsound practice (which could include the payment of dividends),

such authority may require, generally after notice and hearing, that such institution or holding company cease and desist such practice. The federal banking agencies have indicated that paying dividends that deplete a depository institution's or holding company's capital base to an inadequate level would be such an unsafe or unsound banking practice. Moreover, the Federal Reserve and the FDIC have issued policy statements providing that financial holding companies and insured depository institutions generally should only pay dividends out of current operating earnings. Regulation of Our Bank by the OCC. National banks the size of our Bank are subject to continuous regulation, supervision and examination by the OCC. The OCC regulates or monitors all areas of a national bank's operations, including security devices and procedures, adequacy of capitalization and loss reserves, accounting treatment and impact on capital determinations, loans, investments, borrowings, deposits, liquidity, mergers, issuances of securities, payment of dividends, interest rate risk management, establishment of branches, corporate reorganizations, maintenance of books and records, and adequacy of staff training to carry on safe and sound lending and deposit gathering practices. The OCC requires national banks

6

---

## Table of Contents

to maintain specified capital ratios and imposes limitations on their aggregate investment in real estate, bank premises and furniture and fixtures. National banks are required by the OCC to file quarterly reports of their financial condition and results of operations and to obtain an annual audit of their financial statements in compliance with minimum standards and procedures prescribed by the OCC.

**Capital Adequacy Requirements.** Federal banking regulators have adopted a system using risk-based capital guidelines to evaluate the capital adequacy of banks and bank holding companies that is based upon the 1988 capital accord of the Bank for International Settlements' Committee on Banking Supervision (the "Basel Committee"), a committee of central banks and bank regulators from the major industrialized countries that coordinates international standards for bank regulation. Under the guidelines, specific categories of assets and off-balance-sheet activities such as letters of credit are assigned risk weights, based generally on the perceived credit or other risks associated with the asset. Off-balance-sheet activities are assigned a credit conversion factor based on the perceived likelihood that they will become on-balance-sheet assets. These risk weights are multiplied by corresponding asset balances to determine a "risk weighted" asset base which is then measured against various measures of capital to produce capital ratios. An organization's capital is classified in one of two tiers, Core Capital, or Tier 1, and Supplementary Capital, or Tier 2. Tier 1 capital includes common stock, retained earnings, qualifying non-cumulative perpetual preferred stock, minority interests in the equity of consolidated subsidiaries, a limited amount of qualifying trust preferred securities and qualifying cumulative perpetual preferred stock at the holding company level, less goodwill and most intangible assets. Tier 2 capital includes perpetual preferred stock and trust preferred securities not meeting the Tier 1 definition, mandatory convertible debt securities, subordinated debt, and allowances for loan and lease losses. Each category is subject to a number of regulatory definitional and qualifying requirements.

The Basel Committee in 2010 released a set of recommendations for strengthening international capital and liquidity regulation of banking organizations, known as Basel III. 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 became effective for us on January 1, 2015, with certain transition provisions phasing in over a period ending on January 1, 2019.

The Basel III Capital Rules, among other things, (i) specify a capital measure called "Common Equity Tier 1" ("CET1"), (ii) specify that Tier 1 capital consists of CET1 and "Additional Tier 1 capital" instruments meeting specified requirements, (iii) require that most deductions/adjustments to regulatory capital measures be made to CET1 and not to the other components of capital and (iv) define the scope of the deductions/adjustments to the capital measures. Our Series A 6.5% Non-Cumulative Perpetual Preferred Stock constitutes Additional Tier 1 capital and our subordinated notes constitute Tier 2 capital.

The Basel III Capital Rules set risk-based capital requirements and the total risk-based requirements to a minimum of 6.0% and 8.0%, respectively, plus a capital conservation buffer of 2.5% producing targeted ratios of 8.5% and 10.5%, respectively. The leverage ratio requirement under the Basel III Capital Rules is 5.0%. In order to be well capitalized under the rules now in effect, our Bank must maintain a CET1 capital ratio, Tier 1 capital ratio and total capital ratio that is equal to or greater than 6.5%, 8.0% and 10.0%, respectively. See "Selected Financial Data - Capital and Liquidity Ratios."

Additionally, the Basel III Capital Rules specify a capital conservation buffer with respect to each of the CET1, Tier 1 and total capital to risk-weighted assets ratios, which provides for capital levels that exceed the minimum risk-based capital adequacy requirements. The capital conservation buffer is subject to a three year phase-in period that began on January 1, 2016 and will be fully phased-in on January 1, 2019 at 2.5%. The required phase-in capital conservation buffer during 2016 was 0.625%. A financial institution with a conservation buffer of less than the required amount is subject to limitations on capital distributions, including dividend payments and stock repurchases, and certain discretionary bonus payments to executive officers.

We met the capital adequacy requirements under the Basel III Capital Rules on a fully phased-in basis when we commenced filing 2015 reports with the FDIC and OCC. At December 31, 2016 our Bank's CET1 ratio was 8.45% and its total risk-based capital ratio was 11.19% and, as a result, it is currently classified as "well capitalized" for purposes of the OCC's prompt corrective action regulations.

Because we had less than \$15 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. We have elected to exclude the effects of accumulated other comprehensive income items included in stockholders' equity from the determination of capital ratios under the Basel III Capital Rules.

Regulators may change capital and liquidity requirements, including previous interpretations of practices related to risk weights, which could require an increase to the allocation of capital to assets held by our Bank. Regulators could also require us to make retroactive adjustments to financial statements to reflect such changes. A regulatory capital ratio or category may not constitute an accurate representation of the Bank's overall financial condition or prospects. Our regulatory capital status is addressed in more detail under the heading "Liquidity and Capital Resources" within Management's Discussion and Analysis of Financial Condition and Results of Operations and in Note 14 - Regulatory Restrictions in the accompanying notes to the consolidated financial statements included elsewhere in this report.

Table of Contents

The Federal Deposit Insurance Corporation Improvement Act of 1991 (“FDICIA”) sets forth five capital categories for insured depository institutions under the prompt corrective action regulations:

Well capitalized—equals or exceeds a 10% total risk-based capital ratio, 8% Tier 1 risk-based capital ratio, and 5% leverage ratio and is not subject to any written agreement, order or directive requiring it to maintain a specific level for any capital measure;

Adequately capitalized—equals or exceeds an 8% total risk-based capital ratio, 6% Tier 1 risk-based capital ratio, and 4% leverage ratio;

Undercapitalized—total risk-based capital ratio of less than 8%, or a Tier 1 risk-based ratio of less than 6%, or a leverage ratio of less than 4%;

Significantly undercapitalized—total risk-based capital ratio of less than 6%, or a Tier 1 risk-based capital ratio of less than 4%, or a leverage ratio of less than 3%; and

Critically undercapitalized—a ratio of tangible equity to total assets equal to or less than 2%.

Federal bank regulatory agencies are required to implement arrangements for “prompt corrective action” for institutions failing to meet minimum requirements to be at least adequately capitalized. FDICIA imposes an increasingly stringent array of restrictions, requirements and prohibitions as an organization’s capital levels deteriorate. An adequately capitalized institution may not accept or roll over brokered deposits without an FDIC waiver. A significantly undercapitalized institution is subject to mandated capital raising activities, restrictions on interest rates paid and transactions with affiliates, removal of management and other restrictions. The OCC has only very limited discretion in dealing with a critically undercapitalized institution and is virtually required to appoint a receiver or conservator (the FDIC) if the capital deficiency is not corrected promptly.

Under the Federal Deposit Insurance Act (“FDIA”), “critically undercapitalized” banks may not, beginning 60 days after becoming critically undercapitalized, make any payment of principal or interest on their subordinated debt (subject to certain limited exceptions). In addition, under Section 18(i) of the FDIA, banks are required to obtain the advance consent of the FDIC to retire any part of their subordinated notes. Under the FDIA, a bank may not pay interest on its subordinated notes if such interest is required to be paid only out of net profits, or distribute any of its capital assets, while it remains in default on any assessment due to the FDIC.

Federal bank regulators may set capital requirements for a particular banking organization that are higher than the minimum ratios when circumstances warrant. Federal Reserve and OCC guidelines provide that banking organizations experiencing significant growth or making acquisitions will be expected to maintain strong capital positions substantially above the minimum supervisory levels, without significant reliance on intangible assets. Concentration of credit risks arising from non-traditional activities, as well as an institution’s ability to manage these risks, are important factors taken into account by regulatory agencies in assessing an organization’s overall capital adequacy. The OCC and the Federal Reserve also use a leverage ratio as an additional tool to evaluate the capital adequacy of banking organizations. The leverage ratio is a company’s Tier 1 capital divided by its average total consolidated assets. A minimum leverage ratio of 3.0% is required for banks and bank holding companies that either have the highest supervisory rating or have implemented the appropriate federal regulatory authority’s risk-adjusted measure for market risk. All other banks and bank holding companies are required to maintain a minimum leverage ratio of 4.0%, unless a different minimum is specified by an appropriate regulatory authority. In order to be considered well capitalized the leverage ratio must be at least 5.0%.

Our Bank’s leverage ratio was 8.42% at December 31, 2016 and, as a result, it is currently classified as “well capitalized” for purposes of the OCC’s prompt corrective action regulations.

The risk-based and leverage capital ratios established by federal banking regulators are minimum supervisory ratios generally applicable to banking organizations that meet specified criteria, assuming that they otherwise have received the highest regulatory ratings in their most recent examinations. Banking organizations not meeting these criteria are expected to operate with capital positions in excess of the minimum ratios. Regulators can, from time to time, change their policies or interpretations of banking practices to require changes in risk weights, which may require the Bank to obtain additional capital to support future growth or reduce asset balances in order to meet minimum acceptable capital ratios.

Liquidity Requirements. U.S. bank regulators in September 2014 issued a final rule implementing the Basel III liquidity framework for certain U.S. banks - generally those having more than \$50 billion of assets or whose primary federal banking regulator determines compliance with the liquidity framework is appropriate based on the organization's size, level of complexity, risk profile, scope of operations, U.S. or non-U.S. affiliations or risk to the financial system. One of the liquidity tests included in the new rule, referred to as the liquidity coverage ratio ("LCR"), is designed to ensure that a banking entity maintains an adequate level of unencumbered high-quality liquid assets equal to the entity's expected net cash outflow for a 30-day time horizon (or, if greater, 25% of its expected total cash outflow) under an acute liquidity stress scenario.

## Table of Contents

The other test, referred to as the net stable funding ratio (“NSFR”), is designed to promote more medium- and long-term funding of the assets and activities of banking entities over a one-year time horizon. These requirements are predicted to encourage the covered banking entities to increase their holdings of U.S. Treasury securities and other sovereign debt as a component of assets, and also to increase the use of long-term debt as a funding source. Regulators may change capital and liquidity requirements, including previous interpretations of practices related to risk weights, which could require an increase to the allocation of capital to assets held by our Bank. Regulators could also require us to make retroactive adjustments to financial statements and reported capital ratios to reflect such changes.

**Stress Testing.** Pursuant to the Dodd-Frank Act and regulations published by the Federal Reserve and OCC, institutions with average total consolidated assets greater than \$10 billion are required to conduct an annual “stress test” of capital and consolidated earnings and losses under a base case and two severely adverse stress scenarios provided by bank regulatory agencies. We became subject to this requirement in 2014 and have developed dedicated staffing, economic models, policies and procedures to implement stress testing on an annual basis using scenarios released by the agencies each year.

Commencing in 2016 the results of our stress testing must be reported to the agencies in July of each year and public disclosure of our summary stress test results is required to be made in October of each year. The published results of our stress testing are available in the Investor Relations section of our website at [www.texascapitalbank.com](http://www.texascapitalbank.com) under the caption “Financial Information.” Results of stress test calculations are anticipated to become an important factor considered by banking regulators in evaluating a range of banking practices. We are incorporating the economic models and information developed through our stress testing program into our risk management and business planning activities.

**Gramm-Leach-Bliley Financial Modernization Act of 1999 (“Gramm-Leach-Bliley Act”).** The Gramm-Leach-Bliley Act:

- allows bank holding companies meeting management, capital and Community Reinvestment Act standards to engage in a substantially broader range of non-banking activities than was permissible prior to enactment, including insurance underwriting and making merchant banking investments in commercial and financial companies;
- allows insurers and other financial services companies to acquire banks;
- removes various restrictions that applied to bank holding company ownership of securities firms and mutual fund advisory companies; and
- establishes the overall regulatory structure applicable to bank holding companies that also engage in insurance and securities operations.

The Gramm-Leach-Bliley Act also modifies other current financial laws, including laws related to financial privacy. The financial privacy provisions generally prohibit financial institutions, including us, from disclosing non-public personal financial information to non-affiliated third parties unless customers have the opportunity to “opt out” of the disclosure.

**Community Reinvestment Act.** The Community Reinvestment Act of 1977 (“CRA”) requires depository institutions to assist in meeting the credit needs of their market areas consistent with safe and sound banking practice. Under the CRA, each depository institution is required to help meet the credit needs of its market areas by, among other things, providing credit to low- and moderate-income individuals and communities. Depository institutions are periodically examined for compliance with the CRA and are assigned ratings. In order for a financial holding company to commence new activity permitted by the BHCA, each insured depository institution subsidiary of the financial holding company must have received a rating of at least “satisfactory” in its most recent examination under the CRA. The USA Patriot Act, the International Money Laundering Abatement and Financial Anti-Terrorism Act and the Bank Secrecy Act. A major focus of U.S. government policy regarding financial institutions in recent years has been combating money laundering, terrorist financing and other illegal payments. The USA Patriot Act of 2001 and the International Money Laundering Abatement and Financial Anti-Terrorism Act of 2001 substantially broadened the scope of United States anti-money laundering laws and penalties, specifically related to the Bank Secrecy Act of 1970, and expanded the extra-territorial jurisdiction of the U.S. government in this area. Regulations issued under these laws impose obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing and to verify the identity of their customers. Failure of a financial

institution to maintain and implement adequate programs to combat money laundering and terrorist financing, or to comply with relevant laws or regulations, could have serious legal, reputational and financial consequences for the institution. Because of the significance of regulatory emphasis on these requirements, we will continue to expend significant staffing, technology and financial resources to maintain programs designed to ensure compliance with applicable laws and regulations and an effective audit function for testing our compliance with the Bank Secrecy Act on an ongoing basis.

**Safe and Sound Banking Practices; Enforcement.** Banks and bank holding companies are prohibited from engaging in unsafe and unsound banking practices. Bank regulators have broad authority to prohibit and penalize activities of bank holding companies and their subsidiaries which represent unsafe and unsound banking practices or which constitute violations of laws,



Table of Contents

regulations or written directives of or agreements with regulators. Regulators have considerable discretion in identifying what they deem to be unsafe and unsound practices and in pursuing enforcement actions in response to them.

Enforcement actions against us, our Bank and our officers and directors may include the issuance of a written directive, the issuance of a cease-and-desist order that can be judicially enforced, the imposition of civil money penalties, the issuance of directives to increase capital, the issuance of formal and informal agreements, the issuance of removal and prohibition orders against institution-affiliated parties, the imposition of restrictions and sanctions under prompt corrective action provisions, the termination of deposit insurance (in the case of our Bank) and the appointment of a conservator or receiver for our Bank. Civil money penalties can be as high as \$1.0 million for each day a violation continues.

**Transactions with Affiliates and Insiders.** Our Bank is subject to Section 23A of the Federal Reserve Act which places limits on, among other covered transactions, the amount of loans or extensions of credit to affiliates that may be made by our Bank. Extensions of credit to affiliates must be adequately collateralized by specified amounts and types of collateral. Section 23A also limits the amount of loans or advances by our Bank to third party borrowers which are collateralized by our securities or obligations or those of our subsidiaries. Our Bank also is subject to Section 23B of the Federal Reserve Act, which, among other things, prohibits an institution from engaging in transactions with affiliates unless the transactions are on terms substantially the same, or at least as favorable to such institution or its subsidiaries, as those prevailing at the time for comparable transactions with non-affiliates.

We are subject to restrictions on extensions of credit to executive officers, directors, principal stockholders and their related interests. These restrictions are contained in the Federal Reserve Act and Federal Reserve Regulation O and apply to all insured institutions as well as their subsidiaries and holding companies. These restrictions include limits on loans to one borrower and conditions that must be met before such loans can be made. There is also an aggregate limitation on all loans to insiders and their related interests, which cannot exceed the institution's total unimpaired capital and surplus, unless the FDIC determines that a lesser amount is appropriate. Insiders are subject to enforcement actions for knowingly accepting loans in violation of applicable restrictions. Additional restrictions on transactions with affiliates and insiders are discussed in the Dodd-Frank Act section below.

**Restrictions on Dividends and Repurchases.** The sole source of funding of our parent company financial obligations has consisted of proceeds of capital markets transactions and cash payments from our Bank for debt service and dividend payments with respect to our Bank's preferred stock issued to the Company. We may in the future seek to rely upon receipt of dividends paid by our Bank to meet our financial obligations. Our Bank is subject to statutory dividend restrictions. Under such restrictions, national banks may not, without the prior approval of the OCC, declare dividends in excess of the sum of the current year's net profits plus the retained net profits from the prior two years, less any required transfers to surplus. The Basel III Capital Rules further limit the amount of dividends that may be paid by our Bank. In addition, under the FDICIA, our Bank may not pay any dividend if it is undercapitalized or if payment would cause it to become undercapitalized.

**Limits on Compensation.** The Federal Reserve, OCC and FDIC in 2010 issued comprehensive final guidance on incentive compensation policies for executive management of banks and bank holding companies. This guidance was intended to ensure that the incentive compensation policies of banking organizations do not undermine their safety and soundness by encouraging excessive risk-taking. The objective of the guidance is to assure that incentive compensation arrangements (i) provide incentives that do not encourage excessive risk-taking, (ii) are compatible with effective internal controls and risk management and (iii) are supported by strong corporate governance, including oversight by the board of directors.

**The Dodd-Frank Act.** The Dodd-Frank Act became law in 2010 and has had a broad impact on the financial services industry, imposing significant regulatory and compliance changes. A significant volume of financial services regulations required by the Dodd-Frank Act have not yet been finalized by banking regulators, Congress continues to consider legislation that would make significant changes to the law and courts are addressing significant litigation arising under the Act, making it difficult to predict the ultimate effect of the Dodd-Frank Act on our business. The following discussion provides a brief summary of certain provisions of the Dodd-Frank Act that may have an effect on us.

The Dodd-Frank Act significantly reduces the ability of national banks to rely upon federal preemption of state consumer financial laws. Although the OCC, as the primary regulator of national banks, has the ability to make preemption determinations where certain conditions are met, the broad rollback of federal preemption has the potential to create a patchwork of federal and state compliance obligations and enforcement. This could, in turn, result in significant new regulatory requirements applicable to us and certain of our lending activities, with potentially significant changes in our operations and increases in our compliance costs.

The Dodd-Frank Act made permanent the general \$250,000 deposit insurance limit for insured deposits. Amendments to the FDIA also revised the assessment base against which an insured depository institution's deposit insurance premiums paid to the FDIC's deposit insurance fund ("DIF") are calculated. The assessment base now consists of average consolidated total assets less average tangible equity. Additionally, the Dodd-Frank Act made changes to the minimum designated reserve ratio of the DIF, increasing the minimum from 1.15% to 1.35% of the estimated amount of total insured deposits, and eliminating the

## Table of Contents

requirement that the FDIC pay dividends to depository institutions when the reserve ratio exceeds certain thresholds. These changes contributed to an increase in the FDIC deposit insurance premiums paid by us in 2015 and 2016 and may contribute to increasing and less predictable deposit insurance expense in future years.

The Dodd-Frank Act generally enhances the restrictions on transactions with affiliates under Sections 23A and 23B of the Federal Reserve Act, including an expansion of the definition of “covered transactions” and an increase in the amount of time for which collateral requirements regarding covered credit transactions must be satisfied. Insider transaction limitations are expanded through the strengthening of restrictions on loans to insiders and the expansion of the types of transactions subject to the various limits, including derivatives transactions, repurchase agreements, reverse repurchase agreements and securities lending or borrowing transactions. Restrictions are also placed on certain asset sales to and from an insider to an institution, including requirements that such sales be on market terms and, in certain circumstances, approved by the institution’s board of directors.

The Dodd-Frank Act increases the risk of “secondary actor liability” for lenders such as our Bank that provide financing or other services to customers offering financial products or services to consumers. The Act can impose liability on a service provider for knowingly or recklessly providing substantial assistance to a customer found to have engaged in unfair, deceptive or abusive practices that injure a consumer. This exposure contributes to increased compliance and other costs in connection with administration of credit extended to entities engaged in activities covered by the Dodd-Frank Act.

The Dodd-Frank Act may impact the profitability of our business activities, require changes to certain of our business practices, impose upon us more stringent compliance, capital, liquidity and leverage requirements or otherwise adversely affect our business. These developments may also require us to invest significant management attention and resources to evaluate and make changes to our business as necessary to comply with new and changing statutory and regulatory requirements.

**The Volcker Rule.** The Dodd-Frank Act amended the BHCA to require the federal financial regulatory agencies to adopt rules that prohibit banks and their affiliates from engaging in proprietary trading in designated types of financial instruments and from investing in and sponsoring certain hedge funds and private equity funds. The final rule became effective in July 2015. It is highly complex, and many aspects of its application remain uncertain. We do not currently anticipate that the Volcker Rule will have a material effect on our operations since we do not engage in the businesses prohibited by the Volcker Rule. Unanticipated effects of the Volcker Rule’s provisions or future interpretations may have an adverse effect on our business or services provided to our Bank by other financial institutions.

### Available Information

Under the Securities Exchange Act of 1934, we are required to file annual, quarterly and current reports, proxy statements and other information with the Securities and Exchange Commission (“SEC”). You may read and copy any document filed by us with the SEC at the SEC’s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information about the public reference room. The SEC maintains a website at [www.sec.gov](http://www.sec.gov) that contains reports, proxy and information statements and other information regarding issuers that file electronically with the SEC. We file electronically with the SEC.

We make available, free of charge through our website, our reports on Forms 10-K, 10-Q and 8-K, and amendments to those reports, as soon as reasonably practicable after such reports are filed with or furnished to the SEC. Additionally, we have adopted and posted on our website a code of ethics that applies to our principal executive officer, principal financial officer and principal accounting officer. The address for our website is [www.texascapitalbank.com](http://www.texascapitalbank.com). Any amendments to, or waivers from, our code of ethics applicable to our executive officers will be posted on our website within four days of such amendment or waiver. We will provide a printed copy of any of the aforementioned documents to any requesting stockholder.

### ITEM 1A. RISK FACTORS

Our business is subject to risk. The following discussion, along with management’s discussion and analysis and our financial statements and footnotes, sets forth the most significant risks and uncertainties that we believe could adversely affect our business, financial condition or results of operations. Additional risks and uncertainties that management is not aware of or that management currently deems immaterial may also have a material adverse effect

on our business, financial condition or results of operations. There is no assurance that this discussion covers all potential risks that we face. The occurrence of the described risks could cause our results to differ materially from those described in our forward-looking statements included elsewhere in this report or in our other filings with the SEC and could have a material adverse impact on our business or results of operations.

11

---

## Table of Contents

### Risk Factors Associated With Our Business

We must effectively manage our credit risk. The risk of non-payment of loans is inherent in commercial banking. Increased credit risk may result from many factors, including:

- Adverse changes in local, U.S. and global economic and industry conditions;
- Declines in the value of collateral, including asset values that are directly or indirectly related to external factors such as commodity prices, real estate values or interest rates;
- Concentrations of credit associated with specific loan categories, industries or collateral types; and
- Risks specific to individual borrowers.

We rely heavily on information provided by third parties when originating and monitoring loans. If this information is intentionally or negligently misrepresented and we do not detect such misrepresentations, the credit risk associated with the transaction may be increased. Although we attempt to manage our credit risk by carefully monitoring the concentration of our loans within specific loan categories and industries and through prudent loan approval and monitoring practices in all categories of our lending, we cannot assure you that our approval and monitoring procedures will reduce these lending risks. Our significant number of large credit relationships (above \$10 million) could exacerbate credit problems precipitated by a regional or national economic downturn. Competitive pressures could erode underwriting standards leading to a decline in general credit quality and increases in credit defaults and non-performing asset levels. If our credit administration personnel, policies and procedures are not able to adequately adapt to changes in economic, competitive or other conditions that affect customers and the quality of the loan portfolio, we may incur increased losses that could adversely affect our financial results and lead to increased regulatory scrutiny, restrictions on our lending activity or financial penalties.

A significant portion of our assets consists of commercial loans. We generally invest a greater proportion of our assets in commercial loans to business customers than other banking institutions of our size, and our business plan calls for continued efforts to increase our assets invested in these loans. At December 31, 2016, approximately 41% of our LHI portfolio was comprised of commercial loans. Commercial loans may involve a higher degree of credit risk than other types of loans due, in part, to their larger average size, the effects of changing economic conditions on the businesses of our commercial loan customers, the dependence of borrowers on operating cash flow to service debt and our reliance upon collateral which may not be readily marketable. Due to the greater proportion of these commercial loans in our portfolio and because the balances of these loans are, on average, larger than other categories of loans, losses incurred on a relatively small number of commercial loans could have a materially adverse impact on our results of operations and financial condition.

A significant portion of our loans are secured by commercial and residential real estate. At December 31, 2016, approximately 30% of our loan portfolio was comprised of loans with real estate as the primary component of collateral. Our real estate lending activities, and our exposure to fluctuations in real estate collateral values, are significant and expected to increase as our assets increase. The market value of real estate can fluctuate significantly in a relatively short period of time as a result of market conditions in the geographic area in which the real estate is located, in response to factors such as changes in the economic health of industries heavily concentrated in a particular area and in response to changes in market interest rates, which influence capitalization rates used to value revenue-generating commercial real estate. If the value of real estate serving as collateral for our loans declines materially, a significant part of our loan portfolio could become under-collateralized and losses incurred upon borrower defaults would increase. Conditions in certain segments of the real estate industry, including homebuilding, lot development and mortgage lending, may have an effect on values of real estate pledged as collateral for our loans. The inability of purchasers of real estate, including residential real estate, to obtain financing may weaken the financial condition of our borrowers who are dependent on the sale or refinancing of property to repay their loans. Changes in the economic health of certain industries can have a significant impact on other sectors or industries which are directly or indirectly associated with those industries, and may impact the value of real estate in areas where such industries are concentrated.

Our future profitability depends, to a significant extent, upon our middle market business customers. Our future profitability depends, to a significant extent, upon revenue we receive from middle market business customers, and their ability to continue to meet their loan obligations. Adverse economic conditions or other factors affecting this

market segment, and our failure to timely identify and react to unexpected economic downturns, may have a greater adverse effect on us than on other financial institutions that have a more diversified customer base. Additionally, our inability to grow our middle market business customer base in a highly competitive market could affect our future growth and profitability.

We must maintain an appropriate allowance for loan losses. Our experience in the banking industry indicates that some portion of our loans will become delinquent, and some may only be partially repaid or may never be repaid at all. We maintain an allowance for loan losses, which is a reserve established through a provision for loan losses charged to expense each quarter, that is consistent with management's assessment of the collectability of the loan portfolio in light of the amount of loans committed and outstanding and current economic conditions and market trends. When specific loan losses are identified, the amount of the expected loss is removed, or charged-off, from the allowance. Our methodology for establishing the

Table of Contents

appropriateness of the allowance for loan losses depends on our subjective application of risk grades as indicators of each borrower's ability to repay specific loans, together with our assessment of how actual or projected changes in competitor underwriting practices, competition for borrowers and depositors and other conditions in our markets are likely to impact improvement or deterioration in the collectability of our loans as compared to our historical experience.

Our business model makes our Bank more vulnerable to changes in underlying business credit quality than other banks with which we compete. We have a substantially larger percentage of commercial, real estate and other categories of business loans relative to total assets than most other banks in our market and our individual loans are generally larger as a percentage of our total earning assets than other banks. While we have substantially increased our liquidity over the past three years, these funds are invested in low-yielding deposits with federal agencies and other financial institutions. A substantially smaller portion of our assets consists of securities and other earning asset categories that can be less vulnerable to changes in local, regional or industry-specific economic trends, causing our potential for credit losses to be more severe than other banks. Our business model has focused on growth in various loan categories that can be more sensitive to changes in economic trends. We believe our ability to maintain above-peer rates of growth in commercial loans is dependent on maintaining above-peer credit quality metrics. The failure to do so would have a material adverse impact on our growth and profitability.

If our assessment of inherent losses is inaccurate, or economic and market conditions or our borrowers' financial performance experience material unanticipated changes, the allowance may become inadequate, requiring larger provisions for loan losses that can materially decrease our earnings. Certain of our loans individually represent a significant percentage of our total allowance for loan losses. Adverse collection experience in a relatively small number of these loans could require an increase in the provision for loan losses. Federal regulators periodically review our allowance for loan losses and, based on their judgments, which may be different than ours, may require us to change classifications or grades of loans, increase the allowance for loan losses or recognize further loan charge-offs. Any increase in the allowance for loan losses or in the amount of loan charge-offs required by these regulatory agencies could have a negative effect on our results of operations and financial condition.

Our business is concentrated in Texas; our Energy industry exposure could adversely affect our performance. A majority of our customers are located in Texas. As a result, our financial condition and results of operations may be strongly affected by any prolonged period of economic recession or other adverse business, economic or regulatory conditions affecting Texas businesses and financial institutions. Although more than 50% of our loan exposure is outside of Texas and more than 50% of our deposits are sourced outside of Texas, our Texas concentration remains significant compared to other peer banks. While the Texas economy is more diversified than in the 1980's, the energy sector continues to play an important role. At December 31, 2016 our outstanding energy loans represented 5% of total loans. Our energy loans consist primarily of producing reserve-based loans to exploration and production companies with a smaller portion of our loan balances attributable to royalty owners, midstream operators, saltwater disposal and other service companies whose businesses primarily relate to production, not exploration and development, of oil and gas. These businesses have been significantly affected by volatility in oil and natural gas prices and material declines in the level of drilling and production activity in Texas and in other areas of the United States. Adverse developments in the energy sector have had and may continue to have significant spillover effects on the Texas economy, including adverse effects on commercial and residential real estate values and the general level of economic activity. We have been carefully monitoring the impact of the continuing significant decline and volatility in oil and natural gas prices on our loan portfolio since late 2014, and have reflected these events in the determination of our allowance for loan and lease losses. We experienced an increase in non-performing assets and higher charge-offs primarily related to energy loans during 2016, and there is no assurance that we will not be materially adversely impacted by the direct and indirect effects of current and future conditions in the energy industry in Texas and nationally.

Our growth plans are dependent on the availability of capital and funding. Our historical ability to raise capital through the sale of capital stock and debt securities may be affected by economic and market conditions or regulatory changes that are beyond our control. Adverse changes in our operating performance or financial condition could make raising additional capital difficult or more expensive or limit our access to customary sources of funding, including

inter-bank borrowings, repurchase agreements and borrowings from the Federal Reserve Bank or the Federal Home Loan Bank. Unexpected changes in requirements for regulatory capital resulting from regulatory actions or the results of our Dodd-Frank Act stress testing could require us to raise capital at a time, and at a price, that might be unfavorable, or could require that we forego continuing growth or reduce our current loan portfolio. We cannot offer assurance that capital and funding will be available to us in the future, in needed amounts, upon acceptable terms or at all. Our efforts to raise capital could require the issuance of securities at times and with maturities, conditions and rates that are disadvantageous, and which could have a dilutive impact on our current stockholders. Factors that could adversely affect our ability to raise additional capital include conditions in the capital markets, our financial performance, our credit ratings, regulatory actions and general economic conditions. Increases in our cost of capital, including dilution and increased interest or dividend requirements, could have a direct adverse impact on our operating performance and our ability to achieve our growth objectives. Trust preferred securities are no longer viable as a source of new long-term debt capital as a result of regulatory changes. The treatment of our existing trust preferred securities as capital may be subject to further regulatory change prior to their maturity, which could require the Company to seek additional capital.



Table of Contents

We must effectively manage our liquidity risk. Our Bank requires available funds (liquidity) to meet its deposit, debt and other obligations as they come due, borrower requests to draw on committed credit facilities as well as unexpected demands for cash payments. While we are not subject to Basel III liquidity regulations, the adequacy of our liquidity is a matter of regulatory interest given the significant portion of our balance sheet represented by loans as opposed to securities and other more marketable investments. Our Bank's principal source of funding consists of customer deposits. A substantial majority of our Bank's liabilities consist of demand, savings, interest checking and money market deposits, which are payable on demand or upon relatively short notice. By comparison, a substantial portion of our assets are loans, most of which, excluding our mortgage finance loans and mortgage loans held for sale, cannot be collected or sold in so short a time frame, creating the potential for an imbalance in the availability of liquid assets to satisfy depositors and loan funding requirements.

We hold smaller balances of marketable securities than many of our competitors, limiting our ability to increase our liquidity by completing market sales of these assets. An inability to raise funds through deposits, borrowings, the sale of securities and loans and other sources, including our access to capital market transactions, could have a substantial negative effect on our Bank's liquidity. We actively manage our available sources of funds to meet our expected needs under normal and financially stressed conditions, but there is no assurance that our Bank will be able to make new loans, meet ongoing funding commitments to borrowers and replace maturing deposits and advances as necessary under all possible circumstances. Our Bank's ability to obtain funding could be impaired by factors beyond its control, such as disruptions in financial markets, negative expectations regarding the financial services industry generally or in our markets or negative perceptions of our Bank, including our credit ratings.

Our mortgage finance business has experienced, and will likely continue to experience, highly variable usage of our funding capacity resulting from seasonal demands for credit, surges in consumer demand driven by changes in interest rates and month-end "spikes" of residential mortgage closings. These spikes could also result in our Bank having capital ratios that are below internally targeted levels or even levels that could cause our Bank to not be well capitalized and could affect liquidity levels. At the same time managing this risk by declining to respond fully to the needs of our customers could severely impact our business. We have responded to these variable funding demands by, among other things, increasing the extent of participations sold in our mortgage loan interests and by maintaining a substantial borrowing relationship with the Federal Home Loan Bank. Our mortgage finance customers have in recent periods provided significant low-cost deposit balances associated with the borrower escrow accounts created at the time certain mortgage loans are funded, which have benefitted our liquidity and net interest margin. In a rising rate environment or in response to competitive pressures, we may have to pay interest on some or all of these accounts as regulations allow. Individual escrow account balances also experience significant variability monthly as principal and interest payments, as well as ad valorem taxes and insurance premiums, are paid periodically. While the short average holding period of our mortgage interests of approximately 20 days will allow us, if necessitated by a funding shortfall, to rapidly decrease the size of the portfolio and its associated funding requirements, any such action might significantly damage business relationships important to that business.

Our Bank sources a significant volume of its demand deposits from financial services companies, mortgage finance customers and other commercial sources, resulting in a larger percentage of large deposits and a smaller number of sources of deposits than would be typical of other banks in our markets, creating concentrations of deposits that carry a greater risk of unexpected material withdrawals. In recent periods over half of our total deposits have been attributable to customers whose balances exceed the \$250,000 FDIC insurance limit. Many of these customers actively monitor our financial condition and results of operations and could withdraw their deposits quickly upon the occurrence of a material adverse development affecting our Bank or their businesses. Significant deterioration in our credit quality or a downgrade in our credit ratings could affect funding sources such as financial institutions and broker dealers, as well as our borrowing capacity at the Federal Home Loan Bank. In response to this risk we have substantially increased our liquidity over the past three years, but there is no assurance that we will maintain or have access to sufficient liquidity to fully mitigate this risk.

One potential source of liquidity for our Bank consists of "brokered deposits" arranged by brokers acting as intermediaries, typically larger money-center financial institutions. We receive deposits provided by certain of our customers in connection with our delivery of other financial services to them or their customers which are subject to

regulatory classification as “brokered deposits” even though we consider these to be relationship deposits and they are not subject to the typical risks or market pricing associated with conventional brokered deposits.

If we do not maintain our regulatory capital above the level required to be well capitalized we would be required to obtain FDIC consent for us to continue to accept deposits classified as brokered deposits, and there can be no assurance that the FDIC would consent under any circumstances. We could also be required to suspend or eliminate deposit gathering from any source classified as “brokered” deposits. The FDIC can change the definition of or extend the classification to deposits not currently classified as brokered deposits. These non-traditional deposits are subject to greater operational and reputational risk of unexpected withdrawal than traditional demand and time deposits, particularly those provided by consumers. A significant decrease in our balances of relationship brokered deposits could have a material adverse effect upon our financial condition and results of operations. See Management’s Discussion and Analysis of Financial Condition and Results of Operations below for further discussion of our liquidity.

Table of Contents

We must effectively manage our information systems risk. We rely heavily on our communications and information systems to conduct our business. The financial services industry is undergoing rapid technological changes with frequent introductions of new technology-driven products and services. Our ability to compete successfully depends in part upon our ability to use technology to provide products and services that will satisfy customer demands. Many of our larger competitors invest substantially greater resources in technological capabilities than we do. We may not be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to our customers, which may negatively affect our business, results of operations or financial condition.

Our communications and information systems remain vulnerable to unexpected disruptions, failures and cyber-attacks. The frequency and intensity of such attacks in our industry is escalating. Any failure or interruption of these systems could impair our ability to serve our customers and to operate our business and could damage our reputation, result in a loss of business, subject us to additional regulatory scrutiny or enforcement or expose us to civil litigation and possible financial liability. While we have developed extensive recovery plans, we cannot assure that those plans will be effective to prevent adverse effects upon us and our customers resulting from system failures. We collect and store sensitive data, including personally identifiable information of our customers and employees. Computer break-ins of our systems or our customers' systems, thefts of data and other breaches and criminal activity may result in significant costs to respond, liability for customer losses if we are at fault, damage to our customer relationships, regulatory scrutiny and enforcement and loss of future business opportunities due to reputational damage. Breaches can be perpetrated by unknown third parties, but could also be facilitated by employees either inadvertently or by consciously attempting to create disruption or certain acts of fraud. Although we, with the help of third-party service providers, will continue to implement security technology and establish operational procedures to protect sensitive data, there can be no assurance that these measures will be effective. We advise and provide training to our customers regarding protection of their systems, but there is no assurance that our advice and training will be appropriately acted upon by our customers or effective to prevent losses. In some cases we may elect to contribute to the cost of responding to cybercrime against our customers, even when we are not at fault, in order to maintain valuable customer relationships. Successful cyber-attacks on our Bank or customers may affect the reputation of our Bank, and failure to meet customer expectations could have a material impact on our ability to attract and retain deposits as a primary source of funding.

Our operations rely extensively on a broad range of external vendors. We rely on certain external vendors to provide products and services necessary to maintain our day-to-day operations, particularly in the areas of operations, treasury management systems, information technology and security. This reliance exposes us to the risk that these vendors will not perform as required by our agreements as well as risks resulting from disruptions in communications with our vendors, cyber-attacks and security breaches at our vendors, failure of a vendor to provide services for other reasons and poor performance of services. An external vendor's failure to perform in any of these areas could be disruptive to our operations, which could have a material adverse impact on our business, financial condition and results of operations, as well as cause reputation damage if our customers are affected by the failure. External vendors who must have access to our information systems in order to provide their services have been identified as significant sources of information technology security risk. While we have implemented an active program of oversight to address this risk, there can be no assurance that we will not experience material security breaches associated with our vendors.

We must effectively manage our interest rate risk. Our profitability is dependent to a large extent on our net interest income, which is the difference between the interest income paid to us on our loans and investments and the interest we pay to third parties such as our depositors, lenders and debtholders. Changes in interest rates can impact our profits and the fair values of certain of our assets and liabilities. Models that we use to forecast and plan for the impact of rising and falling interest rates may be incorrect or fail to consider the impact of competition and other conditions affecting our loans and deposits.

The banking industry has experienced a prolonged period of unusually low interest rates, which have had an adverse effect on our earnings by reducing yields on loans and other earning assets. The Federal Reserve began raising rates in late 2015 and their benchmark rate and market rates increased during 2016, contributing to some improvement in our net interest income. However there is substantial uncertainty regarding the extent to which interest rates may increase

in 2017 and future periods and what the future effects of any such increases will be. There is no assurance that recent expectations of increasing interest rates in future periods will be realized. Increases in market interest rates can have negative impacts on our business, including reducing our customers' desire to borrow money from us or adversely affecting their ability to repay their outstanding loans by increasing their debt service obligations through the periodic reset of adjustable interest rate loans. If our borrowers' ability to pay their loans is impaired by increasing interest payment obligations, our level of non-performing assets would increase, producing an adverse effect on operating results. Asset values, especially commercial real estate as collateral, securities or other fixed rate earning assets, can decline significantly with relatively minor changes in interest rates.

Increases in interest rates and economic conditions affecting consumer demand for housing can have a material impact on the volume of mortgage originations and refinancings, adversely affecting the profitability of our mortgage finance business. Interest rate risk can also result from mismatches between the dollar amounts of repricing or maturing assets and liabilities and

15

---

Table of Contents

from mismatches in the timing and rates at which our assets and liabilities reprice. We actively monitor and manage the balances of our maturing and repricing assets and liabilities to reduce the adverse impact of changes in interest rates, but there can be no assurance that we will be able to avoid material adverse effects on our net interest margin in all market conditions.

Federal prohibitions on the ability of financial institutions to pay interest on demand deposit accounts were repealed in 2011 by the Dodd-Frank Act. This change has had limited impact to date due to the excess of commercial liquidity and the low interest rate environment. Rising interest rates may result in our interest expense increasing, with a commensurate adverse effect on our net interest income, particularly if we must pay interest on demand deposits to attract or retain customer deposits. There can be no assurance that we will not be materially adversely affected in the future by increases in interest rates.

We are subject to extensive government regulation and supervision. We, as a bank holding company and financial holding company, and our Bank as a national bank, are subject to extensive federal and state regulation and supervision that impacts our business on a daily basis. See the discussion above at Business - Regulation and Supervision. These regulations affect our lending practices, permissible products and services and their terms and conditions, customer relationships, capital structure, investment practices, accounting, financial reporting, operations and our ability to grow, among other things. These regulations also impose obligations to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing and to verify the identities of our customers.

Congress and federal regulatory agencies continually review banking laws, regulations and policies for possible changes. Changes to statutes, regulations or regulatory policies, including changes in interpretation or implementation of statutes, regulations or policies, could affect us in substantial and unpredictable ways. Recent material changes in regulation and requirements imposed on financial institutions, such as the Dodd-Frank Act and the Basel III Accord, result in additional costs, impose more stringent capital, liquidity and leverage requirements, limit the types of financial services and products we may offer and increase the ability of non-bank financial services providers to offer competing financial services and products, among other things. Such changes could result in new regulatory obligations which could prove difficult, expensive or competitively impractical to comply with if not equally imposed upon non-bank financial services providers with whom we compete.

The Dodd-Frank Act has not yet been fully implemented and there are many additional regulations called for by the Act that have not been proposed, or if proposed, have not been adopted. The full impact of the Dodd-Frank Act on our business strategies is not completely known at this time as there is uncertainty related to regulations still pending. The 2016 national election results have introduced additional uncertainty into future implementation and enforcement of the Dodd-Frank Act and other financial sector regulatory requirements. While these developments have contributed to increased market valuations of a broad range of financial services companies, including the Company, there is no assurance that any of the anticipated changes will be implemented or that expected benefits to our future financial performance will be realized.

We receive inquiries from our regulators from time to time regarding, among other things, lending practices, reserve methodology, compliance with ever-changing regulations and interpretations, our management of interest rate, liquidity, capital and operational risk, enterprise risk management, regulatory and financial accounting practices and policies and related matters, which can divert management's time and attention from focusing on our business. We have significantly increased the amount of management time and expense devoted to developing the infrastructure to support our expanding compliance obligations, which can pose significant regulatory enforcement, financial and reputational risks if not appropriately addressed.

We are actively engaged in responding to stress testing requirements contained in the Dodd-Frank Act ("DFAST") to evaluate the adequacy of our capital and liquidity planning. Uncertainties regarding how the financial models of our business created pursuant to this requirement will respond to the regulatory scenarios issued annually, and how our regulators will evaluate our report of the results obtained, subject us to increased regulatory risk in 2017 and future years as the standards for DFAST and regulatory use of our reported data continue to evolve. Any change to our practices or policies requested or required by our regulators, or any changes in interpretation of regulatory policy applicable to our businesses, may have a material adverse effect on our business, results of operations or financial

condition. We have increased our capital and liquidity and expanded our regulatory compliance staffing and systems in recent years in order to address regulatory expectations for high-growth institutions, which reduced our net interest margin and earnings in those periods. There is no assurance that our financial performance in future years will not be similarly burdened.

We expend substantial effort and incur costs to maintain and improve our systems, controls, accounting, operations, information security, compliance, audit effectiveness, analytical capabilities, staffing and training in order to satisfy regulatory requirements. We cannot offer assurance that these efforts will be accepted by our regulators as satisfying the legal and regulatory requirements applicable to us. Failure to comply with relevant laws, regulations or policies could result in sanctions by regulatory agencies, civil money penalties and/or reputation damage, which could have a material adverse effect on our business, financial condition and results of operations. While we have policies and procedures designed to prevent any such violations, there can be no assurance that such violations will not occur.

Table of Contents

The FDIC has imposed higher general and special assessments on deposits or assets based on general industry conditions and as a result of changes in specific programs, as well as qualitative adjustments for individual institutions based on their risk characteristics that cannot be predicted with any certainty. There is no restriction on the amount by which the FDIC may increase deposit and asset assessments in the future. Increases in FDIC assessments, fees and taxes have adversely affected our earnings and may continue to do so in the future.

We must effectively execute our business strategy in order to continue our asset and earnings growth. Our core strategy is to develop our business principally through organic growth. Our prospects for continued growth must be considered in light of the risks, expenses and difficulties frequently encountered by companies seeking to realize significant growth. In order to execute our growth strategy successfully, we must, among other things:

- continue to identify and expand into suitable markets and lines of business, in Texas, regionally and nationally;
- develop new products and services and execute our full range of products and services more efficiently and effectively;
- attract and retain qualified bankers in each of our targeted markets to build our customer base;
- respond to market opportunities promptly and nimbly while balancing the demands of risk management and compliance with regulatory requirements;
- expand our loan portfolio in an intensely competitive environment while maintaining credit quality;
- attract sufficient deposits and capital to fund our anticipated loan growth and satisfy regulatory requirements;
- control expenses; and
- acquire and maintain sufficient qualified staffing and information technology and operational infrastructure to support growth and compliance with increasing and changing regulatory requirements.

Failure to effectively execute our business strategy could have a material adverse effect on our business, future prospects, financial condition or results of operations.

We must be effective in developing and executing new lines of business and new products and services while managing associated risks. Our business strategy requires that we develop and grow new lines of business and offer new products and services within existing lines of business in order to compete successfully and realize our growth objectives for both loans and deposits. Substantial costs, risks and uncertainties are associated with these efforts, particularly in instances where the markets are not fully developed. Developing and marketing new activities requires that we invest significant time and resources before revenues and profits can be realized. Timetables for the development and launch of new activities may not be achieved and price and profitability targets may not prove feasible. External factors, such as compliance with regulations, receipt of necessary licenses or permits, competitive alternatives and shifting market preferences, may also adversely impact the successful execution of new activities.

New activities necessarily entail additional risks and may present additional risks to the effectiveness of our system of internal controls. All service offerings, including current offerings and new activities, may become more risky due to changes in economic, competitive and market conditions beyond our control. Our regulators could determine that our risk management practices are not adequate or our capital levels are not sufficiently in excess of well-capitalized levels and take action to restrain our growth. Failure to successfully manage these risks, generally and to the satisfaction of our regulators, in the development and implementation of new lines of business or new products or services could have a material adverse effect on our business, results of operations and financial condition.

We must continue to attract, retain and develop key personnel. Our success depends to a significant extent upon our ability to attract, develop and retain experienced bankers in each of our markets as well as managers in operational areas, compliance and other support areas to build and maintain the infrastructure and controls required to support continuing loan and deposit growth. Competition for the best people in our industry can be intense, and there is no assurance that we will continue to have the same level of success in this effort that has supported our historical results. Factors that affect our ability to attract, develop and retain key employees include our compensation and benefits programs, our profitability, our ability to establish appropriate succession plans for key talent, our reputation for rewarding and promoting qualified employees and market competition for employees with certain skills, including information systems development and security. The cost of employee compensation is a significant portion of our operating expenses and can materially impact our results of operations. The unanticipated loss of the services of a small number of key personnel could have an adverse effect on our business. Although we have entered into

employment agreements with certain key employees, we cannot assure you that we will be successful in retaining them.

Our business faces unpredictable economic and business conditions. Our business is directly impacted by general economic and business conditions in Texas, the United States and abroad. The credit quality of our loan portfolio necessarily reflects, among other things, the general economic conditions in the areas in which we conduct our business. Our continued financial success can be affected by other factors that are beyond our control, including: national, regional and local economic conditions;

17

---



Table of Contents

the value of the U.S. Dollar in relation to the currencies of other advanced and emerging market countries;  
the performance of both domestic and international equity and debt markets and valuation of securities represented and traded on recognized domestic and international exchanges;  
fluctuations in the value of commodities including but not limited to petroleum and natural gas;  
general economic consequences of international conditions, such as weakness in European sovereign debt and foreign currencies and the impact of that weakness on the US and global economies;  
legislative and regulatory changes impacting our industry;  
the financial health of our customers and economic conditions affecting them and the value of our collateral, including effects from continued low prices of energy and other commodities;  
the incidence of fraud, illegal payments, security breaches and other illegal acts among or impacting our Bank and our customers;  
structural changes in the markets for origination, sale and servicing of residential mortgages;  
changes in governmental economic and regulatory policies generally, including the extent and timing of intervention in credit markets by the Federal Reserve Board or withdrawal from that intervention;  
changes in the availability of liquidity at a systemic level; and  
material inflation or deflation.

Substantial deterioration in any of the foregoing conditions can have a material adverse effect on our prospects and our results of operations and financial condition. There is no assurance that we will be able to sustain our historical rate of growth or our profitability. Our Bank's customer base is primarily commercial in nature, and our Bank does not have a significant retail branch network or retail consumer deposit base. In periods of economic downturn, business and commercial deposits may be more volatile than traditional retail consumer deposits. As a result, our financial condition and results of operations could be adversely affected to a greater degree by these uncertainties than our competitors who have a larger retail customer base.

We compete with many banks and other financial service providers. Competition among providers of financial services in our markets, in Texas, regionally and nationally, is intense. We compete with other financial and bank holding companies, state and national commercial banks, savings and loan associations, consumer finance companies, credit unions, securities brokerages, insurance companies, mortgage banking companies, money market mutual funds, asset-based non-bank lenders, government sponsored or subsidized lenders and other financial services providers. Many of these competitors have substantially greater financial resources, lending limits and technological resources and larger branch networks than we do, and are able to offer a broader range of products and services than we can, including systems and services that could protect customers from cyber threats. Many competitors offer lower interest rates and more liberal loan terms that appeal to borrowers but adversely affect net interest margin and assurance of repayment. We are increasingly faced with competition in many of our products and services by non-bank providers who may have competitive advantages of size, access to potential customers and fewer regulatory requirements. Failure to compete effectively for deposit, loan and other banking customers in our markets could cause us to lose market share, slow or reverse our growth rate or suffer adverse effects on our financial condition and results of operations.

Our mortgage correspondent aggregation business subjects us to additional risks. In the third quarter of 2015 we launched our mortgage correspondent aggregation business ("MCA"), a correspondent lending program that complements our mortgage warehouse lending business. Volatility in the mortgage industry has caused uncertainty related to the pricing of the mortgage loans that we seek to purchase, as well as uncertainty in the pricing of those loans when they are sold or securitized. This volatility may cause the actual returns on mortgage sales or securitization transactions to be less than anticipated, which could adversely affect our overall loans held for sale volumes. Additionally, non-bank competitors may have a pricing advantage as they are not subject to the same capital maintenance requirements relative to mortgage loans and mortgage servicing rights ("MSRs") as our Bank. Our MCA business subjects us to additional interest rate risk, which may have an adverse effect on our business. The persistent low interest rate environment and expectation of future higher rates has resulted in an increase in the value of MSRs, causing other market participants and competitors who are planning to hold MSRs for a longer term to be more aggressive in their pricing of the underlying loan purchases than a participant like our Bank that does not plan to

hold MSR's on a long-term basis. While we believe market and competitive conditions will improve, a prolonged low interest rate environment could adversely affect the economics of our MCA business over a longer period of time. Conversely, an environment of rising interest rates could have a significant effect on loan volumes in our MCA business if refinancing and home purchase activities are reduced.

We have entered into loan purchase commitments and forward sales commitments in connection with the MCA business. While we believe that our hedging strategies will be successful in mitigating our exposure to interest rate risk associated with the

Table of Contents

purchase of mortgage loans held for sale, no hedging strategy can completely protect us. Poorly designed strategies, improperly executed transactions, or inaccurate assumptions regarding future interest rates or market conditions could have a material adverse effect on our financial condition and results of operations.

We may be required to repurchase mortgage loans or reimburse investors as a result of breaches in contractual representations and warranties under the agreements pursuant to which we sell mortgage loans. While our agreements with the originators and sellers of mortgage loans provide us with legal recourse against them that may allow us to recover some or all of our losses, these companies are frequently not financially capable of paying large amounts of damages and as a result we can offer no assurance that we will not bear all of the risk of loss.

We may incur other costs and losses as a result of actual or alleged violations of regulations related to the origination and purchase of residential mortgage loans. The origination of residential mortgage loans is governed by a variety of federal and state laws and regulations, which are frequently changing. We sell residential mortgage loans that we have purchased or that we have originated to various parties, including Ginnie Mae and GSEs such as Fannie Mae or Freddie Mac and other financial institutions that purchase mortgage loans for investment or private label securitization. We may also pool FHA-insured and VA-guaranteed mortgage loans which back securities issued by Ginnie Mae. Our accrued mortgage repurchase liability represents management's best estimate of the probable loss that we may expect to incur for the representations and warranties in the contractual provisions of our sales of mortgage loans, but there is no assurance that our losses will not materially exceed such amounts.

Our accounting estimates and risk management processes rely on management judgment, which may prove inadequate or be adversely impacted by inaccurate assumptions or models. The processes we use to estimate probable credit losses for purposes of establishing the allowance for loan losses and to measure the fair value of financial instruments, certain of our liquidity and capital planning tools, as well as the processes we use to estimate the effects of changing interest rates and other market measures on our financial condition and results of operations, all depend upon management's judgment. Management's judgment and the data relied upon by management may be based on assumptions that prove to be inaccurate, particularly in times of market stress or other unforeseen circumstances. As a bank with total assets exceeding \$10 billion we have become subject to the stress testing requirements of the Dodd-Frank Act and our forecasting and modeling requirements have increased and become more complex. Even if the relevant factual assumptions determined by management are accurate, our decisions may prove to be inadequate or inaccurate because of other flaws in the design or use of analytical tools by management. Any such failures in our processes for producing accounting estimates and managing risks could have a material adverse effect on our business, financial condition and results of operations.

Our risk management strategies and processes may not be effective; our controls and procedures may fail or be circumvented. We continue to invest in the development of risk management techniques, strategies, assessment methods and related controls and monitoring approaches on an ongoing basis. However, these risk management strategies and processes may not be fully effective in mitigating our risk exposure in all economic market environments or against all types of risk. Any failures in our risk management strategies and processes to accurately identify, quantify and monitor our risk exposure could limit our ability to effectively manage our risks. Management regularly reviews and updates our internal controls over financial reporting, disclosure controls and procedures, and corporate governance policies and procedures. Any system of controls, however well designed and operated, is based in part on certain assumptions and management judgment and can provide only reasonable, not absolute, assurances that the objectives of the system are met. Any failure or circumvention of our controls and procedures or failure to comply with regulations related to controls and procedures could have a material adverse effect on our business, results of operations and financial condition.

We must effectively manage our counterparty risk. Financial services institutions are interrelated as a result of trading, clearing, counterparty and other relationships. Our Bank has exposure to many different industries and counterparties, and routinely executes transactions with counterparties in the financial services industry, including commercial banks, brokers and dealers, investment banks, and other institutional clients. Many of these transactions expose our Bank to credit risk in the event of a default by a counterparty or client. In addition, our Bank's credit risk may be increased when the collateral it is entitled to cannot be realized upon or is liquidated at prices not sufficient to recover the full amount of its credit or derivative exposure. Any such losses could have a material adverse effect on our business,

financial condition and results of operations.

Our business is susceptible to fraud. Our business exposes us to fraud risk from our loan and deposit customers, the parties they do business with, as well as from our employees, contractors and vendors. We rely on financial and other data from new and existing customers which could turn out to be fraudulent when accepting such customers, executing their financial transactions and making and purchasing loans and other financial assets. In times of increased economic stress we are at increased risk of fraud losses. We believe we have underwriting and operational controls in place to prevent or detect such fraud, but we cannot provide assurance that these controls will be effective in detecting fraud or that we will not experience fraud losses or incur costs or other damage related to such fraud, at levels that adversely affect our financial results or reputation. Our lending customers may also experience fraud in their businesses which could adversely affect their ability to repay their loans or make use of our services. Our exposure and the exposure of our customers to fraud may increase our

19

---

## Table of Contents

financial risk and reputation risk as it may result in unexpected loan losses that exceed those that have been provided for in our allowance for loan losses.

We must maintain adequate regulatory capital to support our business objectives. Under regulatory capital adequacy guidelines and other regulatory requirements, we must satisfy capital requirements based upon quantitative measures of assets, liabilities and certain off-balance sheet items. Our satisfaction of these requirements is subject to qualitative judgments by regulators that may differ materially from management's and that are subject to being determined retroactively for prior periods. Additionally, regulators can make subjective assessments about the adequacy of capital levels, even those over the "well-capitalized" requirements. Our ability to maintain our status as a financial holding company and to continue to operate our Bank as we have in recent periods is dependent upon a number of factors, including our Bank qualifying as "well capitalized" and "well managed" under applicable prompt corrective action regulations and upon our company qualifying on an ongoing basis as "well capitalized" and "well managed" under applicable Federal Reserve regulations.

Failure to meet regulatory capital standards could have a material adverse effect on our business, including damaging the confidence of customers in us, adversely impacting our reputation and competitive position and retention of key people. Any of these developments could limit our access to:

- Brokered deposits;
- The Federal Reserve discount window;
- Advances from the Federal Home Loan Bank;
- Capital markets transactions; and
- Development of new financial services.

Failure to meet regulatory capital standards may also result in higher FDIC assessments. If we fall below guidelines for being deemed "adequately capitalized" the OCC or Federal Reserve could impose restrictions on our activities and a broad range of regulatory requirements in order to effect "prompt corrective action." The capital requirements applicable to us are in a process of continuous evaluation and revision in connection with Basel III and the requirements of the Dodd-Frank Act. We cannot predict the final form, or the effects, of these regulations on our business, but among the possible effects are requirements that we slow our rate of growth or obtain additional capital which could reduce our earnings or dilute our existing stockholders.

We are dependent on funds obtained from borrowing or capital transactions or from our Bank to fund our obligations. We are a financial holding company engaged in the business of managing, controlling and operating our Bank. We conduct no material business or other activity at the parent company level other than activities incidental to holding equity and debt investments in our Bank. As a result, we rely on the proceeds of capital transactions, borrowings under our revolving line of credit, payments of interest and principal on loans made to our Bank and dividends on preferred stock issued by our Bank to pay our operating expenses, to satisfy our obligations to debtholders and to pay dividends on our preferred stock. Our Bank's ability to pay dividends may be limited. The profitability of our Bank is subject to fluctuation based upon, among other things, the cost and availability of funds, changes in interest rates and economic conditions in general. Our Bank's ability to pay dividends to us is subject to regulatory limitations that can, under certain adverse circumstances, prohibit the payment of dividends to us. Our right to participate in any distribution from the liquidation or sale of our Bank's assets is subject to the prior claims of our Bank's creditors. If we are unable to access funds from capital transactions, borrowing under our revolving line of credit or dividends or interest on loan payments from our Bank, we may be unable to satisfy our obligations to creditors or debtholders or pay dividends on our preferred stock. Changes in our Bank's operating results or capital requirements could require us to convert subordinated notes or preferred stock of our bank held by us into common equity, reducing our cash flow available to meet our obligations.

We are subject to claims and litigation in the ordinary course of our business, including claims that may not be covered by our insurers. Customers and other parties we engage with assert claims and take legal action against us on a regular basis and we regularly take legal action to collect unpaid borrower obligations, realize on collateral and assert our rights in commercial and other contexts. These actions frequently result in counter-claims against us. Litigation arises in a variety of contexts, including lending activities, employment practices, commercial agreements, fiduciary responsibility related to our wealth management services, intellectual property rights and other general

business matters.

Claims and legal actions may result in significant legal costs to defend us or assert our rights and reputational damage that adversely affects existing and future customer relationships. If claims and legal actions are not resolved in a manner favorable to us we may suffer significant financial liability or adverse effects upon our reputation, which could have a material adverse effect on our business, financial condition and results of operations. See Legal Proceedings below for additional disclosures regarding legal proceedings.

We purchase insurance coverage to mitigate a wide range of operating risks, including general liability, errors and omissions, professional liability, business interruption, cyber-crime, fraud and property loss, for events that may be materially detrimental

20

---

## Table of Contents

to our Bank or customers. There is no assurance that our insurance will be adequate to protect us against material losses in excess of our coverage limits or that insurers will perform their obligations under our policies without attempting to limit or exclude coverage. We could be required to pursue legal actions against insurers to obtain payment of amounts we are owed, and there is no assurance that such actions, if pursued, would be successful. We are subject to environmental liability risk associated with lending activities. A significant portion of our loan portfolio is secured by real property. During the ordinary course of business, we may foreclose on and take title to properties securing certain loans. There is a risk that hazardous or toxic substances could be found on these properties, and that we may be liable for remediation costs, as well as for personal injury and property damage. Environmental laws may require us to incur substantial expenses and may materially reduce the affected property's value by limiting our ability to use or sell it. Although we have policies and procedures requiring environmental review before initiating any foreclosure action on real property, these reviews may not be sufficient to detect all potential environmental hazards. The remediation costs and any other financial liabilities associated with an environmental hazard could have a material adverse effect on our financial condition and results of operations. Future laws or regulations or more stringent interpretations or enforcement policies with respect to existing laws and regulations may increase our exposure to environmental liability.

Severe weather, earthquakes, other natural disasters, pandemics, acts of war or terrorism and other external events could significantly impact our business. Severe weather, earthquakes, other natural disasters, pandemics, acts of war or terrorism and other adverse external events could have a significant impact on our ability to conduct business. Such events could affect the stability of our deposit base, impair the ability of borrowers to repay outstanding loans, impair the value of collateral securing loans, cause significant property damage, result in loss of revenue and/or cause us to incur additional expenses. Hurricanes have caused extensive flooding and destruction along the coastal areas of Texas, including communities where we conduct business. Although management has established disaster recovery policies and procedures, the occurrence of any such events could have a material adverse effect on our business, financial condition and results of operations.

### Risks Relating to Our Securities

Our stock price can be volatile. Stock price volatility may make it more difficult for you to resell your common stock when you want and at prices you find attractive. Our stock price can fluctuate significantly in response to a variety of factors including, among other things:

- actual or anticipated variations in quarterly and annual results of operations;
- changes in recommendations by securities analysts;
- changes in composition and perceptions of the investors who own our stock and other securities;
- changes in ratings from national rating agencies on publicly or privately owned debt securities;
- operating and stock price performance of other companies that investors deem comparable to us;
- news reports relating to trends, concerns and other issues in the financial services industry, including regulatory actions against other financial institutions;
- actual or expected economic conditions that are perceived to affect our company such as changes in commodity prices, real estate values or interest rates;
- perceptions in the marketplace regarding us and/or our competitors;
- new technology used, or services offered, by competitors;
- significant acquisitions or business combinations, strategic partnerships, joint ventures or capital commitments by or involving us or our competitors;
- changes in government regulations and interpretation of those regulations, changes in our practices requested or required by regulators and changes in regulatory enforcement focus; and
  - geopolitical conditions such as acts or threats of terrorism or military conflicts.

General market fluctuations, industry factors and general economic and political conditions and events, such as economic slowdowns or recessions, interest rate changes or credit loss trends, could also cause our stock price to decrease regardless of operating results as evidenced by the recent volatility and disruption of capital and credit markets.

The trading volume in our common stock is less than that of other larger financial services companies. Although our common stock is traded on the Nasdaq Global Select Market, the trading volume in our common stock is less than that of other larger financial services companies. Given the lower trading volume of our common stock, significant sales of our common stock, or the expectation of these sales, could cause our stock price to fall. In addition, a substantial majority of common stock outstanding is held by institutional shareholders, and trading activity involving large positions may increase volatility of the stock price. Concentration of ownership by institutional investors and inability to execute trades covering large numbers of

21

---



Table of Contents

shares can increase volatility of stock price. Changes in general economic outlook or perspectives on our business or prospects by our institutional investors, whether factual or speculative, can have a major impact on our stock price. Our preferred stock is thinly traded. There is only a limited trading volume in our preferred stock due to the small size of the issue and its largely institutional holder base. Significant sales of our preferred stock, or the expectation of these sales, could cause the price of the preferred stock to fall substantially.

An investment in our securities is not an insured deposit. Our common stock, preferred stock and indebtedness are not bank deposits and, therefore, are not insured against loss by the FDIC, any other deposit insurance fund or by any other public or private entity. Investment in our common stock is inherently risky for the reasons described in this “Risk Factors” section and elsewhere in this report and is subject to the same market forces that affect the price of securities of any company. As a result, if you acquire our common stock, preferred stock or indebtedness, you may lose some or all of your investment.

The holders of our indebtedness and preferred stock have rights that are senior to those of our common stockholders. As of December 31, 2016, we had \$111.0 million outstanding in subordinated notes issued by our holding company and \$113.4 million outstanding in junior subordinated notes that are held by statutory trusts which issued trust preferred securities to investors. At December 31, 2016 our Bank had \$175.0 million in subordinated notes outstanding. Payments of the principal and interest on our trust preferred securities are conditionally guaranteed by us to the extent not paid by each trust, provided the trust has funds available for such obligations.

Our subordinated notes and junior subordinated notes are senior to our shares of preferred stock and common stock in right of payment of dividends and other distributions. We must be current on interest and principal payments on our indebtedness before any dividends can be paid on our preferred stock or our common stock. In the event of our bankruptcy, dissolution or liquidation, the holders of our indebtedness must be satisfied before any distributions can be made to our preferred or common stockholders. If certain conditions are met, we have the right to defer interest payments on the junior subordinated debentures (and the related trust preferred securities) at any time or from time to time for a period not to exceed 20 consecutive quarters in a deferral period, during which time no dividends may be paid to holders of our preferred stock or common stock. Because our Bank’s subordinated notes are obligations of the Bank, they would in liquidation of our Bank or sale of its assets receive payment before any amounts would be payable to holders of our common stock, preferred stock or subordinated notes.

At December 31, 2016, we had issued and outstanding 6 million shares of our 6.50% Non-Cumulative Perpetual Preferred Stock, Series, A, having an aggregate liquidation preference of \$150.0 million. Our preferred stock is senior to our shares of common stock in right of payment of dividends and other distributions. We must be current on dividends payable to holders of preferred stock before any dividends can be paid on our common stock. In the event of our bankruptcy, dissolution or liquidation, the holders of our preferred stock must be satisfied before any distributions can be made to our common stockholders.

We do not currently pay dividends on our common stock. We have not paid dividends on our common stock and we do not expect to do so for the foreseeable future. Our ability to pay dividends is limited by regulatory restrictions and the need to maintain sufficient consolidated capital. The ability of our Bank to pay dividends to us is limited by its obligation to maintain sufficient capital and by other regulatory restrictions as discussed above at We are dependent on funds obtained from capital transactions or from our Bank to fund our obligations.

Restrictions on Ownership. The ability of a third party to acquire us is limited under applicable U.S. banking laws and regulations. The BHCA requires any bank holding company (as defined therein) to obtain the approval of the Federal Reserve prior to acquiring, directly or indirectly, more than 5% of our outstanding Common Stock. Any “company” (as defined in the BHCA) other than a bank holding company would be required to obtain Federal Reserve approval before acquiring “control” of us. “Control” generally means (i) the ownership or control of 25% or more of a class of voting securities, (ii) the ability to elect a majority of the directors or (iii) the ability otherwise to exercise a controlling influence over management and policies. A holder of 25% or more of our outstanding Common Stock, other than an individual, is subject to regulation and supervision as a bank holding company under the BHCA. In addition, under the Change in Bank Control Act of 1978, as amended, and the Federal Reserve’s regulations thereunder, any person, either individually or acting through or in concert with one or more persons, is required to provide notice to the Federal Reserve prior to acquiring, directly or indirectly, 10% or more of our outstanding common stock.

Anti-takeover provisions of our certificate of incorporation, bylaws and Delaware law may make it more difficult for you to receive a change in control premium. Certain provisions of our certificate of incorporation and bylaws could make a merger, tender offer or proxy contest more difficult, even if such events were perceived by many of our stockholders as beneficial to their interests. These provisions include advance notice for nominations of directors and stockholders' proposals, and authority to issue "blank check" preferred stock with such designations, rights and preferences as may be determined from time to time by our board of directors. In addition, as a Delaware corporation, we are subject to Section 203 of the Delaware General Corporation Law which, in general, prevents an interested stockholder, defined generally as a person owning 15% or more of a

Table of Contents

corporation's outstanding voting stock, from engaging in a business combination with our company for three years following the date that person became an interested stockholder unless certain specified conditions are satisfied. Limitations on payment of subordinated notes. Under the FDIA, "critically undercapitalized" banks may not, beginning 60 days after becoming critically undercapitalized, make any payment of principal or interest on their subordinated debt (subject to certain limited exceptions). In addition, under Section 18(i) of the FDIA, our Bank is required to obtain the advance consent of the FDIC to retire any part of its subordinated notes. Under the FDIA, a bank may not pay interest on its subordinated notes if such interest is required to be paid only out of net profits, or distribute any of its capital assets, while it remains in default on any assessment due to the FDIC.

Our Bank's subordinated indebtedness is unsecured and subordinate and junior in right of payment to the Bank's obligations to its depositors, its obligations under banker's acceptances and letters of credit, its obligations to any Federal Reserve Bank, certain obligations to the FDIC, and its obligations to its other creditors, whether now outstanding or hereafter incurred, except any obligations which expressly rank on a parity with or junior to the subordinated notes.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Our corporate headquarters is located in downtown Dallas, Texas. These facilities, which we lease, house our executive and primary administrative offices, as well as the principal banking headquarters of Texas Capital Bank. We also lease other facilities in our primary market regions of Dallas, Fort Worth, Houston, Austin and San Antonio, as well as in California, Illinois, Missouri and New York, some of which operate as full-service banking centers. We also lease an operations center in Richardson, Texas that houses our loan and deposit operations and our customer call center.

ITEM 3. LEGAL PROCEEDINGS

The Company is subject to various claims and legal actions that may arise in the course of conducting its business. Management does not expect the disposition of any of these matters to have a material adverse impact on the Company's financial statements or results of operations.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock is traded on The Nasdaq Global Select Market under the symbol "TCBI". On February 15, 2017, there were approximately 195 holders of record of our common stock.

Table of Contents

No cash dividends have ever been paid by us on our common stock, and we do not anticipate paying any cash dividends in the foreseeable future. Our principal source of funds to pay cash dividends on our common stock would be cash dividends from our Bank. The payment of dividends by our Bank is subject to certain restrictions imposed by federal banking laws, regulations and authorities.

The following table presents the range of high and low bid prices reported on The Nasdaq Global Select Market for each of the four quarters of 2015 and 2016.

Quarter Ended	Price Per Share	
	High	Low
March 31, 2015	\$54.81	\$40.40
June 30, 2015	63.70	47.55
September 30, 2015	63.25	48.01
December 31, 2015	61.83	46.25
March 31, 2016	49.88	29.78
June 30, 2016	51.84	34.54
September 30, 2016	55.25	42.36
December 31, 2016	81.25	54.20

Table of Contents

## Stock Performance Graph

The following table and graph sets forth the cumulative total stockholder return for the Company's common stock for the five-year period ending on December 31, 2016, compared to an overall stock market index (Russell 2000 Index) and the Company's peer group index (Nasdaq Bank Index). The Russell 2000 Index and Nasdaq Bank Index are based on total returns assuming reinvestment of dividends. The graph assumes an investment of \$100 on December 31, 2011. The performance graph represents past performance and should not be considered to be an indication of future performance.

	12/31/2011	12/31/2012	12/31/2013	12/31/2014	12/31/2015	12/31/2016
Texas Capital Bancshares, Inc.	\$ 100.00	\$ 146.42	\$ 203.20	\$ 177.49	\$ 161.45	\$ 256.13
Russell 2000 Index (RTY)	100.00	114.68	156.71	162.41	153.41	183.02
Nasdaq Bank Index (CBNK)	100.00	116.01	160.04	164.88	175.96	236.70

Source: Bloomberg

Table of Contents

## ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

You should read the selected financial data presented below in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and our consolidated financial statements and the related notes appearing elsewhere in this Form 10-K.

	At or For the Year Ended December 31,				
	2016	2015	2014	2013	2012
	(In thousands, except per share, average share and percentage data)				
Consolidated Operating Data(1)					
Interest income	\$703,408	\$602,958	\$514,547	\$444,625	\$398,457
Interest expense	63,594	46,428	37,582	25,112	21,578
Net interest income	639,814	556,530	476,965	419,513	376,879
Provision for credit losses	77,000	53,250	22,000	19,000	11,500
Net interest income after provision for credit losses	562,814	503,280	454,965	400,513	365,379
Non-interest income	60,780	47,738	42,511	44,024	43,040
Non-interest expense	382,397	326,523	285,114	256,729	219,881
Income before income taxes	241,197	224,495	212,362	187,808	188,538
Income tax expense	86,078	79,641	76,010	66,757	67,866
Net income	155,119	144,854	136,352	121,051	120,672
Preferred stock dividends	9,750	9,750	9,750	7,394	—
Net income available to common stockholders	\$145,369	\$135,104	\$126,602	\$113,657	\$120,672
Consolidated Balance Sheet Data(1)					
Total assets	\$21,697,134	\$18,903,821	\$15,900,034	\$11,717,174	\$10,537,853
Loans held for sale	968,929	86,075	—	—	—
Loans held for investment	13,001,011	11,745,674	10,154,887	8,486,603	6,785,837
Loans held for investment, mortgage finance loans	4,497,338	4,966,276	4,102,125	2,784,265	3,175,272
Liquidity assets(2)	2,725,645	1,681,374	1,233,990	61,427	94,410
Securities available-for-sale	24,874	29,992	41,719	63,214	100,195
Demand deposits	7,994,201	6,386,911	5,011,619	3,347,567	2,535,375
Total deposits	17,016,831	15,084,619	12,673,300	9,257,379	7,440,804
Federal funds purchased and repurchase agreements	109,575	143,051	92,676	170,604	297,115
Other borrowings	2,000,000	1,500,000	1,100,005	855,026	1,650,046
Subordinated notes	281,044	280,682	280,321	108,110	108,009
Trust preferred subordinated debentures	113,406	113,406	113,406	113,406	113,406
Stockholders’ equity	2,009,557	1,623,533	1,484,190	1,096,350	836,242

Table of Contents

At or For the Year Ended December 31,  
2016 2015 2014 2013 2012  
(In thousands, except per share, average share and  
percentage data)

Other Financial Data							
Income per share							
Basic	\$3.14	\$ 2.95	\$ 2.93	\$ 2.78	\$ 3.09		
Diluted	3.11	2.91	2.88	2.72	3.00		
Tangible book value per share(3)	37.17	31.69	28.72	22.54	20.04		
Book value per share	37.56	32.12	29.17	23.06	20.53		
Weighted average shares							
Basic	46,239,245	45,808,440	43,236,344	40,864,225	39,046,340		
Diluted	46,765,905	45,437,872	44,003,256	41,779,881	40,165,847		
Selected Financial Ratios							
Performance Ratios							
Net interest margin	3.14	% 3.14	% 3.78	% 4.22	% 4.41	%	
Return on average assets	0.74	% 0.79	% 1.05	% 1.17	% 1.35	%	
Return on average equity	9.27	% 9.65	% 11.31	% 12.82	% 16.93	%	
Efficiency ratio(4)	54.58	% 54.04	% 54.88	% 55.39	% 52.35	%	
Non-interest expense to average earning assets	1.88	% 1.84	% 2.26	% 2.58	% 2.57	%	
Asset Quality Ratios							
Net charge-offs (recoveries) to average LHI	0.29	% 0.07	% 0.05	% 0.05	% 0.07	%	
Net charge-offs (recoveries) to average LHI excluding mortgage finance loans	0.38	% 0.10	% 0.07	% 0.07	% 0.10	%	
Allowance for loan losses to LHI	0.96	% 0.84	% 0.71	% 0.78	% 0.75	%	
Allowance for loan losses to LHI excluding mortgage finance loans	1.29	% 1.20	% 0.99	% 1.03	% 1.10	%	
Allowance for loan losses to non-accrual loans	1.0x	.8x	2.3x	2.7x	1.3x		
Non-accrual loans to LHI	0.96	% 1.08	% 0.30	% 0.29	% 0.56	%	
Non-accrual loans to LHI excluding mortgage finance loans	1.29	% 1.53	% 0.43	% 0.38	% 0.82	%	
Total NPAs to LHI plus OREO	1.07	% 1.08	% 0.31	% 0.33	% 0.72	%	
Total NPAs to LHI excluding mortgage finance loans plus OREO	1.43	% 1.53	% 0.43	% 0.44	% 1.06	%	
Capital and Liquidity Ratios(5)							
CET1	8.97	% 7.47	% 7.89	% N/A	N/A		
Total capital ratio	10.23	% 11.05	% 11.83	% 10.73	% 9.97	%	
Tier 1 capital ratio	12.48	% 8.81	% 9.46	% 9.15	% 8.27	%	
Tier 1 leverage ratio	9.34	% 8.92	% 10.76	% 10.87	% 9.41	%	
Average equity/average assets	8.20	% 8.51	% 9.75	% 9.68	% 7.95	%	
Tangible common equity/total tangible assets(6)	8.49	% 7.69	% 8.26	% 7.87	% 7.73	%	
Average net loans/average deposits	95.82	% 101.71	% 111.57	% 116.25	% 129.97	%	

The consolidated operating data and consolidated balance sheet data presented above for the five most recent fiscal (1) years have been derived from our audited consolidated financial statements. The historical results are not necessarily indicative of the results to be expected in any future period.

(2) Liquidity assets consist of Federal funds sold and deposits in other banks.

(3) Stockholders' equity excluding preferred stock, less goodwill and intangibles, divided by shares outstanding at period end.

(4) Non-interest expense divided by the sum of net interest income and non-interest income.

27

---



Table of Contents

- (5) The Basel III Capital Rules specifying the CET1 ratio became effective on January 1, 2015.
- (6) Stockholders' equity excluding preferred stock and accumulated other comprehensive income less goodwill and intangibles divided by total assets less accumulated other comprehensive income and goodwill and intangibles.

28

---

Table of Contents

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

Certain 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. These forward-looking statements are based on our beliefs, assumptions and expectations of our future performance taking into account all information available to us at the time such statements are made. Words such as "believes," "expects," "estimates," "anticipates," "plans," "goals," "objectives," "expands," "intends," "seeks," "likely," "targeted," "continue," "remain," "will," "should," "may" and other similar 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 the credit quality of our loan portfolio, economic conditions, including the continued impact on our customers from declines and volatility in oil and gas prices, expectations regarding rates of default or loan losses, volatility in the mortgage industry, our business strategies and our expectations about future financial performance, future growth and earnings, the appropriateness of our allowance for loan losses and provision for loan losses, the impact of increased regulatory requirements on our business, increased competition, interest rate risk, new lines of business, new product or service offerings and new technologies.

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 or declines in the value of collateral related to external factors such as commodity prices, real estate values or interest rates, increased default rates and loan losses or adverse changes in the industry concentrations of our loan portfolio.

- Changing economic conditions or other developments adversely affecting our commercial, entrepreneurial and professional customers.

- 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 to correctly assess and model the assumptions supporting our allowance for loan losses, causing it to become inadequate in the event of deteriorations in loan quality and increases in charge-offs.

- Changes in the U.S. economy in general or the Texas economy specifically resulting in deterioration of credit quality, increases in non-performing assets or charge-offs or reduced demand for credit or other financial services we offer, including the effects from declines in the level of drilling and production related to the continued volatility in oil and gas prices.

- Adverse changes in economic or market conditions, or our operating performance, which could cause access to capital market transactions and other sources of funding to become more difficult to obtain on terms and conditions that are acceptable to us.

- The inadequacy of our available funds to meet our deposit, debt and other obligations as they become due, or our failure to maintain our capital ratios as a result of adverse changes in our operating performance or financial condition, or changes in applicable regulations or regulator interpretation of regulations impacting our business or the characterization or risk weight of our assets.

- The failure to effectively balance our funding sources with cash demands by depositors and borrowers.

- The failure to manage our information systems risk or to prevent cyber-attacks against us or our third party vendors, or to manage risks from disruptions or security breaches affecting our third party vendors.

- The 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, and potential adverse effects to our borrowers including their inability to repay loans with increased interest rates.

-

Legislative and regulatory changes imposing further restrictions and costs on our business, a failure to remain well capitalized or well managed status or regulatory enforcement actions against us, and uncertainty related to future implementation and enforcement of regulatory requirements resulting from the current political environment.

The failure to successfully execute our business strategy, which may include expanding into new markets, developing and launching new lines of business or new products and services within the expected timeframes and budgets or to successfully manage the risks related to the development and implementation of these new businesses, products or services.

Table of Contents

- The failure to attract and retain key personnel or the loss of key individuals or groups of employees.
- Adverse changes in economic or business conditions that impact the financial markets or 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.
- Uncertainty in the pricing of mortgage loans that we purchase, and later sell or securitize, as well as competition for the MSRMs related to these loans and related interest rate risk resulting from retaining MSRMs, and the potential effects of higher interest rates on our MCA loan volumes.
- Material failures of our accounting estimates and risk management processes based on management judgment, or the supporting analytical and forecasting models.
- Failure of our risk management strategies and procedures, including failure or circumvention of our controls.
- Credit risk resulting from our exposure to counterparties.
- An increase in the incidence or severity of fraud, illegal payments, security breaches and other illegal acts impacting our Bank and our customers.
- The failure to maintain adequate regulatory capital to support our business.
- Unavailability of funds obtained from borrowing or capital transactions or from our Bank to fund our obligations.
- 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.
- Environmental liability associated with properties related to our lending activities.
- Severe weather, natural disasters, acts of war or terrorism and other external events.

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 speak only as of the date hereof and 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 effectively service and 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 clientele 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.

In the third quarter of 2015, we launched a correspondent lending program, MCA, to complement our warehouse lending program. Through our MCA program we commit to purchase residential mortgage loans from independent correspondent lenders and deliver those loans into the secondary market via whole loan sales to independent third parties or in securitization transactions to Ginnie Mae and GSEs such as Fannie Mae and Freddie Mac. We retain the MSRMs in some cases with the expectation that they will be sold from time to time. Once purchased, these loans are classified as held for sale and are carried at fair value pursuant to our election of the fair value option. At the commitment date, we enter into a corresponding forward sale commitment with a third party, typically a GSE, to deliver the loans to the third party within a specified timeframe. The estimated gain/loss for the entire transaction (from initial purchase commitment to final delivery of loans) is recorded as an asset or liability. Fair value is derived from observable current market prices, when available, and includes the fair value of the MSRMs. At December 31, 2016 and 2015, we had \$968.9 million and \$86.1 million in loans held for sale related to MCA.

Outstanding energy loans totaled \$996.1 million, or approximately 5% of total loans, at December 31, 2016.

Unfunded energy loan commitments increased by \$24.6 million to \$530.8 million (53% of outstanding energy loans) at December 31, 2016 compared to \$506.2 million at December 31, 2015 reflecting new commitments. We

experienced deterioration in our energy portfolio in 2016, recording \$36.0 million in net charge-offs during 2016 compared to none for 2015. The energy-related deterioration contributed to the increase in our provision for credit losses to \$77.0 million for the year ended December 31, 2016, compared to \$53.3 million for the year ended December 31, 2015 and \$22.0 million for the year ended December 31, 2014, along with loan growth and an increase in criticized assets. Energy non-accruals remained flat at December 31, 2016 at

30

---

Table of Contents

\$121.5 million compared to \$120.4 million at December 31, 2015. We continue to proactively manage our energy portfolio and overall credit quality, and we believe we are appropriately reserved against further energy-related losses. The following discussion and analysis presents the significant factors affecting our financial condition as of December 31, 2016 and 2015 and results of operations for each of the three years related to the periods ended December 31, 2016, 2015 and 2014. This discussion should be read in conjunction with our consolidated financial statements and notes to the financial statements appearing later in this report.

Year ended December 31, 2016 compared to year ended December 31, 2015

We reported net income of \$155.1 million and net income available to common stockholders of \$145.4 million, or \$3.11 per diluted common share, for the year ended December 31, 2016, compared to net income of \$144.9 million and net income available to common stockholders of \$135.1 million, or \$2.91 per diluted common share, for the same period in 2015. Return on average equity ("ROE") was 9.27% and return on average assets ("ROA") was 0.74% for the year ended December 31, 2016, compared to 9.65% and 0.79%, respectively, for the same period in 2015. The decrease in ROE for 2016 compared to 2015 resulted from a higher provision for credit losses and the dilutive effect of the fourth quarter 2016 offering of 3.45 million common shares, which increased common equity by \$236.4 million. ROA remains low as a result of a larger liquidity assets balance, including a \$735.0 million increase in average liquidity assets for the year ended December 31, 2016 compared to the same period of 2015.

Net income increased \$10.3 million for the year ended December 31, 2016 compared to 2015. The \$10.3 million increase was primarily the result of an \$83.3 million increase in net interest income and a \$13.0 million increase in non-interest income, offset by a \$23.8 million increase in the provision for credit losses, a \$55.9 million increase in non-interest expense and a \$6.4 million increase in income tax expense.

Year ended December 31, 2015 compared to year ended December 31, 2014

We reported net income of \$144.9 million and net income available to common stockholders of \$135.1 million, or \$2.91 per diluted common share, for the year ended December 31, 2015, compared to net income of \$136.4 million and net income available to common stockholders of \$126.6 million, or \$2.88 per diluted common share, for the same period in 2014. Return on average equity ("ROE") was 9.65% and return on average assets ("ROA") was 0.79% for the year ended December 31, 2015, compared to 11.31% and 1.05%, respectively, for the same period in 2014. The decrease in ROE and essentially flat earnings per share for 2015 compared to 2014 reflected the dilutive effect of the fourth quarter 2014 offering of 2.5 million common shares for net proceeds of \$149.6 million. The ROA decrease resulted from a combination of reduced yields on loans and a \$2.3 billion increase in average liquidity assets for the year ended December 31, 2015 compared to the same period of 2014.

Net income increased \$8.5 million for the year ended December 31, 2015 compared to 2014. The \$8.5 million increase was primarily the result of a \$79.6 million increase in net interest income and a \$5.2 million increase in non-interest income, offset by a \$31.3 million increase in the provision for credit losses, a \$41.4 million increase in non-interest expense and a \$3.6 million increase in income tax expense.

#### Net Interest Income

Net interest income was \$639.8 million for the year ended December 31, 2016 compared to \$556.5 million for the same period of 2015. The increase in net interest income was primarily due to an increase of \$2.7 billion in average earning assets as compared to the same period of 2015. The increase in average earning assets included a \$1.5 billion increase in average net loans, a \$735.0 million increase in average liquidity assets and a \$410.0 million increase in average loans held for sale. For the year ended December 31, 2016, average net loans, liquidity assets and loans held for sale represented approximately 81%, 17% and 2%, respectively, of average earning assets compared to approximately 84%, 15% and less than 1%, respectively, in 2015.

Average interest-bearing liabilities for the year ended December 31, 2016 increased \$902.1 million from the year ended December 31, 2015, which included an \$803.4 million increase in interest-bearing deposits and a \$98.3 million increase in other borrowings. For the same periods, the average balance of demand deposits increased to \$8.1 billion from \$6.4 billion. The average cost of total deposits and borrowed funds increased to 0.23% for the year ended December 31, 2016, compared to 0.17% for the same period in the prior year. The average cost of interest-bearing liabilities increased from 0.46% for the year ended December 31, 2015 to 0.58% for the same period of 2016.

Net interest income was \$556.5 million for the year ended December 31, 2015 compared to \$477.0 million for the same period of 2014. The increase in net interest income was primarily due to an increase of \$5.1 billion in average earning assets as compared to the same period of 2014. The increase in average earning assets included a \$2.9 billion increase in average net loans and a \$2.3 billion increase in liquidity assets. For the year ended December 31, 2015, average net loans, liquidity assets and securities represented approximately 84%, 15% and less than 1%, respectively, of average earning assets compared to approximately 96%, 4% and 1%, respectively, in 2014.

Average interest-bearing liabilities for the year ended December 31, 2015 increased \$2.6 billion from the year ended December 31, 2014, which included a \$1.6 billion increase in interest-bearing deposits and a \$1.0 billion increase in other

Table of Contents

borrowings. For the same periods, the average balance of demand deposits increased to \$6.4 billion from \$4.2 billion. The average cost of total deposits and borrowed funds remained flat at 0.17% for the year ended December 31, 2015, compared to the same period in the prior year. The average cost of interest-bearing liabilities decreased from 0.50% for the year ended December 31, 2014 to 0.46% for the same period of 2015.

## Volume/Rate Analysis

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

	Years Ended December 31,			2015/2014		
	2016/2015			2015/2014		
	Net Change	Change Due To(1) Volume	Yield/Rate(2)	Net Change	Change Due To(1) Volume	Yield/Rate(2)
Interest income:						
Securities	\$(305 )	\$(301 )	\$ (4 )	\$(672 )	\$(622 )	\$( 50 )
Loans held for sale	13,766	15,667	(1,901 )	243	243	—
Loans held for investment, mortgage finance loans	15,070	9,004	6,066	25,616	33,288	(7,672 )
Loans held for investment	61,222	53,751	7,471	57,264	83,268	(26,004 )
Federal funds sold	865	102	763	475	459	16
Deposits in other banks	10,019	1,792	8,227	5,387	5,217	170
Total	100,637	80,015	20,622	88,313	121,853	(33,540 )
Interest expense:						
Transaction deposits	4,604	808	3,796	1,677	702	975
Savings deposits	8,290	1,530	6,760	4,399	2,852	1,547
Time deposits	294	(89 )	383	1,005	363	642
Deposits in foreign branches	(591 )	(591 )	—	(648 )	(616 )	(32 )
Other borrowings	4,110	180	3,930	1,789	1,966	(177 )
Long-term debt	458	22	436	624	897	(273 )
Total	17,165	1,860	15,305	8,846	6,164	2,682
Net interest income	\$83,472	\$78,155	\$ 5,317	\$79,467	\$115,689	\$(36,222 )

(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 assuming a 35% tax rate.

Net interest margin, which is defined as the ratio of net interest income to average earning assets, remained flat at 3.14% for the year ended December 31, 2016, compared to the same period in the prior year. We experienced a 5 basis point increase in the yield on earning assets, primarily as a result of growth in loans with higher yields. Funding costs, including demand deposits and borrowed funds, increased to 0.23% for 2016 compared to 0.17% for 2015. The spread on total earning assets, net of the cost of deposits and borrowed funds, was 3.22% for 2016 compared to 3.23% for 2015. The decrease resulted from the increase in cost of interest-bearing liabilities, as well as the increased proportion of liquidity assets to total earning assets and growth in lower yielding loans held for sale. Total funding costs, including all deposits, long-term debt and stockholders' equity increased to .30% for 2016 compared to 0.25% for 2015. Average long-term debt remained flat as compared to 2015 and the average interest rate on long-term debt for 2016 was 5.02% compared to 4.90% for 2015.

Net interest margin decreased from 3.78% for 2014 to 3.14% for 2015. This 64 basis point decrease was due to the growth in loans with lower yields and the \$2.3 billion increase in average balances of liquidity assets, which include Federal funds sold and deposits held principally at the Federal Reserve Bank of Dallas. Funding costs, including demand deposits and borrowed funds, remained at 0.17% for 2015 compared to 0.17% for 2014. The spread on total earning assets, net of the cost of deposits and borrowed funds, was 3.23% for 2015 compared to 3.91% for 2014. The decrease resulted from the reduction in yields on total loans, as well as the increased proportion of liquidity assets to total earning assets. Total funding costs, including all deposits, long-term debt and stockholders' equity decreased to



0.25% for 2015 compared to 0.29% for 2014. Average long-term debt increased by \$14.4 million from 2014 and the average interest rate on long-term debt for 2015 was 4.90% compared to 4.93% for 2014.

Table of Contents

## Consolidated Daily Average Balances, Average Yields and Rates

	Year ended December 31,								
	2016			2015			2014		
	Average Balance	Revenue / Expense(1)	Yield / Rate(2)	Average Balance	Revenue / Expense(1)	Yield / Rate(2)	Average Balance	Revenue / Expense(1)	Yield / Rate(2)
<b>Assets</b>									
Securities—taxable	\$26,619	\$943	3.54 %	\$33,616	\$1,197	3.56 %	\$43,029	\$1,590	3.70 %
Securities—non-taxable	604	36	5.92 %	1,544	87	5.63 %	6,171	366	5.93 %
Federal funds sold	310,128	1,547	0.50 %	269,610	682	0.25 %	83,816	207	0.25 %
Deposits in other banks	3,133,196	16,312	0.52 %	2,438,742	6,293	0.26 %	360,857	906	0.25 %
Loans held for sale	416,325	14,009	3.36 %	6,359	243	3.82 %	—	—	— %
Loans held for investment, mortgage finance	4,292,942	134,747	3.14 %	3,992,548	119,677	3.00 %	2,948,938	94,061	3.19 %
Loans held for investment	12,371,634	536,031	4.33 %	11,113,520	474,809	4.27 %	9,265,725	417,545	4.51 %
Less reserve for loan losses	163,623	—	—	114,965	—	—	91,363	—	—
Loans held for investment, net	16,500,953	670,778	4.07 %	14,991,103	594,486	3.97 %	12,123,300	511,606	4.22 %
Total earning assets	20,387,825	703,625	3.45 %	17,740,974	602,988	3.40 %	12,617,173	514,675	4.08 %
Cash and other assets	558,900			480,616			393,884		
Total assets	\$20,946,725			\$18,221,590			\$13,011,057		
<b>Liabilities and stockholders' equity</b>									
Transaction deposits	\$2,199,292	\$7,219	0.33 %	\$1,680,220	\$2,615	0.16 %	\$960,812	\$938	0.10 %
Savings deposits	6,403,306	27,028	0.42 %	5,920,046	18,738	0.32 %	4,938,039	14,339	0.29 %
Time deposits	493,128	2,928	0.59 %	510,378	2,634	0.52 %	417,317	1,629	0.39 %
Deposits in foreign branches	—	—	—	181,657	591	0.33 %	361,203	1,239	0.34 %
Total interest-bearing deposits	9,095,726	37,175	0.41 %	8,292,301	24,578	0.30 %	6,677,371	18,145	0.27 %
Other borrowings	1,480,302	6,645	0.45 %	1,382,013	2,535	0.18 %	380,167	746	0.20 %
Subordinated notes	280,850	16,764	5.97 %	280,487	16,764	5.98 %	265,773	16,202	6.10 %
Trust preferred subordinated debentures	113,406	3,009	2.65 %	113,406	2,551	2.25 %	113,406	2,489	2.19 %
Total interest-bearing liabilities	10,970,284	63,593	0.58 %	10,068,207	46,428	0.46 %	7,436,717	37,582	0.51 %
Demand deposits	8,124,174			6,447,147			4,188,173		
Other liabilities	134,678			155,960			116,566		
Stockholders' equity	1,717,589			1,550,276			1,269,601		
Total liabilities and stockholders' equity	\$20,946,725			\$18,221,590			\$13,011,057		
Net interest income		\$640,032			\$556,560			\$477,093	
Net interest margin			3.14 %			3.14 %			3.78 %
Net interest spread			2.87 %			2.94 %			3.57 %
Loan spread(3)			3.81 %			3.80 %			4.05 %

(1)

The loan averages include non-accrual loans which are stated net of unearned income. Loan interest income includes loan fees totaling \$56.5 million, \$55.8 million and \$50.0 million for the years ended December 31, 2016, 2015 and 2014, respectively.

- (2) Taxable equivalent rates used where applicable assuming a 35% tax rate.
- (3) Yield on loans, net of reserves, less funding cost including all deposits and borrowed funds.

Table of Contents

## Non-interest Income

	Year ended December 31,		
	2016	2015	2014
	(in thousands)		
Service charges on deposit accounts	\$10,341	\$8,323	\$7,253
Trust fee income	4,268	5,022	4,937
Bank owned life insurance (BOLI) income	2,073	2,011	2,067
Brokered loan fees	25,339	18,661	13,981
Swap fees	2,866	4,275	2,992
Other(1)	15,893	9,446	11,281
Total non-interest income	\$60,780	\$47,738	\$42,511

Other non-interest income includes such items as letter of credit fees, gain on sale of loans held for sale, servicing (1) fees related to the MCA program 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 by \$13.0 million during the year ended December 31, 2016 to \$60.8 million, compared to \$47.7 million for the same period in 2015. This increase was primarily due to a \$6.7 million increase in brokered loan fees as a result of an increase in mortgage finance and MCA volumes. Service charges increased \$2.0 million during 2016 compared to the same period of 2015 as a result of an increase in deposit balances year-over-year as well as improved pricing. Other non-interest income increased \$6.4 million during 2016 compared to the same period of 2015. Of this \$6.4 million increase, \$4.7 million relates to increases in servicing fee income and gain on sale of loans held for sale related to our MCA business. Offsetting these increases was a \$1.4 million decrease in swap fee income during the year ended December 31, 2016 as compared to the same period in 2015. Swap fees are fees related to customer swap transactions, are received from the institution that is our counterparty on the transaction and fluctuate from time to time based on the number and volume of transactions closed during the year.

Non-interest income increased by \$5.2 million during the year ended December 31, 2015 to \$47.7 million, compared to \$42.5 million for the same period in 2014. This increase was primarily due to a \$4.7 million increase in brokered loan fees as a result of an increase in mortgage finance volumes. Swap fee income increased \$1.3 million during 2015 compared to the same period of 2014. Service charges increased \$1.1 million during 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 \$1.8 million decrease in other 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 and general economic conditions. In order to achieve continued growth in non-interest income, management from time to time evaluates new products, new lines of business or the expansion of existing lines of business. Any new product introduction or new market entry could place additional demands on capital and managerial resources and introduce new risks to our business.

## Non-interest Expense

	Year ended December 31,		
	2016	2015	2014
	(in thousands)		
Salaries and employee benefits	\$228,985	\$192,610	\$169,051
Net occupancy expense	23,221	23,182	20,866
Marketing	17,303	16,491	15,989
Legal and professional	23,326	22,150	21,182
Communications and technology	25,562	21,425	18,667
FDIC insurance assessment	24,440	17,231	10,919
Allowance and other carrying costs for OREO	824	22	85
Other(1)	38,736	33,412	28,355
Total non-interest expense	\$382,397	\$326,523	\$285,114

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

34

---

## Table of Contents

Non-interest expense for the year ended December 31, 2016 increased \$55.9 million compared to the same period of 2015 primarily related to increases in salaries and employee benefits, legal and professional expense, communications and technology expense, FDIC insurance assessment and other non-interest expense.

Salaries and employee benefits expense increased \$36.4 million to \$229.0 million during the year ended December 31, 2016 compared to the same period of 2015. This increase resulted primarily from general business growth and continued build-out.

Legal and professional expense increased \$1.2 million, or 5%, for the year ended December 31, 2016 compared to the same period in 2015. Our legal and professional expense will continue to fluctuate from year to year and could increase in the future due to additional growth and as we respond to continued regulatory changes and execute strategic initiatives.

Communications and technology expense increased \$4.1 million to \$25.6 million during the year ended December 31, 2016 compared to the same period in 2015 as a result of general business and customer growth and continued build-out needed to support that growth, including investment in IT security.

FDIC insurance assessment expense increased \$7.2 million from \$17.2 million in 2015 to \$24.4 million primarily as a result of the increase in total assets from December 31, 2015 to December 31, 2016.

Non-interest expense for the year ended December 31, 2015 increased \$41.4 million compared to the same period of 2014 primarily related to increases in salaries and employee benefits, net occupancy expense, legal and professional expense, communications and technology expense, FDIC insurance assessment and other non-interest expense.

Salaries and employee benefits expense increased \$23.6 million to \$192.6 million during the year ended December 31, 2015 compared to the same period in 2014. This increase resulted primarily from general business growth and continued build-out.

Net occupancy expense for the year ended December 31, 2015 increased \$2.3 million compared to the same period in 2014 as a result of general business growth and continued build-out needed to support our growth.

Legal and professional expense increased \$968,000, or 5%, for the year ended December 31, 2015 compared to the same period in 2014.

Communications and technology expense increased \$2.8 million to \$21.4 million during the year ended December 31, 2015 compared to the same period in 2014 as a result of general business and customer growth and continued build-out needed to support that growth, including investment in IT security.

FDIC insurance assessment expense increased \$6.3 million from \$10.9 million in 2014 to \$17.2 million primarily as a result of the increase in total assets from December 31, 2014 to December 31, 2015.

### Analysis of Financial Condition

#### Loans Held for Investment

Our total loans held for investment have grown at an annual rate of 5%, 17% and 26% in 2016, 2015 and 2014, respectively, reflecting the continued build-up of our lending operations. 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, representing 73% of total loans held for investment at December 31, 2016. Consumer loans generally have represented 1% or less of the portfolio from December 31, 2012 to December 31, 2016. 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 December 31, 2016, we had \$2.2 billion in syndicated loans, \$598.3 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 December 31, 2016, \$83.6 million of our syndicated loans were on non-accrual.



Table of Contents

The following table summarizes our loans held for investment on a gross basis by major category as of the dates indicated (in thousands):

	December 31,				
	2016	2015	2014	2013	2012
Commercial	\$7,291,545	\$6,672,631	\$5,869,219	\$5,020,565	\$4,106,419
Mortgage finance	4,497,338	4,966,276	4,102,125	2,784,265	3,175,272
Construction	2,098,706	1,851,717	1,416,405	1,262,905	737,637
Real estate	3,462,203	3,139,197	2,807,127	2,146,522	1,892,753
Consumer	34,587	25,323	19,699	15,350	19,493
Equipment leases	185,529	113,996	99,495	93,160	69,470
Total loans held for investment	\$17,569,908	\$16,769,140	\$14,314,070	\$11,322,767	\$10,001,044

For additional information on the types of loans we originate, see Note 3 - Loans Held for Investment and Allowance for Loan Losses in the accompanying notes to the consolidated financial statements included elsewhere in this report.

Portfolio Geographic and Industry Concentrations

When considering our mortgage finance loans and other national lines of business, more than 50% of our loan exposure is outside of Texas and more than 50% of our deposits are sourced outside of Texas. However, as of December 31, 2016, a 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. We also make loans to these customers that are 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.

We updated our internal industry reporting during 2016 to provide more clarity in our portfolio analysis and comparison to our banking peers. The table below summarizes the industry concentrations of our funded loans held for investment on a gross basis at December 31, 2016.

(in thousands except percentage data)	Amount	Percent of Total Loans Held for Investment	
Real estate and construction	\$4,894,517	27.9	%
Mortgage finance loans	4,497,338	25.6	%
Financials excluding banks	3,518,984	20.0	%
Oil & gas and pipelines	996,079	5.7	%
Healthcare and pharmaceuticals	620,319	3.5	%
Retail	371,193	2.1	%
Machinery, equipment and parts manufacturing	351,924	2.0	%
Technology, telecom and media	306,334	1.7	%
Government and education	305,302	1.7	%
Commercial services	299,239	1.7	%
Materials and commodities	190,726	1.1	%
Consumer services	183,772	1.1	%
Transportation services	131,336	0.7	%
Entertainment and recreation	120,719	0.7	%
Food and beverage manufacturing and wholesale	113,251	0.7	%
Auto-related	92,162	0.5	%
Diversified or miscellaneous	576,713	3.3	%
Total loans held for investment	\$17,569,908	100.0	%





Table of Contents

Our largest concentration in any single industry is in real estate and construction. Loans extended to borrowers within the real estate and construction industries generally include market risk real estate loans. We extend market risk real estate loans, including both construction/development financing and limited term financing, to builders, professional real estate developers and owners/managers of commercial real estate projects and properties who have a demonstrated record of past success with similar properties. These loans are generally repaid through the borrowers' sale or lease of the properties, and loan amounts are determined in part from an analysis of pro forma cash flows.

Borrowers represented within the real estate and construction category are largely owners and managers of both residential and non-residential commercial real estate properties, including homebuilders.

Loans extended to borrowers in the financials excluding banks category are comprised largely of loans to companies who loan money to businesses and consumers for various purposes including, but not limited to, insurance, consumer goods and real estate. This category also includes loans to companies involved in investment management and securities and commodities trading.

We make loans that are appropriately collateralized under our credit standards. Approximately 97% of our funded loans held for investment are secured by collateral. Over 77% of the real estate collateral is located in Texas. The table below sets forth information regarding the distribution of our funded loans held for investment on a gross basis among various types of collateral at December 31, 2016 (in thousands except percentage data):

	Amount	Percent of Total Loans	
Collateral type:			
Business assets	\$5,496,756	31.3	%
Real property	5,560,909	31.7	%
Mortgage finance loans	4,497,338	25.6	%
Energy	621,811	3.5	%
Unsecured	520,119	3.0	%
Other assets	578,514	3.2	%
Highly liquid assets	231,526	1.3	%
Rolling stock	46,464	0.3	%
U. S. Government guaranty	16,471	0.1	%
Total loans held for investment	\$17,569,908	100.0	%

Table of Contents

As noted in the table above, approximately 32% of our loans held for investment as of December 31, 2016 are secured by real property. The table below summarizes our real estate loan portfolio as segregated by the type of property securing the credit. Property type concentrations are stated as a percentage of year-end total real estate loans as of December 31, 2016 (in thousands except percentage data):

	Amount	Percent of Total Real Estate Loans	
Property type:			
Market risk			
1-4 Family dwellings (other than condominium)	\$809,580	15.0	%
Office buildings	642,474	12.0	%
Apartment buildings	583,704	10.0	%
Industrial buildings	529,794	10.0	%
Residential lots	425,922	8.0	%
Shopping center/mall buildings	397,237	7.0	%
Hotel/motel buildings	348,270	6.0	%
Senior housing	341,215	6.0	%
Commercial lots	121,335	2.0	%
Medical buildings	110,741	2.0	%
Commercial buildings	103,386	2.0	%
Unimproved land	28,296	1.0	%
Other	181,591	3.0	%
Other than market risk			
Commercial buildings	168,485	3.0	%
Industrial buildings	216,275	4.0	%
1-4 Family dwellings (other than condominium)	232,430	4.0	%
Other	320,174	5.0	%
Total real estate loans	\$5,560,909	100.0	%

The table below summarizes our market risk real estate portfolio at December 31, 2016 as segregated by the geographic region in which the property is located (in thousands except percentage data):

	Amount	Percent of Total	
Geographic region:			
Dallas/Fort Worth	\$1,142,477	24.7	%
Houston	1,287,200	27.9	%
San Antonio	478,006	10.3	%
Austin	538,009	11.6	%
Other Texas cities	198,481	4.3	%
Other states	979,372	21.2	%
Total market risk real estate loans	\$4,623,545	100.0	%

We extend market risk real estate loans, including both construction/development financing and limited term financing, to builders, professional real estate developers and owners/managers of commercial real estate projects and properties who have a demonstrated record of past success with similar properties. Collateral properties include office buildings, warehouse/distribution buildings, shopping centers, apartment buildings and residential and commercial tract development located primarily within our five major metropolitan markets in Texas. These loans are generally repaid through the borrowers' sale or lease of the properties, and loan amounts are determined in part from an analysis of pro forma cash flows. Loans are also underwritten to comply with product-type specific advance rates against both cost and market value. We engage a variety of



Table of Contents

professional firms to supply appraisals, market studies and feasibility reports, environmental assessments and project site inspections to complement our internal resources to underwrite and monitor these credit exposures.

The determination of collateral value is critically important when financing real estate. As a result, obtaining current and objectively prepared appraisals is a major part of our underwriting and monitoring processes. Generally, our policy requires a new appraisal every three years. However, in periods of economic uncertainty where real estate values can fluctuate rapidly as in recent years, more current appraisals are obtained when warranted by conditions such as a borrower's deteriorating financial condition, their possible inability to perform on the loan or other indicators of increasing risk of reliance on collateral value as the sole repayment of the loan. Annual appraisals are generally obtained for loans graded substandard or worse where real estate is a material portion of the collateral value and/or the income from the real estate or sale of the real estate is the primary source of debt service.

Appraisals are, in substantially all cases, reviewed by a third party to determine the reasonableness of the appraised value. The third party reviewer will challenge whether or not the data used is appropriate and relevant, form an opinion as to the appropriateness of the appraisal methods and techniques used, and determine if overall the analysis and conclusions of the appraiser can be relied upon. Additionally, the third party reviewer provides a detailed report of that analysis. Further review may be conducted by our credit officers, as well as by the Bank's managed asset committee as conditions warrant. These additional steps of review are undertaken to confirm that the underlying appraisal and the third party analysis can be relied upon. If we have differences, we address those with the reviewer and determine an appropriate resolution. Both the appraisal process and the appraisal review process can be less reliable in establishing accurate collateral values during and following periods of economic weakness due to the lack of comparable sales and the limited availability of financing to support an active market of potential purchasers.

**Large Credit Relationships**

We originate and maintain large credit relationships with numerous customers in the ordinary course of business. The legal limit of our Bank is approximately \$344.6 million. We employ much lower house limits which vary by assigned risk grade, product and collateral type. Such house limits, which generally range from \$20 million to \$50 million, may be exceeded with appropriate authorization for exceptionally strong borrowers and otherwise where business opportunity and perceived credit risk warrant a somewhat larger investment. We consider large credit relationships to be those with commitments equal to or in excess of \$10.0 million. The following table provides additional information on our large held for investment credit relationships, excluding mortgage finance, outstanding at year-end (in thousands, except relationship data):

	December 31, 2016		December 31, 2015	
	Period End Balances		Period End Balances	
	Number		Number	
	of	Committed Outstanding	of	Committed Outstanding
	Relationships	Relationships	Relationships	Relationships
\$20.0 million and greater	252	\$7,172,490 \$4,244,458	233	\$6,504,087 \$3,915,113
\$10.0 million to \$19.9 million	317	4,543,916 3,319,070	309	4,367,431 2,925,850

Growth in period-end outstanding balances related to large credit relationships primarily resulted from an increase in number of commitments. The following table summarizes the average per relationship committed and outstanding loan balances related to our large held for investment credit relationships, excluding mortgage finance, at year-end (in thousands, except relationship data):

	2016 Average		2015 Average	
	Balance	Balance	Balance	Balance
	Committed	Outstanding	Committed	Outstanding
\$20.0 million and greater	\$28,462	\$26,636	\$27,915	\$16,803
\$10.0 million to \$19.9 million	14,334	10,470	14,134	9,469



Table of Contents

## Loan Maturities and Interest Rate Sensitivity as of December 31, 2016

(in thousands)	Remaining Maturities of Selected Loans			
	Total	Within 1 Year	1-5 Years	After 5 Years
Loan maturity:				
Commercial	\$7,291,545	\$ 3,228,402	\$3,640,185	\$ 422,958
Mortgage finance	4,497,338	4,497,338	—	—
Construction	2,098,706	692,148	1,323,960	82,598
Real estate	3,462,203	708,417	1,969,963	783,823
Consumer	34,587	29,607	1,502	3,478
Equipment leases	185,529	5,393	117,799	62,337
Total loans held for investment	\$17,569,908	\$ 9,161,305	\$7,053,409	\$ 1,355,194
Interest rate sensitivity for selected loans with:				
Predetermined interest rates	\$2,224,155	\$ 1,194,053	\$ 518,222	\$ 511,880
Floating or adjustable interest rates	15,345,753	7,967,252	6,535,187	843,314
Total loans held for investment	\$17,569,908	\$ 9,161,305	\$7,053,409	\$ 1,355,194

## Interest Reserve Loans

As of December 31, 2016 and December 31, 2015, we had \$870.0 million and \$687.3 million, respectively, in loans held for investment that included interest reserve arrangements, representing approximately 41% and 37%, respectively, of our construction loans. Interest reserve provisions are common in construction loans. The use of interest reserves is carefully controlled by our underwriting standards, which consider the feasibility of the project, the creditworthiness of the borrower and guarantors and the loan-to-value coverage of the collateral. The interest reserve allows the borrower to draw loan funds to pay interest charges on the outstanding balance of the loan when financial conditions precedent are met. When drawn, the interest is capitalized and added to the loan balance, subject to conditions specified during the initial underwriting and at the time the credit is approved. We have ongoing controls for monitoring compliance with loan covenants, advancing funds and determining default conditions.

When we finance land on which improvements will be constructed, construction funds are generally not advanced until the borrower has received lease or purchase commitments which will meet cash flow coverage requirements and/or our analysis of market conditions and project feasibility indicates to our satisfaction that such lease or purchase commitments are forthcoming or other sources of repayment have been identified to repay the loan. It is our general policy to require a substantial equity investment by the borrower to complement the Bank's credit commitment. Any such required borrower investment is first contributed and invested in the project before any draws are allowed under the Bank's credit commitment. We require current financial statements of the borrowing entity and guarantors, as well as conduct periodic inspections of the project and analysis of whether the project is on schedule or delayed. Updated appraisals are ordered when necessary to validate the collateral values to support all advances, including reserve interest. Advances of interest reserves are discontinued if collateral values do not support the advances or if the borrower does not comply with other terms and conditions in the loan agreements. In addition, most of our construction lending is performed in Texas and our lenders are very familiar with trends in local real estate. If at any time we believe that our collateral position is jeopardized, we retain the right to stop the use of interest reserves. As of December 31, 2016, none of our loans with interest reserves were on non-accrual.

Table of Contents

## Non-performing Assets

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

	As of December 31,		
	2016	2015	2014
Non-accrual loans(1)(2)			
Commercial			
Oil and gas properties	\$115,599	\$104,179	\$694
Assets of the borrowers	18,592	30,360	31,179
Inventory	27,630	2,099	
Other	3,119	2,020	1,249
Total commercial	164,940	138,658	33,122
Construction			
Commercial building	—	16,667	—
Other	159	—	—
Total construction	159	16,667	—
Real estate			
Commercial property	2,083	2,867	4,781
Unimproved land and/or developed residential lots	—	3,576	3,735
Farm land	326	12,486	—
Other	—	383	1,431
Total real estate	2,409	19,312	9,947
Consumer	200	—	62
Equipment leases	83	5,151	173
Total non-accrual loans	167,791	179,788	43,304
Repossessed assets:			
OREO(3)	18,961	278	568
Other repossessed assets	—	230	—
Total other repossessed assets	18,961	508	568
Total non-performing assets	\$186,752	\$180,296	\$43,872
Restructured loans - accruing	\$—	\$249	\$1,806
Loans past due 90 days and accruing(4)	\$10,729	\$7,013	\$5,274

If these loans had been current throughout their terms, interest and fees on loans would have increased by (1) approximately \$7.9 million, \$7.0 million and \$2.1 million for the years ended December 31, 2016, 2015 and 2014, respectively.

(2) As of December 31, 2016, 2015 and 2014, non-accrual loans included \$18.1 million, \$24.9 million and \$12.1 million, respectively, in loans that met the criteria for restructured.

At December 31, 2016, 2015 and 2014, there was no valuation allowance recorded against the OREO balance. For (3) additional information on OREO, see Note 4 - OREO and Valuation Allowance for Losses on OREO in the accompanying notes to the consolidated financial statements included elsewhere in this report.

(4) At December 31, 2016, 2015 and 2014, loans past due 90 days and still accruing includes premium finance loans of \$6.8 million, \$6.6 million and \$3.7 million, respectively.

Total non-performing assets at December 31, 2016 increased \$6.5 million from December 31, 2015, compared to a \$136.4 million increase from December 31, 2014 to December 31, 2015. Energy non-performing assets totaled \$121.5 million at December 31, 2016 compared to \$120.4 million at December 31, 2015. Our provision for credit losses increased as a result of the deterioration of our energy portfolio and the significant growth in loans held for investment, excluding mortgage finance loans, and an increase in total criticized loans, as well as a change in applied risk weights. Risk weights are based on historical loss experience as adjusted for current environmental factors as well as changes in the composition of our pass-rated loan portfolio. This growth resulted in an increase in the reserve for



loan losses as a percent of loans excluding mortgage finance loans for 2016 as compared to 2015.

41

---

Table of Contents

Specific reserves on impaired loans held for investment were \$34.6 million at December 31, 2016, compared to \$23.5 million at December 31, 2015 and \$8.4 million at December 31, 2014. We recognized \$1.4 million in interest income on non-accrual loans during 2016 compared to \$1.6 million in 2015 and \$1.7 million in 2014. Additional interest income that would have been recorded if the loans had been current during the years ended December 31, 2016, 2015 and 2014 totaled \$7.9 million, \$7.0 million and \$2.1 million, respectively. Average impaired loans outstanding during the years ended December 31, 2016, 2015 and 2014 totaled \$174.1 million, \$102.3 million and \$46.4 million, respectively.

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 December 31, 2016, we had \$19.3 million in loans of this type, compared to none at December 31, 2015.

For additional information on non-performing assets, see Note 3 - Loans Held for Investment and Allowance for Loan Losses in the accompanying notes to the consolidated financial statements included elsewhere in this report.

Summary of Loan Loss Experience

The provision for credit losses, which includes a provision for losses on unfunded commitments, is a charge to earnings to maintain the allowance for loan losses at a level consistent with management's assessment of the collectability of the loan portfolio in light of current economic conditions and market trends. We recorded a provision for credit losses of \$77.0 million for the year ended December 31, 2016, \$53.3 million for the year ended December 31, 2015, and \$22.0 million for the year ended December 31, 2014. The increase in provision recorded during 2016 compared to the same period in 2015 is related to the deterioration in our energy portfolio, growth in loans held for investment, excluding mortgage finance loans, and an increase in total criticized loans, as well as changes in applied risk weights. Risk weights are based on historical loss experience as well as changes in the composition of our pass-rated loan portfolio.

The allowance for credit losses, which includes a liability for losses on unfunded commitments, totaled \$179.5 million at December 31, 2016, \$150.1 million at December 31, 2015 and \$108.0 million at December 31, 2014. The combined allowance percentage increased to 1.38% at year-end 2016 from 1.28% and 1.06% of loans held for investment excluding mortgage finance loans at December 31, 2015 and 2014, respectively. The combined allowance as a percent of loans held for investment, excluding mortgage finance loans, trended down during 2014 as we recognized losses on loans for which there were specific or general allocations of reserves and saw an improvement in our overall credit quality. During 2016 and 2015, the combined allowance began trending up primarily as a result of the increasing provision for credit losses driven by deterioration in our energy portfolio and management's allocation of a higher reserve to the Bank's pass-rated portfolio as deemed appropriate in light of current environmental conditions.

The overall allowance for loan losses results from consistent application of our loan loss reserve methodology. At December 31, 2016, we believe the allowance is sufficient to cover all inherent losses in the portfolio and has been derived from consistent application of our methodology. Should any of the factors considered by management in evaluating the appropriateness of the allowance for loan losses change, our estimate of inherent losses in the portfolio could also change, which would affect the level of future provisions for loan losses.

See Note 1 - Operations and Summary of Significant Accounting Policies and Note 3 - Loans Held for Investment and Allowance for Loan Losses in the accompanying notes to the consolidated financial statements included elsewhere in this report for details of the allowance for loan losses.

Table of Contents

The table below presents a summary of our loan loss experience for the past five years (in thousands except percentage and multiple data):

	Year Ended December 31,					
	2016	2015	2014	2013	2012	
Allowance for loan losses:						
Beginning balance	\$141,111	\$100,954	\$87,604	\$74,337	\$70,295	
Loans charged-off:						
Commercial	56,558	16,254	9,803	6,575	6,708	
Construction	—	—	—	—	—	
Real estate	528	389	296	144	899	
Consumer	47	62	266	45	49	
Equipment leases	—	25	—	2	204	
Total charge-offs	57,133	16,730	10,365	6,766	7,860	
Recoveries:						
Commercial	9,364	4,944	2,762	1,203	832	
Construction	34	400	—	—	10	
Real estate	63	33	79	270	812	
Consumer	21	173	162	73	33	
Equipment leases	77	38	1,082	322	108	
Total recoveries	9,559	5,588	4,085	1,868	1,795	
Net charge-offs	47,574	11,142	6,280	4,898	6,065	
Provision for loan losses	74,589	51,299	19,630	18,165	10,107	
Ending balance	\$168,126	\$141,111	\$100,954	\$87,604	\$74,337	
Allowance for off-balance sheet credit losses:						
Beginning balance	\$9,011	\$7,060	\$4,690	\$3,855	\$2,462	
Provision for off-balance sheet credit losses	2,411	1,951	2,370	835	1,393	
Ending balance	\$11,422	\$9,011	\$7,060	\$4,690	\$3,855	
Total allowance for credit losses	\$179,548	\$150,122	\$108,014	\$92,294	\$78,192	
Total provision for credit losses	\$77,000	\$53,250	\$22,000	\$19,000	\$11,500	
Allowance for loan losses to LHI	0.96	% 0.84	% 0.71	% 0.78	% 0.75	%
Allowance for loan losses to LHI excluding mortgage finance loans	1.29	% 1.20	% 0.99	% 1.03	% 1.10	%
Net charge-offs to average LHI	0.29	% 0.07	% 0.05	% 0.05	% 0.07	%
Net charge-offs to average LHI excluding mortgage finance loans	0.38	% 0.10	% 0.07	% 0.07	% 0.10	%
Total provision for credit losses to average LHI	0.46	% 0.35	% 0.18	% 0.19	% 0.14	%
Total provision for credit losses to average LHI excluding mortgage finance loans	0.62	% 0.48	% 0.24	% 0.25	% 0.19	%
Recoveries to total charge-offs	16.73	% 33.40	% 39.41	% 27.61	% 22.84	%
Allowance for off-balance sheet credit losses to off-balance sheet credit commitments	0.19	% 0.16	% 0.13	% 0.12	% 0.14	%
Combined allowance for credit losses to LHI	1.03	% 0.90	% 0.76	% 0.82	% 0.78	%
Combined allowance for credit losses to LHI excluding mortgage finance loans	1.38	% 1.28	% 1.06	% 1.09	% 1.15	%
Non-performing assets:						
Non-accrual loans(1)(2)	\$167,791	\$179,788	\$43,304	\$32,375	\$55,833	
OREO(3)	18,961	278	568	5,110	15,991	
Other repossessed assets	—	230	—	—	42	
Total	\$186,752	\$180,296	\$43,872	\$37,485	\$71,866	

Edgar Filing: TEXAS CAPITAL BANCSHARES INC/TX - Form 10-K

Restructured loans - accruing	\$—	\$249	\$1,806	\$1,935	\$10,407
Loans past due 90 days and still accruing(4)	\$10,729	\$7,013	\$5,274	\$9,325	\$3,674
Allowance as a multiple of non-performing loans	1.0	x 0.8	x 2.3	x 2.7	x 1.3

43

---

Table of Contents

- If these loans had been current throughout their terms, interest and fees on loans would have increased by
- (1) approximately \$7.9 million, \$7.0 million and \$2.1 million for the years ended December 31, 2016, 2015 and 2014, respectively.
- (2) As of December 31, 2016, 2015 and 2014, non-accrual loans included \$18.1 million, \$24.9 million and \$12.1 million, respectively, in loans that met the criteria for restructured.
- At December 31, 2016, 2015 and 2014, we did not have a valuation allowance recorded against the OREO balance.
- (3) For additional information on OREO, see Note 4 - OREO and Valuation Allowance for Losses on OREO in the accompanying notes to the consolidated financial statements included elsewhere in this report.
- (4) At December 31, 2016, 2015 and 2014, loans past due 90 days and still accruing includes premium finance loans of \$6.8 million, \$6.6 million and \$3.7 million, respectively.

## Allowance for Loan Loss Allocation

(in thousands except percentage data)	December 31, 2016		2015		2014		2013		2012	
	Reserve	% of Loans	Reserve	% of Loans	Reserve	% of Loans	Reserve	% of Loans	Reserve	% of Loans
Loan category:										
Commercial	\$128,768	41 %	\$112,446	40 %	\$70,654	41 %	\$39,868	44 %	\$21,547	41 %
Mortgage finance loans(1)	—	26 %	—	29 %	—	28 %	—	25 %	—	32 %
Construction	13,144	12 %	6,836	11 %	7,935	10 %	14,553	11 %	12,097	7 %
Real estate	19,149	20 %	13,381	19 %	15,582	20 %	24,210	19 %	30,893	19 %
Consumer	241	—	338	—	240	—	149	—	226	—
Equipment leases	1,124	1 %	3,931	1 %	1,141	1 %	3,105	1 %	2,460	1 %
Additional qualitative reserve	5,700	—	4,179	—	5,402	—	5,719	—	7,114	—
Total loans held for investment	\$168,126	100 %	\$141,111	100 %	\$100,954	100 %	\$87,604	100 %	\$74,337	100 %

(1) No amount of the reserve is allocated to these loans based on the internal risk grade assigned.

Increases in the allowance allocated to loan categories at December 31, 2016 compared to December 31, 2015 are due to the growth in the overall loan portfolio, as well as changes in applied risk weights. The increase in allowance allocated to commercial loans recorded at December 31, 2016 compared to 2015 is primarily related to the deterioration in our energy portfolio. During 2016, the total outstandings in our energy portfolio declined from 2015. At December 31, 2016, total energy criticized loans as a percent of the energy portfolio increased to 20% from 16% at December 31, 2015, resulting in a higher allowance allocation. We have traditionally maintained an additional qualitative allowance component 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 additional qualitative allowance at December 31, 2016 was 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 and continued volatility in the energy sector.

## Loans Held for Sale

We launched our MCA business in the third quarter of 2015. In that business, we commit to purchase residential mortgage loans from independent correspondent lenders and deliver those loans into the secondary market via whole loans sales to independent third parties or in securitization transactions to Ginnie Mae and GSEs such as Fannie Mae and Freddie Mac. For additional information on our loans held for sale portfolio, see Note 5 - Certain Transfers of Financial Assets in the accompanying notes to the consolidated financial statements included elsewhere in this report.

## Deposits

We compete for deposits by offering a broad range of products and services to our customers. While this includes offering competitive interest rates and fees, the primary means of competing for deposits is convenience and service to

our customers. However, our strategy to provide service and convenience to customers does not include a large branch network. Our Bank offers thirteen banking centers, courier services and online banking. BankDirect, the Internet division of our Bank, serves its customers on a 24 hours-a-day, 7 days-a-week basis solely through Internet banking.

44

---

Table of Contents

Average deposits for the year ended December 31, 2016 increased \$2.5 billion compared to the same period of 2015. Average demand deposits, interest-bearing transaction deposits and savings deposits increased by \$1.7 billion, \$519.1 million and \$483.3 million, respectively. Average time deposits (excluding deposits in foreign branches) and deposits in foreign branches decreased \$17.3 million and \$181.7 million, respectively. The significant decrease in deposits in foreign branches related to the discontinuation of that deposit offering and closure of our Cayman Islands branch during 2015. The average cost of deposits increased to .22% in 2016 from .17% in 2015 mainly due to the full year effect of the December 2015 increase in interest rates.

Average deposits for the year ended December 31, 2015 increased \$3.9 billion compared to the same period of 2014. Average demand deposits, interest-bearing transaction deposits, savings deposits and time deposits (excluding deposits in foreign branches) increased by \$2.3 billion, \$719.4 million, \$982.0 million and \$93.1 million, respectively. Average deposits in foreign branches decreased \$179.5 million related to the discontinuation of that deposit offering and closure of our Cayman Islands branch during 2015. The average cost of deposits remained level at .17% in 2015 as compared to 2014 mainly due to our focused effort to reduce rates paid on deposits and the significant increase in non-interest-bearing deposits during 2015.

The following table discloses our average deposits for the years ended December 31, 2016, 2015 and 2014 (in thousands):

	Average Balances		
	2016	2015	2014
Non-interest-bearing	\$8,124,174	\$6,447,147	\$4,188,173
Interest-bearing transaction	2,199,292	1,680,220	960,812
Savings	6,403,306	5,920,046	4,938,039
Time deposits	493,128	510,378	417,317
Deposits in foreign branches	—	181,657	361,203
Total average deposits	\$17,219,900	\$14,739,448	\$10,865,544

Uninsured deposits at December 31, 2016 were 54% of total deposits, compared to 56% of total deposits at December 31, 2015 and 72% of total deposits at December 31, 2014. The insured deposit data for 2016, 2015 and 2014 reflect the deposit insurance impact of "combined ownership segregation" of escrow and other accounts at an aggregate level but does not reflect an evaluation of all of the account styling distinctions that would determine the availability of deposit insurance to individual accounts based on FDIC regulations.

At December 31, 2014, we had \$311.1 million in interest-bearing time deposits of \$100,000 or more in our Cayman Islands branch, which was closed during 2015. All deposits in the Cayman Branch came from U.S. based customers of our Bank. Deposits did not originate from foreign sources, and funds transfers neither came from nor went to facilities outside of the U.S. All deposits were in U.S. dollars.

#### Maturity of Domestic CDs and Other Time Deposits in Amounts of \$100,000 or More

(In thousands)	December 31,		
	2016	2015	2014
Months to maturity:			
3 or less	\$160,495	\$240,291	\$160,504
Over 3 through 6	95,482	100,582	77,199
Over 6 through 12	97,761	89,860	103,396
Over 12	17,118	15,714	22,359
Total	\$370,856	\$446,447	\$363,458

Table of Contents

## 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, repurchase 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, formulated and monitored by our senior management and our Balance Sheet Management Committee (“BSMC”), which take into account the demonstrated marketability of our assets, the sources and stability of our 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 years ended December 31, 2016 and 2015, our principal source of funding has been our customer deposits, supplemented by our short-term and long-term borrowings, primarily from Federal funds purchased and Federal Home Loan Bank (“FHLB”) borrowings, generally used to fund mortgage finance assets.

Deposit growth and increases in borrowing capacity related to our mortgage finance loans have resulted in an increase in liquidity assets to \$2.7 billion at December 31, 2016. The following table summarizes the growth in and composition of liquidity assets (in thousands):

	December 31,		
	2016	2015	2014
Federal funds sold and securities purchased under resale agreements	\$25,000	\$55,000	\$—
Interest-bearing deposits	2,700,645	1,626,374	1,233,990
Total liquidity assets	\$2,725,645	\$1,681,374	\$1,233,990

Total liquidity assets as a percent of:

Total loans held for investment, excluding mortgage finance loans	21.0	% 14.3	% 12.2	%
Total loans held for investment	15.6	% 10.1	% 8.7	%
Total earning assets	12.9	% 9.2	% 8.0	%
Total deposits	16.0	% 11.1	% 9.7	%

Our liquidity needs to support growth in loans held for investment have been fulfilled primarily 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 customer relationships, 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 fund temporary differences in the growth in loan balances, including growth in loans held for sale or other specific categories of loans as compared to customer deposits. The following table summarizes our period-end and average year-to-date core customer deposits, relationship brokered deposits and traditional brokered deposits (in millions):



Table of Contents

	December 31,		
	2016	2015	
Deposits from core customers	\$ 15,141.6	\$ 13,743.8	
Deposits from core customers as a percent of total deposits	89.0	% 91.1	%
Relationship brokered deposits	\$ 1,875.2	\$ 1,340.8	
Relationship brokered deposits as a percent of average total deposits	11.0	% 8.9	%
Traditional brokered deposits	\$—	\$—	
Traditional brokered deposits as a percent of total deposits	—	% —	%
Average deposits from core customers	\$ 15,494.0	\$ 13,172.6	
Average deposits from core customers as a percent of average total deposits	90.0	% 89.4	%
Average relationship brokered deposits	\$ 1,725.9	\$ 1,566.8	
Average relationship brokered deposits as a percent of average total deposits	10.0	% 10.6	%
Average traditional brokered deposits	\$—	\$—	
Average traditional brokered deposits as a percent of average total deposits	—	% —	%

We have access to sources of traditional 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 December 31, 2016 increased \$1.9 billion from December 31, 2015.

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 loans, due to their liquidity, short duration and interest spreads available. These borrowing sources 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 borrowings (in thousands):

	December 31,		2015		2014		
	Balance	Rate(3)	Maximum Outstanding at Any Month End	Balance	Rate(3)	Maximum Outstanding at Any Month End	Maximum Outstanding at Any Month End
Federal funds purchased(4)	\$ 101,800	0.80 %		\$ 74,164	0.55 %		
Customer repurchase agreements(1)	7,775	0.05 %		68,887	0.02 %		
FHLB borrowings(2)	2,000,000	0.61 %		1,500,000	0.31 %		
Total borrowings	\$ 2,109,575		\$ 2,117,280	\$ 1,643,051		\$ 1,643,051	\$ 1,192,681

(1) Securities pledged for customer repurchase agreements were \$10.2 million, \$14.2 million and \$21.8 million at December 31, 2016, 2015 and 2014, respectively.

FHLB borrowings are collateralized by a blanket floating lien on certain real estate-secured loans, mortgage finance assets and also certain pledged securities. The weighted-average interest rate for the years ended (2)December 31, 2016, 2015 and 2014 was 0.43%, 0.18% and 0.15%, respectively. The average balance of FHLB borrowings for the years ended December 31, 2016, 2015 and 2014 was \$1.4 billion, \$1.2 billion and \$213.4 million, respectively.

(3) Interest rate as of period end.

The weighted-average interest rate on Federal funds purchased for the years ended December 31, 2016, 2015 and (4)2014 was 0.57%, 0.29% and 0.27%, respectively. The average balance of Federal funds purchased for the years ended December 31, 2016, 2015 and 2014 was \$517.8 million, \$98.8 million and \$139.3 million, respectively.



Table of Contents

The following table summarizes our other borrowing capacities in excess of balances outstanding (in thousands):

	December 31,		
	2016	2015	2014
FHLB borrowing capacity relating to loans	\$3,057,915	\$4,101,396	\$3,602,994
FHLB borrowing capacity relating to securities	1,653	1,213	535
Total FHLB borrowing capacity	\$3,059,568	\$4,102,609	\$3,603,529
Unused Federal funds lines available from commercial banks	\$1,118,000	\$1,231,000	\$1,186,000
Unused Federal Reserve Borrowings capacity	\$3,179,087	\$2,966,702	\$2,643,000

From time to time, we borrow funds on an overnight basis from the Federal Reserve. We did not incur such borrowings during 2016, 2015 or 2014.

Our unsecured, revolving, non-amortizing line of credit had maximum availability of \$130.0 million and matured on December 21, 2016. This line of credit was renewed on December 20, 2016 with a new maximum availability of \$130.0 million and a maturity date of December 19, 2017. 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. No borrowings were outstanding as of December 31, 2016 or December 31, 2015. The average borrowings during the year ended December 31, 2016 were \$6.8 million compared to none during the year ended December 31, 2015.

From November 2002 to September 2006 various Texas Capital Statutory Trusts were created and subsequently issued floating rate trust preferred securities in various private offerings totaling \$113.4 million. After deducting underwriter compensation and other expenses of each offering, the net proceeds were available to the Company to increase capital and for general corporate purposes, including use in investment and lending activities. Interest payments on all trust preferred subordinated debentures are deductible for federal income tax purposes. As of December 31, 2016, the weighted average quarterly rate on the trust preferred subordinated debentures was 2.83%, compared to 2.65% average for all of 2016, and 2.25% for all of 2015.

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. Our equity capital averaged \$1.7 billion for the year ended December 31, 2016 as compared to \$1.6 billion in 2015 and \$1.3 billion 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.

On December 2, 2016, we completed a sale of 3.45 million shares of our common stock in a public offering. Net proceeds from the sale totaled \$236.4 million. The additional equity will be used for general corporate purposes, including repayment of \$20.0 million of short-term debt and as additional capital to support continued loan growth. For additional information on our capital and stockholders' equity, see Note 14 - Regulatory Restrictions and Note 21 - Stockholders' Equity in the accompanying notes to the consolidated financial statements included elsewhere in this report.

**Commitments and Contractual Obligations**

The following table presents, as of December 31, 2016, significant fixed and determinable contractual 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. Further discussion of the nature of each obligation is included in the referenced note to the consolidated financial statements elsewhere in this Form 10-K.

(In thousands)	Note Reference	Within One Year	After One But After Three			Total
			Within Three Years	But Within Five Years	After Five Years	
Deposits without a stated maturity(1)	8	\$16,574,212	\$ —	\$ —	\$ —	\$16,574,212
Time deposits(1)	8	417,911	22,836	1,872	—	442,619
Federal funds purchased and customer repurchase agreements(1)	9	109,575	—	—	—	109,575
FHLB borrowings(1)	9	2,000,000	—	—	—	2,000,000

Edgar Filing: TEXAS CAPITAL BANCSHARES INC/TX - Form 10-K

Operating lease obligations(1)(2)	17	16,243	33,214	28,775	30,375	108,607
Subordinated notes(1)	9	—	—	—	281,044	281,044
Trust preferred subordinated debentures(1)	9, 10	—	—	—	113,406	113,406
Total contractual obligations(1)		\$19,117,941	\$ 56,050	\$ 30,647	\$424,825	\$19,629,463

(1) Excludes interest.

(2) Non-balance sheet item.

Off-Balance Sheet Arrangements

In addition to the off-balance sheet obligations described under the caption "Loans Held for Sale," we have the following off-balance sheet contractual obligations as of December 31, 2016 (in thousands):

	Within One Year	After One But Within Three Years	After Three But Within Five Years	After Five Years	Total
Commitments to extend credit	\$2,070,329	\$ 2,581,452	\$ 910,638	\$ 141,962	\$5,704,381
Standby and commercial letters of credit	135,569	29,495	6,152	50	171,266
Total financial instruments with off-balance sheet risk	\$2,205,898	\$ 2,610,947	\$ 916,790	\$ 142,012	\$5,875,647

Due to the nature of our unfunded loan commitments, including unfunded lines of credit, the amounts presented in the table above do not necessarily represent amounts that we anticipate funding in the periods presented above.

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 - Operations and Summary of Significant Accounting Policies in the accompanying notes to the consolidated financial statements included elsewhere in this report. Not all significant accounting policies require management to make difficult, subjective or complex judgments. However, the policy noted below could be deemed to meet the SEC's definition of a critical accounting policy.

## Table of Contents

### Allowance for Loan Losses

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 Accounting Standards Codification (“ASC”) 310, Receivables, and ASC 450, Contingencies. The allowance for loan losses is established through a provision for credit 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 allowance, 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” above and Note 3 – Loans Held for Investment 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.

### New Accounting Standards

See Note 23 – New Accounting Standards in the accompanying notes to the consolidated financial statements included elsewhere in this report for details of recently issued accounting pronouncements and their expected impact on our financial statements.

### ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURE 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 and 2015, and prices have continued to be suppressed through 2016. Such declines in commodity prices have and, if continued, could negatively impact our energy clients' ability to perform on their loan obligations. Management does not currently expect the current decline in 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 plus or minus 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. Oversight of our compliance with these guidelines is the ongoing responsibility of the BSMC, with exceptions reported to the Risk Management Committee, and to our board of directors if deemed necessary, 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 December 31, 2016, 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

49

---

Table of Contents

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.

## Interest Rate Sensitivity Gap Analysis

December 31, 2016

(in thousands)	0-3 mo Balance	4-12 mo Balance	1-3 yr Balance	3+ yr Balance	Total Balance
<b>Assets:</b>					
Securities(1)	\$6,214	\$6,769	\$1,920	\$9,971	\$24,874
Total variable loans	16,013,070	69,966	—	—	16,083,036
Total fixed loans	436,713	1,148,873	576,093	294,122	2,455,801
Total loans(2)	16,449,783	1,218,839	576,093	294,122	18,538,837
Total interest sensitive assets	\$16,455,997	\$1,225,608	\$578,013	\$304,093	\$18,563,711
<b>Liabilities</b>					
Interest-bearing customer deposits	\$8,580,011	\$—	\$—	\$—	\$8,580,011
CDs & IRAs	186,191	231,720	22,836	1,872	442,619
Total interest-bearing deposits	8,766,202	231,720	22,836	1,872	9,022,630
Repurchase agreements, Federal funds purchased, FHLB borrowings	2,109,575	—	—	—	2,109,575
Subordinated notes	—	—	—	281,044	281,044
Trust preferred subordinated debentures	—	—	—	113,406	113,406
Total borrowings	2,109,575	—	—	394,450	2,504,025
Total interest sensitive liabilities	\$10,875,777	\$231,720	\$22,836	\$396,322	\$11,526,655
GAP	\$5,580,220	\$993,888	\$555,177	\$(92,229)	\$—
Cumulative GAP	5,580,220	6,574,108	7,129,285	7,037,056	7,037,056
Demand deposits					\$7,994,201
Stockholders' equity					2,009,557
Total					\$10,003,758

(1) Securities based on fair market value.

(2) Loans are stated at gross.

The table above sets forth the balances as of December 31, 2016 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 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; the prime lending rate and the 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. These are our primary interest rate exposures. We

are currently not using derivatives to manage our interest rate exposure.

50

---



Table of Contents

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 2015 and 2016, 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.

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, 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			
December 31, 2016		December 31, 2015	
100 bps Increase	200 bps Increase	100 bps Increase	200 bps Increase

Change in net interest income	\$ 124,583	\$ 254,308	\$ 85,334	\$ 178,066
-------------------------------	------------	------------	-----------	------------

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 will 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.

Table of Contents

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Index to Consolidated Financial Statements

	Page Reference
<u>Report of Independent Registered Public Accounting Firm</u>	<u>53</u>
<u>Consolidated Balance Sheets — December 31, 2016 and December 31, 2015</u>	<u>54</u>
<u>Consolidated Statements of Income and Other Comprehensive Income — Years ended December 31, 2016, 2015 and 2014</u>	<u>55</u>
<u>Consolidated Statements of Stockholders' Equity — Years ended December 31, 2016, 2015 and 2014</u>	<u>56</u>
<u>Consolidated Statements of Cash Flows — Years ended December 31, 2016, 2015 and 2014</u>	<u>57</u>
<u>Notes to Consolidated Financial Statements</u>	<u>58</u>

52

---

Table of Contents

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders of  
Texas Capital Bancshares, Inc.

We have audited the accompanying consolidated balance sheets of Texas Capital Bancshares, Inc. (the Company) as of December 31, 2016 and 2015, and the related consolidated statements of income and other comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2016. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Texas Capital Bancshares, Inc. at December 31, 2016 and 2015, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2016, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Texas Capital Bancshares, Inc.'s internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated February 17, 2017 expressed an unqualified opinion thereon.

Dallas, Texas  
February 17, 2017

Table of ContentsTEXAS CAPITAL BANCSHARES, INC.  
CONSOLIDATED BALANCE SHEETS

(in thousands except per share data)	December 31,	
	2016	2015
Assets		
Cash and due from banks	\$113,707	\$109,496
Interest-bearing deposits	2,700,645	1,626,374
Federal funds sold and securities purchased under resale agreements	25,000	55,000
Securities, available-for-sale	24,874	29,992
Loans held for sale, at fair value	968,929	86,075
Loans held for investment, mortgage finance	4,497,338	4,966,276
Loans held for investment (net of unearned income)	13,001,011	11,745,674
Less: Allowance for loan losses	168,126	141,111
Loans held for investment, net	17,330,223	16,570,839
Mortgage servicing rights, net	28,536	423
Premises and equipment, net	19,775	23,561
Accrued interest receivable and other assets	465,933	382,101
Goodwill and intangible assets, net	19,512	19,960
Total assets	\$21,697,134	\$18,903,821
Liabilities and Stockholders' Equity		
Liabilities:		
Deposits:		
Non-interest-bearing	\$7,994,201	\$6,386,911
Interest-bearing	9,022,630	8,697,708
Total deposits	17,016,831	15,084,619
Accrued interest payable	5,498	5,097
Other liabilities	161,223	153,433
Federal funds purchased and repurchase agreements	109,575	143,051
Other borrowings	2,000,000	1,500,000
Subordinated notes, net	281,044	280,682
Trust preferred subordinated debentures	113,406	113,406
Total liabilities	19,687,577	17,280,288
Stockholders' equity:		
Preferred stock, \$.01 par value, \$1,000 liquidation value:		
Authorized shares—10,000,000		
Issued shares—6,000,000 shares issued at December 31, 2016 and 2015	150,000	150,000
Common stock, \$.01 par value:		
Authorized shares—100,000,000		
Issued shares—49,504,079 and 45,874,224 at December 31, 2016 and 2015, respectively	495	459
Additional paid-in capital	955,468	714,546
Retained earnings	903,187	757,818
Treasury stock (shares at cost: 417 at December 31, 2016 and 2015)	(8	) (8
Accumulated other comprehensive income, net of taxes	415	718
Total stockholders' equity	2,009,557	1,623,533
Total liabilities and stockholders' equity	\$21,697,134	\$18,903,821
See accompanying notes to consolidated financial statements.		



Table of Contents

TEXAS CAPITAL BANCSHARES, INC.  
CONSOLIDATED STATEMENTS OF INCOME AND OTHER  
COMPREHENSIVE INCOME

(In thousands except per share data)	Year ended December 31,		
	2016	2015	2014
Interest income			
Interest and fees on loans	\$684,582	\$594,729	\$511,606
Securities	967	1,254	1,828
Federal funds sold and securities purchased under resale agreements	1,547	682	207
Deposits in other banks	16,312	6,293	906
Total interest income	703,408	602,958	514,547
Interest expense			
Deposits	37,175	24,578	18,145
Federal funds purchased	518	284	373
Repurchase agreements	9	19	17
Other borrowings	6,119	2,232	356
Subordinated notes	16,764	16,764	16,202
Trust preferred subordinated debentures	3,009	2,551	2,489
Total interest expense	63,594	46,428	37,582
Net interest income	639,814	556,530	476,965
Provision for credit losses	77,000	53,250	22,000
Net interest income after provision for credit losses	562,814	503,280	454,965
Non-interest income			
Service charges on deposit accounts	10,341	8,323	7,253
Trust fee income	4,268	5,022	4,937
Bank owned life insurance (BOLI) income	2,073	2,011	2,067
Brokered loan fees	25,339	18,661	13,981
Swap fees	2,866	4,275	2,992
Other	15,893	9,446	11,281
Total non-interest income	60,780	47,738	42,511
Non-interest expense			
Salaries and employee benefits	228,985	192,610	169,051
Net occupancy expense	23,221	23,182	20,866
Marketing	17,303	16,491	15,989
Legal and professional	23,326	22,150	21,182
Communications and technology	25,562	21,425	18,667
FDIC insurance assessment	24,440	17,231	10,919
Allowance and other carrying costs for OREO	824	22	85
Other	38,736	33,412	28,355
Total non-interest expense	382,397	326,523	285,114
Income before income taxes	241,197	224,495	212,362
Income tax expense	86,078	79,641	76,010
Net income	155,119	144,854	136,352
Preferred stock dividends	9,750	9,750	9,750
Net income available to common stockholders	\$145,369	\$135,104	\$126,602
Other comprehensive gain (loss)			
Change in unrealized gain on available-for-sale securities arising during period, before tax	\$(467)	\$(877)	\$(522)
Income tax benefit related to unrealized loss on available-for-sale securities	(164)	(306)	(183)

Edgar Filing: TEXAS CAPITAL BANCSHARES INC/TX - Form 10-K

Other comprehensive loss net of tax	(303	)	(571	)	(339	)
Comprehensive income	\$154,816		\$144,283		\$136,013	
Basic earnings per common share	\$3.14		\$2.95		\$2.93	
Diluted earnings per common share	\$3.11		\$2.91		\$2.88	

See accompanying notes to consolidated financial statements.

55

---

Table of ContentsTEXAS CAPITAL BANCSHARES, INC.  
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(In thousands except share data)	Preferred Stock		Common Stock		Additional	Retained	Treasury	Accumulated		Total
	Shares	Amount	Shares	Amount	Paid-in Capital		Stock	Other Comprehensive Income		
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	—	—	—	—	—	136,352	—	—	—	136,352
Change in unrealized gain (loss) on available-for-sale securities, net of taxes of \$183	—	—	—	—	—	—	—	—	(339)	(339)
Total comprehensive income										136,013
Tax expense related to exercise of stock-based awards	—	—	—	—	2,929	—	—	—	—	2,929
Stock-based compensation expense recognized in earnings	—	—	—	—	4,628	—	—	—	—	4,628
Preferred stock dividend	—	—	—	—	—	(9,750)	—	—	—	(9,750)
Issuance of stock related to stock-based awards	—	—	201,280	2	(2,205)	—	—	—	—	(2,203)
Issuance of common stock	—	—	4,398,128	44	256,179	—	—	—	—	256,223
Issuance of stock related to warrants	—	—	99,229	1	(1)	—	—	—	—	—
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	—	—	—	—	—	144,854	—	—	—	144,854
Change in unrealized gain	—	—	—	—	—	—	—	—	(571)	(571)



(loss) on available-for-sale securities, net of taxes of \$306										
Total comprehensive income										144,283
Tax expense related to exercise of stock-based awards	—	—	—	—	1,452	—	—	—	—	1,452
Stock-based compensation expense recognized in earnings	—	—	—	—	4,597	—	—	—	—	4,597
Preferred stock dividend	—	—	—	—	—	(9,750)	—	—	—	(9,750)
Issuance of stock related to stock-based awards	—	—	138,800	2	(1,241)	—	—	—	—	(1,239)
Balance at December 31, 2015	6,000,000	150,000	45,874,224	459	714,546	757,818	(417)	(8)	718	1,623,533
Comprehensive income:										
Net income	—	—	—	—	—	155,119	—	—	—	155,119
Change in unrealized gain (loss) on available-for-sale securities, net of taxes of \$164	—	—	—	—	—	—	—	—	(303)	(303)
Total comprehensive income										154,816
Tax expense related to exercise of stock-based awards	—	—	—	—	1,879	—	—	—	—	1,879
Stock-based compensation expense recognized in earnings	—	—	—	—	5,093	—	—	—	—	5,093
Preferred stock dividend	—	—	—	—	—	(9,750)	—	—	—	(9,750)
Issuance of common stock related to	—	—	172,459	1	(2,482)	—	—	—	—	(2,481)

stock-based awards										
Issuance of common stock	—	—	3,450,000	35	236,432	—	—	—	—	236,467
Issuance of stock related to warrants	—	—	7,396	—	—	—	—	—	—	—
Balance at December 31, 2016	6,000,000	\$150,000	49,504,079	\$495	\$955,468	\$903,187	(417)	\$(8)	\$415	\$2,009,557

See accompanying notes to consolidated financial statements.

Table of ContentsTEXAS CAPITAL BANCSHARES, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)	Year ended December 31,		
	2016	2015	2014
Operating activities			
Net income	\$155,119	\$144,854	\$136,352
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for credit losses	77,000	53,250	22,000
Deferred tax expense (benefit)	(2,946 )	(3,561 )	(3,969 )
Depreciation and amortization	21,814	16,495	14,798
BOLI income	(2,073 )	(2,011 )	(2,067 )
Stock-based compensation expense	13,578	12,304	14,577
Excess tax benefits from stock-based compensation arrangements	(2,013 )	(1,499 )	(2,929 )
Purchases of loans held for sale	(3,327,482 )	(127,002 )	—
Proceeds from sales and repayments of loans held for sale	2,405,592	40,490	—
(Gain) loss on sale of loans held for sale and other assets	(2,519 )	179	(822 )
Changes in operating assets and liabilities:			
Accrued interest receivable and other assets	(59,787 )	(61,002 )	(58,579 )
Accrued interest payable and other liabilities	(2,576 )	(3,554 )	38,366
Net cash provided by (used in) operating activities	(726,293 )	68,943	157,727
Investing activities			
Purchases of available-for-sale securities	(1,760 )	—	—
Maturities and calls of available-for-sale securities	555	2,430	11,150
Principal payments received on available-for-sale securities	5,856	8,419	9,822
Originations of mortgage finance loans	(100,574,326)	(86,342,672)	(58,090,177)
Proceeds from pay-offs of mortgage finance loans	101,043,264	85,478,521	56,772,317
Net increase in loans held for investment, excluding mortgage finance loans	(1,321,733 )	(1,603,880 )	(1,676,927 )
Purchase of premises and equipment, net	(2,176 )	(5,034 )	(15,732 )
Proceeds from sale of foreclosed assets	110	1,430	5,877
Net cash used in investing activities	(850,210 )	(2,460,786 )	(2,983,670 )
Financing activities			
Net increase in deposits	1,932,212	2,411,319	3,415,921
Costs from issuance of stock related to stock-based awards and warrants	(2,481 )	(1,239 )	(2,203 )
Net proceeds from issuance of common stock	236,467	—	256,223
Preferred dividends paid	(9,750 )	(9,750 )	(9,750 )
Net increase (decrease) in other borrowings	500,000	399,995	244,979
Excess tax benefits from stock-based compensation arrangements	2,013	1,499	2,929
Net increase (decrease) in Federal funds purchased and repurchase agreements	(33,476 )	50,375	(77,928 )
Issuance of subordinated notes	—	—	172,375
Net cash provided by financing activities	2,624,985	2,852,199	4,002,546
Net increase (decrease) in cash and cash equivalents	1,048,482	460,356	1,176,603
Cash and cash equivalents at beginning of period	1,790,870	1,330,514	153,911
Cash and cash equivalents at end of period	\$2,839,352	\$1,790,870	\$1,330,514
Supplemental disclosures of cash flow information:			
Cash paid during the period for interest	\$63,193	\$46,078	\$33,584
Cash paid during the period for income taxes	88,262	87,450	74,998
Transfers from loans/leases to OREO and other repossessed assets	18,822	1,267	851
See accompanying notes to consolidated financial statements.			



## Table of Contents

### (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 are primarily a secured lender and 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.

#### 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.

#### 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, the fair value of mortgage servicing rights ("MSRs") and the status of contingencies are particularly susceptible to significant change in the near term.

#### Cash and Cash Equivalents

Cash equivalents include amounts due from banks, interest-bearing deposits and Federal funds sold.

#### Securities

Securities are classified as trading, available-for-sale or held-to-maturity. Management classifies securities at the time of purchase and re-assesses such designation at each balance sheet date; however, transfers between categories from this re-assessment are rare.

#### Trading Account

Securities acquired for resale in anticipation of short-term market movements are classified as trading, with realized and unrealized gains and losses recognized in income. To date, we have not had any activity in our trading account.

#### Available-for-Sale

Debt securities are classified as held-to-maturity when we have the positive intent and ability to hold the securities to maturity. Held-to-maturity securities are stated at amortized cost. Debt securities not classified as held-to-maturity or trading and marketable equity securities not classified as trading are classified as available-for-sale.

Available-for-sale securities are stated at fair value, with the unrealized gains and losses reported in a separate component of accumulated other comprehensive income (loss), net of tax. The amortized cost of debt securities is adjusted for amortization of premiums and accretion of discounts to maturity, or in the case of mortgage-backed securities, over the estimated life of the security. Such amortization and accretion is included in interest income from securities. 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.

All securities are available-for-sale as of December 31, 2016 and 2015.

#### Loans

##### Loans Held for Sale

Through our MCA program, we commit to purchase residential mortgage loans from independent correspondent lenders and deliver those loans into the secondary market via whole loan sales to independent third parties or in securitization transactions to third parties such as Ginnie Mae or to GSEs such as Fannie Mae or Freddie Mac. In some cases, we retain the mortgage servicing rights. Once purchased, these loans are classified as held for sale and are carried at fair value pursuant to our election of the fair value option in accordance with Accounting Standards Codification 825, Financial Instruments ("ASC 825"). At the commitment date, we enter into a corresponding forward sale commitment with a third party, typically Ginnie Mae or a GSE, to deliver the loans within a specified timeframe. The estimated gain/loss for the entire transaction (from initial purchase commitment to final delivery of loans) is

recorded as an asset or liability. Fair value is derived from observable current market prices, when available, and includes the fair value of the mortgage servicing rights. Adjustments to reflect unrealized gains and

58

---

## Table of Contents

losses resulting from changes in fair value and realized gains and losses upon ultimate sale of the loans are classified as other non-interest income in the consolidated statements of income and other comprehensive income.

### Loans Held for Investment

Loans held for investment (which include equipment leases accounted for as financing leases) are stated at the amount of unpaid principal reduced by deferred income (net of costs). Interest on loans is recognized using the simple-interest method on the daily balances of the principal amounts outstanding. Loan origination fees, net of direct loan origination costs, and commitment fees, are deferred and amortized as an adjustment to yield over the life of the loan, or over the commitment period, as applicable.

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. Reserves on impaired loans are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the underlying collateral, less cost to sell. Impaired loans, or portions thereof, are charged off when a confirmed loss exists.

The accrual of interest on loans is discontinued 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 book balance of the asset is deemed to be 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.

Loans held for investment includes legal ownership interests in mortgage loans that we purchase through our mortgage warehouse lending division. The ownership interests are purchased from unaffiliated mortgage originators who are seeking additional funding through sale of the undivided ownership interests to facilitate their ability to originate loans. The mortgage originator has no obligation to offer and we have no obligation to purchase these interests. The originator closes mortgage loans consistent with underwriting standards established by approved investors, and, at the time of the sale to the investor, our ownership interest and that of the originator are delivered by us to the investor selected by the originator and approved by us. We typically purchase up to a 99% ownership interest in each mortgage with the originator owning the remaining percentage. These mortgage ownership interests are generally held by us for a period of less than 30 days and more typically 10-20 days. Because of conditions in agreements with originators designed to reduce transaction risks, under ASC 860, Transfers and Servicing of Financial Assets ("ASC 860"), the ownership interests do not qualify as participating interests. Under ASC 860, the ownership interests are deemed to be loans to the originators and payments we receive from investors are deemed to be payments made by or on behalf of the originator to repay the loan deemed made to the originator. Because we have an actual, legal ownership interest in the underlying residential mortgage loan, these interests are not extensions of credit to the originators that are secured by the mortgage loans as collateral.

Due to market conditions or events of default by the investor or the originator, we could be required to purchase the remaining interests in the mortgage loans and hold them beyond the expected 10-20 days. Mortgage loans acquired under these conditions would require mark-to-market adjustments to income and could require future allocations of the allowance for loan losses or be subject to charge off in the event the loans become impaired. Mortgage loan interests purchased and disposed of as expected receive no allocation of the allowance for loan losses due to the minimal loss experience with these assets.

### Allowance for Loan Losses

The allowance for loan losses is comprised of specific reserves for impaired loans and an additional qualitative reserve based on our estimate of losses inherent in the portfolio at the balance sheet date, but not yet identified with specified loans. We regularly evaluate our allowance for loan losses to maintain an appropriate level to absorb estimated loan losses inherent in the loan portfolio. Factors contributing to the determination of the allowance 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 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.



## Table of Contents

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 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 inappropriately protected by 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 highly questionable and improbable. The possibility of loss is extremely high. All doubtful loans are on non-accrual. The allowance 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 allowance considers the results of reviews performed by third party reviewers as reflected in their confirmations of assigned credit grades within the portfolio. 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 Bank's maintaining an additional qualitative 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 additional qualitative 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. The methodology used in the periodic review of the appropriateness of the allowance, 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 allowance 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 appropriateness of the allowance 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.

### Other Real Estate Owned

Other real estate owned ("OREO"), which is included in other assets on the consolidated balance sheet, consists of real estate that has been foreclosed. Real estate that has been foreclosed is recorded at the fair value of the real estate, less selling costs, through a charge to the allowance for loan losses, if necessary. Subsequent write-downs required for declines in value are recorded through a valuation allowance, or taken directly to the asset, charged to other non-interest expense.

### Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, which range from three to ten years. Gains or losses on disposals of premises and equipment are included in results of operations.

### Marketing and Software

Marketing costs are expensed as incurred. Ongoing maintenance and enhancements of websites are expensed as incurred. Costs incurred in connection with development or purchase of internal use software are capitalized and

amortized over a period not to exceed five years. Internal use software costs are included in other assets in the consolidated balance sheets.

**Goodwill and Other Intangible Assets**

Intangible assets are acquired assets that lack physical substance but can be distinguished from goodwill because of contractual or other legal rights or because the asset is capable of being sold or exchanged either on its own or in combination with a related contract, asset, or liability. Our intangible assets relate primarily to loan customer relationships. Intangible assets with definite useful lives are amortized on an accelerated basis over their estimated life. Goodwill and intangible assets are tested for impairment during the fourth quarter on an annual basis or whenever events or changes in circumstances indicate the carrying

## Table of Contents

amount of the assets may not be recoverable from future undiscounted cash flows. If impaired, the assets are recorded at fair value.

### Segment Reporting

We have determined that all of our lending divisions and subsidiaries meet the aggregation criteria of ASC 280, Segment Reporting, since all offer similar products and services, operate with similar processes, and have similar customers.

### Stock-based Compensation

We account for all stock-based compensation transactions in accordance with ASC 718, Compensation — Stock Compensation (“ASC 718”), which requires that stock compensation transactions be recognized as compensation expense in the consolidated statement of income and other comprehensive income based on their fair values on the measurement date, which is the date of the grant.

### Accumulated Other Comprehensive Income

Unrealized gains or losses on our available-for-sale securities (after applicable income tax expense or benefit) are included in accumulated other comprehensive income, net. Accumulated other comprehensive income (loss), net for the three years ended December 31, 2016 is reported in the accompanying consolidated statements of stockholders’ equity and consolidated statements of income and other comprehensive income.

### Income Taxes

The Company and its subsidiary file a consolidated federal income tax return. We utilize the liability method in accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based upon the difference between the values of the assets and liabilities as reflected in the financial statements and their related tax basis using enacted tax rates in effect for the year in which the differences are expected to be recovered or settled. As changes in tax law or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. A valuation allowance is provided against deferred tax assets unless it is more likely than not that such deferred tax assets will be realized.

### Basic and Diluted Earnings Per Common Share

Basic earnings per common share is based on net income available to common stockholders divided by the weighted-average number of common shares outstanding during the period excluding non-vested stock. Diluted earnings per common share include the dilutive effect of stock options and non-vested stock awards granted using the treasury stock method. A reconciliation of the weighted-average shares used in calculating basic earnings per common share and the weighted average common shares used in calculating diluted earnings per common share for the reported periods is provided in Note 15 — Earnings Per Share.

### Fair Values of Financial Instruments

ASC 820, Fair Value Measurements and Disclosures (“ASC 820”), defines fair value, establishes a framework for measuring fair value under GAAP and enhances disclosures about fair value measurements. In general, fair values of financial instruments are based upon quoted market prices, where available. If such quoted market prices are not available, fair value is 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.

### Mortgage Servicing Rights

Mortgage servicing rights are created by selling purchased or originated mortgage loans with servicing rights retained. We identify classes of servicing rights based upon the nature of the underlying assumptions used to value the asset along with the risks associated with the underlying asset. Based upon these criteria we have one class of MSR, residential.

Originated MSR are recognized based on the estimated fair value of the mortgage loans and the related servicing rights at the date of sale using values derived from a valuation model managed by a third party. MSR are amortized proportionally over the estimated life of the projected net servicing revenue and are periodically evaluated for impairment. MSR are reported on the consolidated balance sheets at lower of cost or market. Loan servicing fee income represents income earned for servicing mortgage loans owned by investors and includes mortgage servicing fees and other ancillary servicing income. Servicing fees are recorded as income when earned and are reported in other non-interest income on the consolidated statements of income and other comprehensive income. For additional

information on MSRs, see Note 5 - Certain Transfers of Financial Assets.

61

---

Table of Contents

## Financial Instruments with Off-Balance Sheet Risk

The Company has undertaken certain guarantee obligations in the ordinary course of business. These guarantees include liabilities with both balance sheet and off-balance sheet risk. We consider the following arrangements to be guarantees: commitments to extend credit, standby letters credit and indemnification agreements included within third party contractual arrangements. For additional information on commitments and contingencies, see Note 13 - Financial Instruments with Off-Balance Sheet Risk.

## Derivative Financial Instruments

All contracts that satisfy the definition of a derivative are recorded at fair value in other assets and other liabilities in the consolidated balance sheets. We record the derivatives 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. For additional information on derivative financial instruments, see Note 20 - Derivative Financial Instruments.

## (2) Securities

The following is a summary of securities (in thousands):

	December 31, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale securities:				
Residential mortgage-backed securities	\$ 14,680	\$ 972	\$ —	\$ 15,652
Municipals	275	—	—	275
Equity securities(1)	9,280	27	(360 )	8,947
	\$ 24,235	\$ 999	\$ (360 )	\$ 24,874

	December 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Available-for-sale securities:				
Residential mortgage-backed securities	\$ 20,536	\$ 1,365	\$ —	\$ 21,901
Municipals	828	3	—	831
Equity securities(1)	7,522	11	(273 )	7,260
	\$ 28,886	\$ 1,379	\$ (273 )	\$ 29,992

(1) Equity securities consist of Community Reinvestment Act funds and investments related to our non-qualified deferred compensation plan.

Table of Contents

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

	December 31, 2016				
	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	\$9	\$ 2,047	\$ 3,147	\$ 9,477	\$ 14,680
Estimated fair value	9	2,104	3,495	10,044	15,652
Weighted average yield(3)	5.50%	4.70 %	5.55 %	2.84 %	3.68 %
Municipals:(2)					
Amortized cost	275	—	—	—	275
Estimated fair value	275	—	—	—	275
Weighted average yield(3)	5.6%	— %	— %	— %	5.61 %
Equity securities:(4)					
Amortized cost	9,280	—	—	—	9,280
Estimated fair value	8,947	—	—	—	8,947
Total available-for-sale securities:					
Amortized cost					\$24,235
Estimated fair value					\$24,874
	December 31, 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	\$214	\$ 4,655	\$ 4,265	\$ 11,402	\$ 20,536
Estimated fair value	217	4,837	4,747	12,100	21,901
Weighted average yield(3)	5.62 %	4.71 %	5.54 %	2.53 %	3.75 %
Municipals:(2)					
Amortized cost	265	563	—	—	828
Estimated fair value	265	566	—	—	831
Weighted average yield(3)	5.46 %	5.69 %	— %	— %	5.79 %
Equity securities:(4)					
Amortized cost	7,522	—	—	—	7,522
Estimated fair value	7,260	—	—	—	7,260
Total available-for-sale securities:					
Amortized cost					\$28,886
Estimated fair value					\$29,992

Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay (1) obligations with or without prepayment penalties. The average expected life of the mortgage-backed securities was 1.1 years at December 31, 2016 and 0.8 years at December 31, 2015.

(2) Yields have been adjusted to a tax equivalent basis assuming a 35% federal tax rate.

(3) Yields are calculated based on amortized cost.



Table of Contents

(4) These equity securities do not have a stated maturity.

Securities with carrying values of approximately \$13.6 million and \$20.7 million were pledged to secure certain borrowings and deposits at December 31, 2016 and 2015, respectively. See Note 9 — Borrowing Arrangements for discussion of securities securing borrowings. Of the pledged securities at December 31, 2016 and 2015, approximately \$3.4 million and \$6.6 million, respectively, were pledged for certain deposits.

The following table discloses, as of December 31, 2016 and December 31, 2015, 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):

December 31, 2016	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Equity securities	\$1,015	\$ (6 )	\$6,146	\$ (354 )	\$7,161	\$ (360 )

December 31, 2015	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
Equity securities	\$—	\$ —	\$6,227	\$ (273 )	\$6,227	\$ (273 )

Equity securities \$— \$ — \$6,227 \$ (273 ) \$6,227 \$ (273 )

At December 31, 2016 we owned two securities with an unrealized loss position and one at December 31, 2015. These securities are publicly traded equity funds and are subject to market pricing volatility. We do not believe that this unrealized loss is “other than temporary.” We have evaluated the near-term prospects of the investments in relation to the severity and duration of the impairment and based on that evaluation have the ability and intent to hold the investments until recovery of fair value.

Unrealized gains or losses on our available-for-sale securities (after applicable income tax expense or benefit) are included in accumulated other comprehensive income, net. We had comprehensive income of \$154.8 million for the year ended December 31, 2016 and comprehensive income of \$144.3 million for the year ended December 31, 2015.

### (3) Loans Held for Investment and Allowance for Loan Losses

Loans held for investment are summarized by category as follows (in thousands):

	December 31,	
	2016	2015
Commercial	\$7,291,545	\$6,672,631
Mortgage finance	4,497,338	4,966,276
Construction	2,098,706	1,851,717
Real estate	3,462,203	3,139,197
Consumer	34,587	25,323
Equipment leases	185,529	113,996
Gross loans held for investment	17,569,908	16,769,140
Deferred income (net of direct origination costs)	(71,559 )	(57,190 )
Allowance for loan losses	(168,126 )	(141,111 )
Total loans held for investment	\$17,330,223	\$16,570,839

**Commercial Loans and Leases.** Our commercial loan 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 transaction 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, or more frequently, as needed, and are supported by accounts receivable, inventory, equipment and other assets of our clients' businesses.

64

---

Table of Contents

**Mortgage Finance Loans.** Our mortgage finance loans consist of ownership interests purchased in single-family residential mortgages funded through our mortgage finance group. These loans are typically held 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. December 31, 2016 and 2015 balances are stated net of \$839.0 million and \$454.8 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 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 and the impact of the inability of potential purchasers and lessees to obtain financing and a lack of transactions at comparable values.

At December 31, 2016 and 2015, we had a blanket floating lien on certain real estate-secured loans, mortgage finance loans and also certain securities used as collateral for FHLB borrowings.

**Summary of Loan Losses**

The allowance for loan losses is comprised of specific reserves for impaired loans and an additional qualitative reserve based on our estimate of losses inherent in the portfolio at the balance sheet date, but not yet identified with specified loans. We consider the allowance at December 31, 2016 to be appropriate, given management's assessment of losses inherent in the portfolio as of the evaluation date, the significant growth in the loan and lease portfolio, current economic conditions in our market areas and other factors.

Table of Contents

The following tables summarize the credit risk profile of our loan portfolio by internally assigned grades and non-accrual status as of December 31, 2016 and 2015 (in thousands):

	Commercial	Mortgage Finance	Construction	Real Estate	Consumer	Equipment Leases	Total
December 31, 2016							
Grade:							
Pass	\$6,941,310	\$4,497,338	\$2,074,859	\$3,430,346	\$34,249	\$181,914	\$17,160,016
Special mention	69,447	—	10,901	21,932	—	3,532	105,812
Substandard- accruing	115,848	—	12,787	7,516	138	—	136,289
Non-accrual	164,940	—	159	2,409	200	83	167,791
Total loans held for investment	\$7,291,545	\$4,497,338	\$2,098,706	\$3,462,203	\$34,587	\$185,529	\$17,569,908

	Commercial	Mortgage Finance	Construction	Real Estate	Consumer	Equipment Leases	Total
December 31, 2015							
Grade:							
Pass	\$6,375,332	\$4,966,276	\$1,821,678	\$3,085,463	\$25,093	\$103,560	\$16,377,402
Special mention	111,911	—	13,090	30,585	3	334	155,923
Substandard-accruing	46,731	—	281	3,837	227	4,951	56,027
Non-accrual	138,657	—	16,668	19,312	—	5,151	179,788
Total loans held for investment	\$6,672,631	\$4,966,276	\$1,851,717	\$3,139,197	\$25,323	\$113,996	\$16,769,140

Table of Contents

The following tables detail activity in the allowance for loan losses by portfolio segment for the years ended December 31, 2016 and 2015 (in thousands). Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

	Commercial	Mortgage Finance	Construction	Real Estate	Consumer	Equipment Leases	Additional Qualitative Reserve	Total
December 31, 2016								
Allowance for loan losses								
Beginning balance	\$ 112,446	\$ -6,836	\$ 13,381	\$ 338	\$ 3,931	\$ 4,179		\$ 141,111
Provision for loan losses	63,516	—	6,274	6,233	(71)	(2,884)	1,521	74,589
Charge-offs	56,558	—	—	528	47	—	—	57,133
Recoveries	9,364	—	34	63	21	77	—	9,559
Net charge-offs (recoveries)	47,194	—	(34)	465	26	(77)	—	47,574
Ending balance	\$ 128,768	\$ -13,144	\$ 19,149	\$ 241	\$ 1,124	\$ 5,700		\$ 168,126
Period end amount allocated to:								
Loans individually evaluated for impairment	\$ 34,405	\$ -24	\$ 133	\$ 30	\$ 13	\$ —		\$ 34,605
Loans collectively evaluated for impairment	94,363	—	13,120	19,016	211	1,111	5,700	133,521
Ending balance	\$ 128,768	\$ -13,144	\$ 19,149	\$ 241	\$ 1,124	\$ 5,700		\$ 168,126

	Commercial	Mortgage Finance	Construction	Real Estate	Consumer	Equipment Leases	Additional Qualitative Reserve	Total
December 31, 2015								
Allowance for loan losses								
Beginning balance	\$ 70,654	\$ -7,935	\$ 15,582	\$ 240	\$ 1,141	\$ 5,402		\$ 100,954
Provision for loan losses	53,102	—	(1,499)	(1,845)	(13)	2,777	(1,223)	51,299
Charge-offs	16,254	—	—	389	62	25	—	16,730
Recoveries	4,944	—	400	33	173	38	—	5,588
Net charge-offs (recoveries)	11,310	—	(400)	356	(111)	(13)	—	11,142
Ending balance	\$ 112,446	\$ -6,836	\$ 13,381	\$ 338	\$ 3,931	\$ 4,179		\$ 141,111
Period end amount allocated to:								
Loans individually evaluated for impairment	\$ 19,840	\$ —	\$ 1,191	\$ —	\$ 2,436	\$ —		\$ 23,467
Loans collectively evaluated for impairment	92,606	—	6,836	12,190	338	1,495	4,179	117,644
Ending balance	\$ 112,446	\$ -6,836	\$ 13,381	\$ 338	\$ 3,931	\$ 4,179		\$ 141,111

The table below presents the activity in the portion of the allowance for credit losses related to losses on unfunded commitments for the years ended December 31, 2016 and 2015 (in thousands). This liability is recorded in other liabilities in the consolidated balance sheet.

	Year Ended	
	December 31, 2016	2015
Beginning balance	\$9,011	\$7,060
Provision for off-balance sheet credit losses	2,411	1,951
Ending balance	\$11,422	\$9,011

We have traditionally maintained an additional qualitative 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 additional qualitative reserves at December 31, 2016 and 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 and continued volatility in the energy sector.

67

---

Table of Contents

Our recorded investment in loans as of December 31, 2016 and 2015 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):

	Commercial	Mortgage Finance	Construction	Real Estate	Consumer	Equipment Leases	Total
December 31, 2016							
Loans individually evaluated for impairment	\$ 166,669	\$—	\$ 159	\$ 3,751	\$ 200	\$ 83	\$ 170,862
Loans collectively evaluated for impairment	7,124,876	4,497,338	2,098,547	3,458,452	34,387	185,446	17,399,046
Total	\$ 7,291,545	\$ 4,497,338	\$ 2,098,706	\$ 3,462,203	\$ 34,587	\$ 185,529	\$ 17,569,908
	Commercial	Mortgage Finance	Construction	Real Estate	Consumer	Equipment Leases	Total
December 31, 2015							
Loans individually evaluated for impairment	\$ 140,479	\$—	\$ 16,668	\$ 21,042	\$—	\$ 5,151	\$ 183,340
Loans collectively evaluated for impairment	6,532,152	4,966,276	1,835,049	3,118,155	25,323	108,845	16,585,800
Total	\$ 6,672,631	\$ 4,966,276	\$ 1,851,717	\$ 3,139,197	\$ 25,323	\$ 113,996	\$ 16,769,140

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. We recognized \$1.4 million in interest income on non-accrual loans during 2016 compared to \$1.6 million in 2015 and \$1.7 million in 2014. Additional interest income that would have been recorded if the loans had been current during the years ended December 31, 2016, 2015 and 2014 totaled \$7.9 million, \$7.0 million and \$2.1 million, respectively. As of December 31, 2016, \$811,000 of our non-accrual loans were earning on a cash basis, compared to \$884,000 at December 31, 2015. 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.

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. Specific reserves on impaired loans are measured based on the present value of the expected future cash flows discounted at the loan's effective interest rate or the fair value of the underlying collateral less cost to sell. In accordance with ASC 310, Receivables, we have included all restructured loans in our impaired loan totals.

Table of Contents

The following tables detail our impaired loans, by portfolio class as of December 31, 2016 and 2015 (in thousands):  
December 31, 2016

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial					
Business loans	\$ 23,868	\$27,992	\$ —	\$ 12,361	\$ —
Energy loans	46,753	54,522	—	54,075	—
Construction					
Market risk	—	—	—	2,778	—
Real estate					
Market risk	—	—	—	—	—
Commercial	2,083	2,083	—	4,483	38
Secured by 1-4 family	—	—	—	—	—
Consumer	—	—	—	—	—
Equipment leases	—	—	—	403	—
Total impaired loans with no allowance recorded	\$ 72,704	\$84,597	\$ —	\$ 74,100	\$ 38
With an allowance recorded:					
Commercial					
Business loans	\$ 21,303	\$21,303	\$ 7,055	\$ 22,277	\$ —
Energy loans	74,745	88,987	27,350	73,637	24
Construction					
Market risk	159	159	24	53	—
Real estate					
Market risk	1,342	1,342	20	3,000	—
Commercial	—	—	—	—	—
Secured by 1-4 family	326	326	113	435	—
Consumer	200	200	30	67	—
Equipment leases	83	83	13	548	—
Total impaired loans with an allowance recorded	\$ 98,158	\$ 112,400	\$ 34,605	\$ 100,017	\$ 24
Combined:					
Commercial					
Business loans	\$ 45,171	\$49,295	\$ 7,055	\$ 34,638	\$ —
Energy loans	121,498	143,509	27,350	127,712	24
Construction					
Market risk	159	159	24	2,831	—
Real estate					
Market risk	1,342	1,342	20	3,000	—
Commercial	2,083	2,083	—	4,483	38
Secured by 1-4 family	326	326	113	435	—
Consumer	200	200	30	67	—
Equipment leases	83	83	13	951	—
Total impaired loans	\$ 170,862	\$ 196,997	\$ 34,605	\$ 174,117	\$ 62

Table of Contents

December 31, 2015

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Commercial					
Business loans	\$ 11,097	\$ 13,529	\$ —	\$ 17,311	\$ —
Energy loans	37,968	37,968	—	21,791	36
Construction					
Market risk	16,668	16,668	—	9,764	—
Real estate					
Market risk	—	—	—	3,352	—
Commercial	15,353	15,353	—	4,364	24
Secured by 1-4 family	—	—	—	—	—
Consumer					
Equipment leases	2,417	2,417	—	3,233	—
Total impaired loans with no allowance recorded	\$ 83,503	\$ 85,935	\$ —	\$ 59,815	\$ 60
With an allowance recorded:					
Commercial					
Business loans	\$ 20,983	\$ 25,300	\$ 5,737	\$ 31,131	\$ —
Energy loans	70,431	70,431	14,103	6,641	—
Construction					
Market risk	—	—	—	—	—
Real estate					
Market risk	5,335	5,335	1,066	2,558	—
Commercial	—	—	—	306	—
Secured by 1-4 family	354	354	125	1,580	—
Consumer					
Equipment leases	2,734	2,734	2,436	302	—
Total impaired loans with an allowance recorded	\$ 99,837	\$ 104,154	\$ 23,467	\$ 42,528	\$ —
Combined:					
Commercial					
Business loans	\$ 32,080	\$ 38,829	\$ 5,737	\$ 48,442	\$ —
Energy loans	108,399	108,399	14,103	28,432	36
Construction					
Market risk	16,668	16,668	—	9,764	—
Real estate					
Market risk	5,335	5,335	1,066	5,910	—
Commercial	15,353	15,353	—	4,670	24
Secured by 1-4 family	354	354	125	1,580	—
Consumer					
Equipment leases	5,151	5,151	2,436	3,535	—
Total impaired loans	\$ 183,340	\$ 190,089	\$ 23,467	\$ 102,343	\$ 60

Average impaired loans outstanding during the years ended December 31, 2016, 2015 and 2014 totaled \$174.1 million, \$102.3 million and \$46.4 million respectively.



Table of Contents

The table below provides an age analysis of our loans held for investment as of December 31, 2016 (in thousands):

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days(1)	Total Past Due	Non-accrual	Current	Total
Commercial							
Business loans	\$ 33,630	\$ 5,684	\$ 10,236	\$ 49,550	\$ 43,442	\$ 6,308,970	\$ 6,401,962
Energy	2,505	—	—	2,505	121,498	765,580	889,583
Mortgage finance loans	—	—	—	—	—	4,497,338	4,497,338
Construction							
Market risk	818	1,429	—	2,247	159	2,075,654	2,078,060
Secured by 1-4 family	581	—	—	581	—	20,065	20,646
Real estate							
Market risk	2,984	12,155	—	15,139	—	2,612,655	2,627,794
Commercial	—	—	—	—	2,083	630,699	632,782
Secured by 1-4 family	3,217	53	493	3,763	326	197,538	201,627
Consumer	119	—	—	119	200	34,268	34,587
Equipment leases	—	—	—	—	83	185,446	185,529
Total loans held for investment	\$ 43,854	\$ 19,321	\$ 10,729	\$ 73,904	\$ 167,791	\$ 17,328,213	\$ 17,569,908

Loans past due 90 days and still accruing includes premium finance loans of \$6.8 million. These loans are (1) 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.

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, or a reduction of the face amount of debt, or forgiveness of either principal or accrued interest. As of December 31, 2016, we did not have any loans considered restructured that were not on non-accrual compared to \$249,000 at December 31, 2015. These loans did not have unfunded commitments at December 31, 2016 or 2015. Of the non-accrual loans at December 31, 2016 and 2015, \$18.1 million and \$24.9 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.

The following tables summarize, as of December 31, 2016 and 2015, loans that have been restructured during 2016 and 2015 (in thousands):

December 31, 2016

	Number of Contracts	Pre-Restructuring Outstanding Recorded Investment	Post-Restructuring Outstanding Recorded Investment
Energy loans	2	\$ 14,235	\$ 12,236
Total new restructured loans in 2016	2	\$ 14,235	\$ 12,236

December 31, 2015

	Number of Contracts	Pre-Restructuring Outstanding Recorded Investment	Post-Restructuring Outstanding Recorded

			Investment
Commercial business loans	5	\$ 20,459	\$ 14,992
Total new restructured loans in 2015	5	\$ 20,459	\$ 14,992

71

---

Table of Contents

The restructured loans generally include terms to temporarily place the loan on interest only, extend the payment terms or reduce the interest rate. We did not forgive any principal on the above loans. The \$2.0 million decrease in the post-restructuring recorded investment in the restructured loans in 2016 and the \$5.5 million decrease in 2015 are due to paydowns. At December 31, 2016, \$12.2 million of the above loans restructured in 2016 are on non-accrual. The restructuring of the loans did not have a significant impact on our allowance for loan losses at December 31, 2016 or 2015.

The following table provides information on how loans were modified as a restructured loan during the year ended December 31, 2016 and 2015 (in thousands):

	December 31,	
	2016	2015
Extended maturity	\$—	\$—
Combination of maturity extension and payment schedule adjustment	12,236	14,992
Total	\$12,236	\$14,992

As of December 31, 2016 and 2015, we did not have any loans that were restructured within the last 12 months that subsequently defaulted.

**(4) OREO and Valuation Allowance for Losses on OREO**

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

	Year ended December 31,		
	2016	2015	2014
Beginning balance	\$278	\$568	\$5,110
Additions	18,822	1,267	851
Sales	(139 )	(1,557)	(5,393 )
Valuation allowance for OREO	—	—	—
Direct write-downs	—	—	—
Ending balance	\$18,961	\$278	\$568

The additions to OREO during the year ended December 31, 2016 relates to the foreclosure of three commercial properties.

When foreclosure occurs, the acquired asset is recorded at fair value less selling costs, generally based on appraised value, which may result in partial charge-off of the loan. So long as the property is retained, further reductions in appraised value will result in valuation adjustments being taken as non-interest expense. If the decline in value is believed to be permanent and not solely driven by short-term market conditions, a direct write-down of 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 to decreases in the appraised value of the asset and the incurrence of carrying costs during that holding period. We did not record a valuation allowance or related expense during the years ended December 31, 2016, 2015 and 2014.

**(5) Certain Transfers of Financial Assets**

Through our MCA business, we commit to purchase residential mortgage loans from independent correspondent lenders and deliver those loans into the secondary market via whole loans sales to independent third parties or in securitization transactions to Ginnie Mae and GSEs such as Fannie Mae and Freddie Mac. We have elected to carry these loans at fair value based on sales commitments and market quotes. Changes in the fair value of the loans held for sale are included in other non-interest income.

Residential mortgage loans are subject to both credit and interest rate risk. Credit risk is managed through underwriting policies and procedures, including collateral requirements, which are generally accepted by the secondary loan markets. Exposure to interest rate fluctuations is partially managed through forward sales contracts, which set the price for loans that will be delivered in the next 60 to 90 days.

Table of Contents

The table below presents the unpaid principal balance of loans held for sale and related fair values at December 31, 2016 and 2015 (in thousands):

	December 31,	
	2016	2015
Unpaid principal balance	\$962,096	\$82,853
Fair value	968,929	86,075
Fair value over unpaid principal balance	\$6,833	\$3,222

No loans held for sale were 90 days or more past due or on non-accrual as of December 31, 2016 or December 31, 2015.

The differences between the fair value and the aggregate unpaid principal balance include changes in fair value recorded at and subsequent to purchase, gains and losses on the related loan purchase commitment prior to purchase and premiums or discounts on acquired loans.

The table below presents a reconciliation of the changes in loans held for sale is for the years December 31, 2016 and 2015 (in thousands):

	Year Ended December 31,	
	2016	2015
Beginning balance	\$86,075	\$—
Loans purchased	3,327,482	127,002
Payments and proceeds from sales	(2,433,348)	(40,927)
Change in fair value	(11,280)	—
Ending balance	\$968,929	\$86,075

We generally retain the right to service the loans sold, creating MSR assets on our balance sheet. A summary of MSR activities for the years ended December 31, 2016 and 2015 is as follows (in thousands):

	Year Ended December 31,	
	2016	2015
Servicing asset:		
Balance, beginning of year	\$423	\$—
Capitalized servicing rights	29,816	437
Amortization	(1,703)	(14)
Balance, end of period	\$28,536	\$423
Valuation allowance:		
Balance, beginning of year	\$—	\$—
Increase in valuation allowance	—	—
Balance, end of period	\$—	\$—
Servicing asset, net(1)	\$28,536	\$423
Fair value	\$30,877	\$423

(1) MSRs are reported on the consolidated balance sheets at lower of cost or market.

At December 31, 2016 and 2015, our servicing portfolio of residential mortgage loans sold included 8,618 and 168 loans, respectively, with an outstanding principal balance of \$2.2 billion and \$39.0 million, respectively. In connection with the servicing of these loans, we maintain escrow funds for taxes and insurance in the name of investors, as well as collections in transit to investors. These escrow funds are segregated and held in separate non-interest-bearing bank accounts at the Bank. These deposits, included in total non-interest-bearing deposits on the consolidated balance sheets, were \$21.0 million at December 31, 2016 and \$240,000 at December 31, 2015.

The estimated fair value of the MSR assets is obtained from an independent third party on a quarterly basis. MSRs do not trade in an active, open market with readily observable prices. Due to the nature of the valuation inputs, MSRs are characterized as



Table of Contents

Level 3 assets in the fair value hierarchy. The fair value of MSR is determined using a discounted cash flow model to calculate the present value of the estimated future net servicing income. The assumptions are a combination of market and Company specific data. Management and the independent third party discuss the key assumptions used in the discounted cash flow model and make adjustments as necessary. As of December 31, 2016 and December 31, 2015, management used the following assumptions to determine the fair value of MSR:

	December 31,	
	2016	2015
Average discount rates	9.96%	9.76%
Expected prepayment speeds	7.91%	9.14%
Weighted-average life, in years	8.0	7.3

A sensitivity analysis of changes in the fair value of our MSR portfolio resulting from certain key assumptions is presented in the following table (in thousands):

	December 31,	
	2016	2015
50 bp adverse change in prepayment speed	\$(2,833)	\$(53)
100 bp adverse change in prepayment speed	(6,812)	(146)

In conjunction with the sale and securitization of loans held for sale, we may be exposed to liability resulting from recourse agreements and repurchase agreements. If it is determined subsequent to our sale of a loan that the loan sold is in breach of the representations or warranties made in the applicable sale agreement, we may have an obligation to either (a) repurchase the loan for the unpaid principal balance, accrued interest and related advances, (b) indemnify the purchaser against any loss it suffers or (c) make the purchaser whole for the economic benefits of the loan. During the years ended December 31, 2016 and 2015, we originated or purchased and sold approximately \$2.4 billion and \$39.1 million, respectively, of mortgage loans.

Our repurchase, indemnification and make whole obligations vary based upon the terms of the applicable agreements, the nature of the asserted breach and the status of the mortgage loan at the time a claim is made. We establish reserves for estimated losses of this nature inherent in the origination of mortgage loans by estimating the losses inherent in the population of all loans sold based on trends in claims and actual loss severities experienced. The reserve will include accruals for probable contingent losses in addition to those identified in the pipeline of claims received. The estimation process is designed to include amounts based on actual losses experienced from actual repurchase activity. Because the MCA business commenced in 2015, we have little historical data to support the establishment of a reserve. The baseline for the repurchase reserve uses historical loss factors obtained from industry data that are applied to loan pools originated and sold during the years ended December 31, 2016 and 2015. The historical industry data loss factors and experienced losses will be accumulated for each sale vintage (year loan was sold) and applied to more recent sale vintages to estimate inherent losses not yet realized. Our estimated exposure related to these loans was \$835,000 at December 31, 2016 and \$20,000 at December 31, 2015 and is recorded in other liabilities in the consolidated balance sheets. We had no losses due to repurchase, indemnification or make-whole obligations during the years ended December 31, 2016 and 2015.

**(6) Goodwill and Other Intangible Assets**

In May 2013, we acquired the assets of a premium finance company and recorded a total intangible asset of \$2.1 million. Of this total, \$954,000 was allocated to goodwill, \$554,000 to customer relationships, \$457,000 to developed technology and \$98,000 to trade name. The \$554,000 customer relationship intangible is being amortized over 14 years, the \$457,000 technology intangible is being amortized over 7 years, and the \$98,000 intangible related to the trade name was determined to have an indefinite life.

Table of Contents

Goodwill and other intangible assets at December 31, 2016 and 2015 are summarized as follows (in thousands):

	Gross Goodwill and Intangible Assets	Accumulated Amortization	Net Goodwill and Intangible Assets
December 31, 2016			
Goodwill	\$ 15,468	\$ (374 )	\$ 15,094
Intangible assets—customer relationships and trademarks	9,006	(4,588 )	4,418
Total goodwill and intangible assets	\$ 24,474	\$ (4,962 )	\$ 19,512
December 31, 2015			
Goodwill	\$ 15,468	\$ (374 )	\$ 15,094
Intangible assets—customer relationships and trademarks	9,006	(4,140 )	4,866
Total goodwill and intangible assets	\$ 24,474	\$ (4,514 )	\$ 19,960

Amortization expense related to intangible assets totaled \$448,000 in 2016, \$628,000 in 2015 and \$699,000 in 2014. The estimated aggregate future amortization expense for intangible assets remaining as of December 31, 2016 is as follows (in thousands):

2017	\$470
2018	470
2019	470
2020	432
2021	405
Thereafter	2,171
	\$4,418

## (7) Premises and Equipment

Premises and equipment at December 31, 2016 and 2015 are summarized as follows (in thousands):

	December 31,	
	2016	2015
Premises	\$22,887	\$21,020
Furniture and equipment	24,159	26,185
	47,046	47,205
Accumulated depreciation	(27,271 )	(23,644 )
Total premises and equipment, net	\$19,775	\$23,561

Depreciation expense for the above premises and equipment was approximately \$6.0 million, \$4.6 million and \$4.1 million in 2016, 2015 and 2014, respectively.

Table of Contents

## (8) Deposits

Deposits at December 31, 2016 and 2015 were as follows (in thousands):

	December 31,	
	2016	2015
Non-interest-bearing demand deposits	\$7,994,201	\$6,386,911
Interest-bearing deposits		
Transaction	1,954,834	2,006,591
Savings	6,625,177	6,163,622
Time	442,619	527,495
Total interest-bearing deposits	9,022,630	8,697,708
Total deposits	\$17,016,831	\$15,084,619

The scheduled maturities of interest-bearing time deposits were as follows at December 31, 2016 (in thousands):

2017	\$417,911
2018	18,384
2019	4,452
2020	1,640
2021	232
2022 and after —	\$442,619

At December 31, 2016 and 2015, the Bank had approximately \$15.4 million and \$16.6 million, respectively, in deposits from related parties, including directors, stockholders and their affiliates.

At December 31, 2016 and 2015, interest-bearing time deposits of \$250,000 or more were approximately \$225.5 million and \$274.4 million, respectively.

## (9) Borrowing Arrangements

The following table summarizes our borrowings at December 31, 2016, 2015 and 2014 (in thousands):

	December 31,					
	2016		2015		2014	
	Balance	Rate(3)	Balance	Rate(3)	Balance	Rate(3)
Federal funds purchased(4)	\$101,800	0.80 %	\$74,164	0.55 %	\$66,971	0.30 %
Customer repurchase agreements(1)	7,775	0.05 %	68,887	0.02 %	25,705	0.07 %
FHLB borrowings(2)	2,000,000	0.61 %	1,500,000	0.31 %	1,100,005	0.13 %
Line of credit	—	— %	—	— %	—	— %
Subordinated notes	281,044	5.87 %	280,682	5.75 %	280,321	5.82 %
Trust preferred subordinated debentures	113,406	2.90 %	113,406	2.47 %	113,406	2.18 %
Total borrowings	\$2,504,025		\$2,037,139		\$1,586,408	
Maximum outstanding at any month end	\$2,511,579		\$2,042,457		\$1,592,087	



Table of Contents

- (1) Securities pledged for customer repurchase agreements were \$10.2 million, \$14.2 million and \$21.8 million at December 31, 2016, 2015 and 2014, respectively.

FHLB borrowings are collateralized by a blanket floating lien on certain real estate secured loans, mortgage finance assets and also certain pledged securities. The weighted-average interest rate for the years ended

- (2) December 31, 2016, 2015 and 2014 was 0.43%, 0.18% and 0.15%, respectively. The average balance of FHLB borrowings for the years ended December 31, 2016, 2015 and 2014 was \$1.4 billion, \$1.2 billion and \$213.4 million, respectively.

- (3) Interest rate as of period end.

The weighted-average interest rate on Federal funds purchased for the years ended December 31, 2016, 2015 and

- (4) 2014 was 0.57%, 0.29% and 0.27%, respectively. The average balance of Federal funds purchased for the years ended December 31, 2016, 2015 and 2014 was \$90.9 million, \$98.8 million and \$139.3 million, respectively.

The following table summarizes our other borrowing capacities net of balances outstanding at December 31, 2016, 2015 and 2014 (in thousands):

	December 31,		
	2016	2015	2014
FHLB borrowing capacity relating to loans	\$3,057,915	\$4,101,396	\$3,602,994
FHLB borrowing capacity relating to securities	1,653	1,213	535
Total FHLB borrowing capacity	\$3,059,568	\$4,102,609	\$3,603,529
Unused Federal funds lines available from commercial banks	\$1,118,000	\$1,231,000	\$1,186,000
Unused Federal Reserve Borrowings capacity	\$3,179,087	\$2,966,702	\$2,643,000

Our unsecured, revolving, non-amortizing line of credit had maximum availability of \$130.0 million and matured on December 21, 2016. This line of credit was renewed on December 20, 2016 with a new maximum availability of \$130.0 million and a maturity date of December 19, 2017. 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. There were no borrowings outstanding as of December 31, 2016 or December 31, 2015. The average borrowings during the year ended December 31, 2016 were \$6.8 million compared to none during the year ended December 31, 2015.

The scheduled maturities of our borrowings at December 31, 2016, were as follows (in thousands):

	Within One Year	After One But Within Three Years	After Three But Within Five Years	After Five Years	Total
Federal funds purchased and customer repurchase agreements(1)	\$109,575	\$—	\$—	\$—	\$109,575
FHLB borrowings(1)	2,000,000	—	—	—	2,000,000
Subordinated notes(1)	—	—	—	281,044	281,044
Trust preferred subordinated debentures(1)	—	—	—	113,406	113,406
Total borrowings	\$2,109,575	\$—	\$—	\$394,450	\$2,504,025

(1) Excludes interest.

(10) Long-Term Debt

From November 2002 to September 2006 various Texas Capital Statutory Trusts were created and subsequently issued floating rate trust preferred securities in various private offerings totaling \$113.4 million. As of December 31, 2016, the details of the trust preferred subordinated debentures are summarized below (in thousands):

	Texas Capital Bancshares Statutory Trust I	Texas Capital Statutory Trust II	Texas Capital Statutory Trust III	Texas Capital Statutory Trust IV	Texas Capital Statutory Trust V
Date issued	November 19, 2002	April 10, 2003	October 6, 2005	April 28, 2006	September 29, 2006
	\$10,310	\$10,310	\$25,774	\$25,774	\$41,238

Trust preferred securities  
issued

Floating or fixed rate securities	Floating	Floating	Floating	Floating	Floating
Interest rate on subordinated debentures	3 month LIBOR + 3.35%	3 month LIBOR + 3.25%	3 month LIBOR + 1.51%	3 month LIBOR + 1.60%	3 month LIBOR + 1.71%
Maturity date	November 2032	April 2033	December 2035	June 2036	December 2036

77

---

Table of Contents

On September 21, 2012, we issued \$111.0 million of subordinated notes. The notes mature in September 2042 and bear interest at a rate of 6.50% per annum, payable quarterly. The indenture governing the notes contains customary covenants and restrictions.

On January 31, 2014, the Bank issued \$175.0 million of subordinated notes in an offering to institutional investors exempt from registration under Section 3(a)(2) of the Securities Act of 1933 and 12 C.F.R. Part 16. Net proceeds from the transaction were \$172.4 million. The notes mature in January 2026 and bear interest at a rate of 5.25% per annum, payable semi-annually. The notes are unsecured and are subordinate to the Bank's obligations to its depositors, its obligations under banker's acceptances and letters of credit, certain obligations to Federal Reserve Banks and the FDIC and the Bank's obligations to its other creditors, except any obligations which expressly rank on a parity with or junior to the notes. The notes qualify as Tier 2 capital for regulatory capital purposes, subject to applicable limitations.

Interest payments on all long-term debt are deductible for federal income tax purposes.

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.

Table of Contents

## (11) Income Taxes

We have a gross deferred tax asset of \$91.5 million and \$78.8 million at December 31, 2016 and 2015, respectively, which relates primarily to our allowance for loan losses, loan origination fees and stock compensation. Management believes it is more likely than not that all of the deferred tax assets will be realized. Our net deferred tax asset is included in other assets in the consolidated balance sheets.

Income tax expense/(benefit) consists of the following for the years ended (in thousands):

	Year ended December 31,		
	2016	2015	2014
Current:			
Federal	\$86,612	\$80,957	\$77,855
State	2,412	2,245	2,124
Total	89,024	83,202	79,979
Deferred			
Federal	(2,946 )	(3,561 )	(3,969 )
State	—	—	—
Total	(2,946 )	(3,561 )	(3,969 )
Total expense			
Federal	83,666	77,396	73,886
State	2,412	2,245	2,124
Total	\$86,078	\$79,641	\$76,010

The tax effect of unrealized gains and losses on available-for-sale securities is recorded to other comprehensive income and is not a component of income tax expense/(benefit).

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of deferred tax assets and liabilities are as follows (in thousands):

	December 31,	
	2016	2015
Deferred tax assets:		
Allowance for credit losses	\$64,009	\$53,368
Loan origination fees	13,536	13,435
Stock compensation	5,761	5,509
Non-accrual interest	2,537	1,198
Deferred lease expense	3,375	3,779
Other	2,322	1,491
Total deferred tax assets	91,540	78,780
Deferred tax liabilities:		
Loan origination costs	(1,722 )	(1,726 )
Leases	(7,962 )	(10,121 )
MSRs	(10,973 )	(151 )
Depreciation	(8,797 )	(8,296 )
Unrealized gain on securities	(223 )	(387 )
Other	(2,971 )	(2,317 )
Total deferred tax liabilities	(32,648 )	(22,998 )
Net deferred tax asset	\$58,892	\$55,782

ASC 740-10, Income Taxes — Accounting for Uncertainties in Income Taxes (“ASC 740-10”) prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of a tax position taken or



Table of Contents

expected to be taken in a tax return. Benefits from tax positions should be recognized in the financial statements only when it is more likely than not that the tax position will be sustained upon examination by the appropriate taxing authority that would have full knowledge of all relevant information. A tax position that meets the more-likely-than-not recognition threshold is measured at the largest amount of cumulative benefit that is greater than fifty percent likely of being realized upon ultimate settlement. Tax positions that previously failed to meet the more-likely-than-not recognition threshold should be recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not recognition threshold should be derecognized in the first subsequent financial reporting period in which that threshold is no longer met. ASC 740-10 also provides guidance on the accounting for and disclosure of unrecognized tax benefits, interest and penalties.

We file income tax returns in the U.S. federal jurisdiction and several U.S. state jurisdictions. We are no longer subject to U.S. federal income tax examinations by tax authorities for years before 2013.

The reconciliation of income computed at the U.S. federal statutory tax rates to income tax expense (benefit) is as follows:

	Year ended December 31,					
	2016	2015	2014	2016	2015	2014
Tax at U.S. statutory rate	35	35	35	%	%	%
State taxes	1	1	1	%	%	%
Non-deductible expenses	1	1	1	%	%	%
Non-taxable income	(1)	(1)	(1)	%	%	%
Other	—	(1)	—	%	%	%
Total	36	35	36	%	%	%

**(12) Stock-Based Compensation and Employee Benefits**

We have a qualified retirement plan, with a salary deferral feature designed to qualify under Section 401 of the Internal Revenue Code (“the 401(k) Plan”). The 401(k) Plan permits our employees to defer a portion of their compensation. Matching contributions may be made in amounts and at times determined by the Company. We contributed approximately \$6.8 million, \$6.3 million, and \$4.5 million for the years ended December 31, 2016, 2015 and 2014, respectively. Employees are eligible to participate in the 401(k) Plan when they meet certain requirements concerning minimum age and period of credited service. All contributions to the 401(k) Plan are invested in accordance with participant elections among certain investment options.

During 2000, we implemented an Employee Stock Purchase Plan (“ESPP”). Employees are eligible for the plan when they meet certain requirements concerning period of credited service and minimum hours worked. Eligible employees may contribute a minimum of 1% to a maximum of 10% of eligible compensation up to the Section 423 of the Internal Revenue Code limit of \$25,000. In 2006, stockholders approved the 2006 ESPP, which allocated 400,000 shares for purchase. As of December 31, 2016, 2015 and 2014, 124,572, 113,910 and 102,836 shares had been purchased on behalf of the employees under the 2006 ESPP.

We have stock-based compensation plans under which equity-based compensation grants are made by the board of directors, or its designated committee. Grants are subject to vesting requirements. Under the plans, we may grant, among other things, non-qualified stock options, incentive stock options, restricted stock, restricted stock units (“RSUs”), stock appreciation rights (“SARs”), cash-based performance units or any combination thereof. Plans include grants for employees and directors. There are 2,550,000 total shares authorized under the plans. Total shares which may be issued under the plans at December 31, 2016 were 2,270,699.

We also offer a non-qualified deferred compensation plan for our executives and key members of management in order to assist us in attracting and retaining these individuals. Participants in the plan may elect to defer up to 75% of their annual salary and/or short-term incentive payout into deferral accounts that mirror the gains or losses of investments selected by the participants. We do not currently match deferrals made pursuant to the plan. The plan allows us to make discretionary contributions on behalf of a participant. No such contributions were made in 2016 or 2015. All participant contributions to the plan and any related earnings are immediately vested and may be withdrawn upon the participant's separation from service, death or disability or upon a date specified by the participant. The

deferrals are recorded to salaries and benefits as a reduction and a corresponding accrual is recorded in other liabilities.

80

---

Table of Contents

A summary of our SAR activity and related information for 2016, 2015 and 2014 is as follows. These rights are time-vested and generally vest ratably over a period of five years.

	December 31, 2016		December 31, 2015		December 31, 2014	
	SARs	Weighted Average Exercise Price	SARs	Weighted Average Exercise Price	SARs / PSARs	Weighted Average Exercise Price
SARs outstanding at beginning of year	360,544	\$ 25.73	445,009	\$ 24.83	537,149	\$ 23.68
SARs granted	—	—	—	—	8,000	62.02
SARs exercised	(234,681 )	22.54	(84,465 )	20.97	(92,640 )	20.87
SARs forfeited	—	—	—	—	(7,500 )	31.16
SARs outstanding at year-end	125,863	\$ 31.68	360,544	\$ 25.73	445,009	\$ 24.83
SARs vested and exercisable at year-end	94,463	\$ 26.73	307,144	\$ 22.49	355,509	\$ 21.16
Weighted average remaining contractual life of SARs vested		3.62		2.36		2.89
Compensation expense	\$307,000		\$367,000		\$530,000	
Unrecognized compensation expense	\$392,000		\$699,000		\$1,066,000	
Weighted average period over which unrecognized compensation expense is expected to be recognized (in years)		1.52		2.40		3.20
Weighted average fair value of SARs granted		\$ —		\$ —		\$ 23.02
Fair value of shares vested during the year	\$337,000		\$436,000		\$580,345	
Weighted average remaining contractual life of SARs currently outstanding (in years)		4.32		3.08		3.85
Intrinsic value of SARs exercised	\$4,881,000		\$8,291,000		\$11,794,000	



Table of Contents

A summary of our RSU activity and related information for 2016, 2015 and 2014 is as follows. Grants of RSUs include both performance-based and time-based vesting conditions and generally vest over a three-year period.

	December 31, 2016		December 31, 2015		December 31, 2014	
	RSUs	Weighted Average Grant Date Fair Value	RSUs	Weighted Average Grant Date Fair Value	RSUs	Weighted Average Grant Date Fair Value
RSUs outstanding at beginning of year	333,174	\$ 48.60	295,165	\$ 42.93	403,739	\$ 33.72
RSUs granted	213,577	51.75	145,952	51.96	70,050	57.84
RSUs exercised	(94,296 )	42.87	(95,743 )	38.05	(161,249 )	26.40
RSUs forfeited	(27,400 )	51.18	(12,200 )	43.89	(17,375 )	37.70
RSUs outstanding at year-end	425,055	\$ 51.28	333,174	\$ 48.60	295,165	\$ 42.93
Compensation expense	\$4,771,000		\$4,230,000		\$4,098,000	
Unrecognized compensation expense	\$17,167,000		\$13,038,000		\$10,556,000	
Weighted average period over which unrecognized compensation expense is expected to recognized (in years)		3.37		3.30		3.50
Weighted average remaining contractual life of RSUs currently outstanding		8.65		8.29		8.11

During 2016, we granted 1,472 shares of restricted stock to a new non-employee director that vest ratably over a 3 year period. Total compensation cost for the restricted stock, net of taxes, was \$15,000 for the year ended December 31, 2016. No shares were granted in 2015 or 2014.

Total compensation cost for all share-based arrangements, net of taxes, was \$3.3 million, \$3.0 million and \$3.0 million for the years ended December 31, 2016, 2015 and 2014, respectively.

Cash flows from financing activities included \$2.0 million, \$1.5 million and \$2.9 million in cash inflows from excess tax benefits related to stock-based compensation in 2016, 2015 and 2014, respectively.

We granted a total of 224,071 cash-based performance units in 2016, with a total of 459,000 outstanding at December 31, 2016. We granted a total of 146,153 and 171,808 cash-based performance units in 2015 and 2014. Of the outstanding units at December 31, 2016, 429,865 are service-based and vest ratably over a period of four years. Additionally, 29,135 units contain both service and performance based vesting requirements: 50% of the units will vest on the third anniversary of the date of grant, and the balance will vest based on attainment of certain performance metrics determined by the Human Resources Committee. Since these units have a cash payout feature, they are accounted for under the liability method and the related expense is based on the stock price at period end.

Compensation cost for the units was \$8.5 million, \$7.7 million and \$9.9 million for the years ended December 31, 2016, 2015 and 2014 respectively. At December 31, 2016, the weighted average remaining contractual life of the units was 8.16 years.

Total compensation cost for all cash-based arrangements, net of taxes, for the years ended December 31, 2016, 2015 and 2014 was \$5.5 million, \$5.0 million and \$6.5 million, respectively.

### (13) 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 that 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 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.

82

---

Table of Contents

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.

At December 31, 2016 and 2015, commitments to extend credit and standby and commercial letters of credit were as follows (in thousands):

	December 31,	
	2016	2015
Commitments to extend credit	\$5,704,381	\$5,542,363
Standby letters of credit	171,266	182,219

At December 31, 2016 and 2015, we had \$11.4 million and \$9.0 million, respectively, in allowance allocations for these off-balance sheet commitments recorded in other liabilities.

**(14) Regulatory Restrictions**

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.

The Basel III regulatory capital framework (the "Basel III Capital Rules") adopted by U.S. federal regulatory authorities, among other things, (i) establish the capital measure called "Common Equity Tier 1" ("CET1"), (ii) specify that Tier 1 capital consist of CET1 and "Additional Tier 1 Capital" instruments meeting stated requirements, (iii) define CET1 narrowly by requiring that most deductions/adjustments to regulatory capital measures be made to CET1 and not to the other components of capital and (iv) set forth the acceptable scope of deductions/adjustments to the specified capital measures. The Basel III Capital Rules became effective for us on January 1, 2015 with certain transition provisions fully phased in on January 1, 2019.

Additionally, the Basel III Capital Rules require that we maintain a capital conservation buffer with respect to each of the CET1, Tier 1 and total capital to risk-weighted assets, which provides for capital levels that exceed the minimum risk-based capital adequacy requirements. The capital conservation buffer is subject to a three year phase-in period that began on January 1, 2016 and will be fully phased-in on January 1, 2019 at 2.5%. The required phase-in capital conservation buffer during 2016 was 0.625%. A financial institution with a conservation buffer of less than the required amount is subject to limitations on capital distributions, including dividend payments and stock repurchases, and certain discretionary bonus payments to executive officers.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios of 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 December 31, 2016, that the Company and the Bank meet 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 December 31, 2016 and 2015. 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 change 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 effect on 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.



Table of Contents

The table below summarizes our actual and required capital ratios under the Basel III Capital Rules:

	Actual		Minimum Capital Required - Basel III Phase-In Schedule		Minimum capital Required - Basel III Fully Phased-In		Required to be Considered Well Capitalized	
	Capital Amount	Ratio	Capital Amount	Ratio	Capital Amount	Ratio	Capital Amount	Ratio
As of December 31, 2016:								
CET1								
Company	\$1,841,219	8.97 %	\$1,052,205	5.125 %	\$1,437,159	7.00 %	N/A	N/A
Bank	1,735,496	8.45 %	1,051,989	5.125 %	1,436,863	7.00 %	1,334,244	6.50 %
Total capital (to risk-weighted assets)								
Company	2,561,663	12.48 %	1,770,766	8.625 %	2,155,715	10.50 %	N/A	N/A
Bank	2,297,528	11.19 %	1,770,421	8.625 %	2,155,295	10.50 %	2,052,683	10.00 %
Tier 1 capital (to risk-weighted assets)								
Company	2,101,071	10.23 %	1,360,154	6.625 %	1,745,103	8.50 %	N/A	N/A
Bank	1,895,348	9.23 %	1,359,888	6.625 %	1,744,762	8.50 %	1,642,147	8.00 %
Tier 1 capital (to average assets)(1)								
Company	2,101,071	9.34 %	900,268	4.00 %	900,268	4.00 %	N/A	N/A
Bank	1,895,348	8.42 %	900,070	4.00 %	900,070	4.00 %	1,125,087	5.00 %
As of December 31, 2015:(2)								
CET1								
Company	\$1,455,662	7.47 %	\$876,563	4.50 %	N/A	N/A	N/A	N/A
Bank	1,522,729	7.82 %	876,336	4.50 %	N/A	N/A	1,265,819	6.50 %
Total capital (to risk-weighted assets)								
Company	2,152,292	11.05 %	1,558,334	8.00 %	N/A	N/A	N/A	N/A
Bank	2,058,359	10.57 %	1,557,931	8.00 %	N/A	N/A	1,947,414	10.00 %
Tier 1 capital (to risk-weighted assets)								
Company	1,716,170	8.81 %	1,168,751	6.00 %	N/A	N/A	N/A	N/A
Bank	1,683,237	8.64 %	1,168,448	6.00 %	N/A	N/A	1,557,931	8.00 %
Tier 1 capital (to average assets)(1)								
Company	1,716,170	8.92 %	769,258	4.00 %	N/A	N/A	N/A	N/A
Bank	1,683,237	8.75 %	769,498	4.00 %	N/A	N/A	961,873	5.00 %

(1) The Tier 1 capital ratio (to average assets) is not impacted by the Basel III Capital Rules; however, it should be noted that the Federal Reserve Board and the FDIC may require the Company and the Bank, respectively, to maintain a Tier 1 capital ratio (to average assets) above the required minimum.

(2) The minimum capital required ratios for December 31, 2015 do not reflect the phase-in as it was not effective until January 1, 2016.

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 December 31, 2016, our total mortgage finance loans were \$4.5 billion compared to the average for the year ended December 31, 2016 of \$4.3 billion. As CET1, Tier 1 and total capital ratios are calculated using quarter-end 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 actual 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 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 our common stock during 2016, 2015 or 2014.

Table of Contents

The required reserve balances at the Federal Reserve at December 31, 2016 and 2015 were approximately \$221.9 million and \$150.6 million, respectively.

## (15) Earnings Per Share

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

	Year ended December 31,		
	2016	2015	2014
Numerator:			
Net income	\$ 155,119	\$ 144,854	\$ 136,352
Preferred stock dividends	9,750	9,750	9,750
Net income available to common stockholders	\$ 145,369	\$ 135,104	\$ 126,602
Denominator:			
Denominator for basic earnings per share—weighted average shares	46,239,210	45,808,440	43,236,344
Effect of employee stock-based awards(1)	128,228	211,168	311,423
Effect of warrants to purchase common stock	398,464	418,264	455,489
Denominator for dilutive earnings per share—adjusted weighted average shares and assumed conversions	46,765,902	46,437,872	44,003,256
Basic earnings per common share	\$3.14	\$ 2.95	\$ 2.93
Diluted earnings per common share	\$3.11	\$ 2.91	\$ 2.88

- (1) Stock options, SARs and RSUs outstanding of 150,416, 64,700 and 51,300 in 2016, 2015 and 2014, respectively, have not been included in diluted earnings per share because to do so would have been antidilutive for the periods presented. Stock options are antidilutive when the exercise price is higher than the average market price of the Company's common stock.

## (16) 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.

Quoted prices in active markets for identical assets or liabilities. This category includes the assets and Level 1 liabilities related to our non-qualified deferred compensation plan where values are based on quoted market prices for identical equity securities in an active market.

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 also includes loans held for sale and 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 Level 3 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.





Table of Contents

Assets and liabilities measured at fair value at December 31, 2016 and 2015 are as follows (in thousands):

	Fair Value Measurements Using	
	Level 1	Level 2 Level 3
December 31, 2016		
Available for sale securities:(1)		
Residential mortgage-backed securities	\$ 15,652	\$ —
Municipals	275	—
Equity securities(2)	1,786	—
Loans held for sale(3)	968,929	—
Loans held for investment(4)(6)	—	52,323
OREO(5)(6)	—	18,961
Derivative assets(7)	37,878	—
Derivative liabilities(7)	26,240	—
Non-qualified deferred compensation plan liabilities(8)	1,844	—
December 31, 2015		
Available for sale securities:(1)		
Residential mortgage-backed securities	\$ 21,901	\$ —
Municipals	831	—
Equity securities(2)	7,260	—
Loans held for sale(3)	86,075	—
Loans held for investment(4)(6)	—	41,420
OREO(5)(6)	—	278
Derivative assets(7)	35,292	—
Derivative liabilities(7)	35,420	—
Non-qualified deferred compensation plan liabilities(8)	—	—

(1) Securities are measured at fair value on a recurring basis, generally monthly.

(2) Equity securities consist of Community Reinvestment Act funds and investments related to our non-qualified deferred compensation plan.

(3) Loans held for sale are measured at fair value on a recurring basis, generally monthly.

(4) Includes impaired loans that have been measured for impairment at the fair value of the loan's collateral.

(5) OREO is transferred from loans to OREO at fair value less selling costs.

(6) Loans held for investment and OREO are measured on a nonrecurring basis, generally annually or more often as warranted by market and economic conditions

(7) Derivative assets and liabilities are measured at fair value on a recurring basis, generally quarterly.

(8) Non-qualified deferred compensation plan liabilities represent the fair value of the obligation to the employee, which corresponds to the fair value of the invested assets, and are measured at fair value on a recurring basis, generally monthly.

#### 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 held for investment

During the years ended December 31, 2016 and 2015, certain impaired loans held for investment were re-evaluated and reported at fair value through a specific valuation allowance allocation of the allowance for loan losses based

upon the fair value of the underlying collateral. The \$52.3 million total above includes impaired loans at December 31, 2016 with a carrying value of \$74.1 million that were reduced by specific valuation allowance allocations totaling \$21.8 million for a total reported fair value of \$52.3 million based on collateral valuations utilizing Level 3 valuation inputs. The \$41.4 million total above includes impaired loans at December 31, 2015 with a carrying value of \$49.7 million that were reduced by specific valuation

86

---

Table of Contents

allowance allocations totaling \$8.3 million for a total reported fair value of \$41.4 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 recorded at fair value less estimated selling costs. At December 31, 2016 and 2015, OREO had a carrying value of \$19.0 million and \$278,000, respectively, with no specific valuation allowance. The fair value of OREO was computed based on third party appraisals, which are Level 3 valuation inputs.

**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):

	December 31, 2016		December 31, 2015	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
<b>Financial assets:</b>				
Level 1 inputs:				
Cash and cash equivalents	\$2,839,352	\$2,839,352	\$1,790,870	\$1,790,870
Securities, available-for-sale	1,786	1,786	—	—
Level 2 inputs:				
Securities, available-for-sale	23,088	23,088	29,992	29,992
Loans held for sale	968,929	968,929	86,075	86,075
Derivative assets	37,878	37,878	35,292	35,292
Level 3 inputs:				
Loans held for investment, net	17,330,223	17,347,199	16,570,839	16,576,297
<b>Financial liabilities:</b>				
Level 2 inputs:				
Federal funds purchased	101,800	101,800	74,164	74,164
Customer repurchase agreements	7,775	7,775	68,887	68,887
Other borrowings	2,000,000	2,000,000	1,500,000	1,500,000
Subordinated notes	281,044	304,672	280,682	291,091
Derivative liabilities	26,240	26,240	35,420	35,420
Level 3 inputs:				
Deposits	17,016,831	17,017,221	15,084,619	15,085,080
Trust preferred subordinated debentures	113,406	113,406	113,406	113,406

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

**Cash and cash equivalents**

The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents approximate their fair value, and these financial instruments are characterized as Level 1 assets in the fair value hierarchy.

**Securities**

Within the securities available-for-sale portfolio, we hold equity securities related to our non-qualified deferred compensation plan which are valued using quoted market prices for identical equity securities in an active market. These financial instruments are classified as Level 1 assets in the fair value hierarchy. The fair value of the remaining investment portfolio is based on prices obtained from independent pricing services which are based on quoted market prices for the same or similar securities, and these financial instruments are characterized as Level 2 assets in the fair value hierarchy. We have obtained documentation



Table of Contents

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 sale

Fair value for loans held for sale valued under the fair value option is derived from quoted market prices for similar loans, and these financial instruments are characterized as Level 2 assets in the fair value hierarchy.

Loans held for investment, net

Loans held for investment are characterized as Level 3 assets in the fair value hierarchy. For variable-rate loans held for investment 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 held for investment is estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. The carrying amount of accrued interest approximates its fair value.

Derivatives

The estimated fair value of the interest rate swaps and caps is obtained from independent pricing services based on quoted market prices for similar derivative contracts and these financial instruments are characterized as Level 2 assets in the fair value hierarchy. On a quarterly basis, we independently verify the fair value using an additional independent pricing source. Any significant differences are investigated and resolved. The derivative instruments related to the loans held for sale portfolio include loan purchase commitments and forward sales commitments. Loan purchase commitments are valued based upon the fair value of the underlying mortgage loans to be purchased, which is based on observable market data for similar loans. Forward sales commitments are valued based upon the quoted market prices from brokers. As such, these loan purchase commitments and forward sales commitments are classified as Level 2 assets in the fair value hierarchy.

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 certificates of deposit fair values are estimated using a discounted cash flow calculation that applies interest rates currently being offered on 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 value reported in the consolidated balance sheets for Federal funds purchased, customer repurchase agreements and other short-term, floating rate borrowings approximates their fair value, and these financial instruments are characterized as Level 2 liabilities in the fair value hierarchy. The fair value 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, and these financial instruments are characterized as Level 3 liabilities in the fair value hierarchy. The subordinated notes are publicly, though infrequently, traded and are valued based on market prices, and are characterized as Level 2 liabilities in the fair value hierarchy.

(17) Commitments and Contingencies

We lease various premises under operating leases with various expiration dates ranging from October 2017 through April 2027. Rent expense incurred under operating leases totaled approximately \$13.9 million, \$15.3 million and \$13.6 million for the years ended December 31, 2016, 2015 and 2014, respectively.

Table of Contents

Minimum future lease payments under operating leases are as follows (in thousands):

Year ending December 31,	Minimum Payments
2017	\$ 16,243
2018	16,750
2019	16,464
2020	15,623
2021	13,152
2022 and thereafter	30,375
	\$ 108,607

## (18) Parent Company Only

Summarized financial information for Texas Capital Bancshares, Inc. – Parent Company Only follows (in thousands):

## Balance Sheet

	December 31,	
	2016	2015
Assets		
Cash and cash equivalents	\$ 220,499	\$ 53,061
Investment in subsidiaries	1,927,392	1,714,158
Other assets	85,560	83,670
Total assets	\$ 2,233,451	\$ 1,850,889
Liabilities and Stockholders' Equity		
Other liabilities	\$ 1,284	\$ 1,119
Subordinated notes	108,412	108,311
Trust preferred subordinated debentures	113,406	113,406
Total liabilities	223,102	222,836
Preferred stock	150,000	150,000
Common stock	495	459
Additional paid-in capital	965,620	724,698
Retained earnings	893,827	752,186
Treasury stock	(8	) (8
Accumulated other comprehensive income	415	718
Total stockholders' equity	2,010,349	1,628,053
Total liabilities and stockholders' equity	\$ 2,233,451	\$ 1,850,889

Table of Contents

## Statement of Earnings

	Year ended December 31,		
	2016	2015	2014
Interest on loans	\$3,250	\$3,250	\$10,850
Dividend income	10,400	10,400	5,275
Other income	90	76	28
Total income	13,740	13,726	16,153
Other non-interest income	152	8	—
Interest expense	10,525	9,867	10,038
Salaries and employee benefits	431	499	617
Legal and professional	1,429	1,640	2,237
Other non-interest expense	1,594	1,637	933
Total expense	13,979	13,643	13,825
Income (loss) before income taxes and equity in undistributed income of subsidiary	(87	) 91	2,328
Income tax expense (benefit)	(33	) 33	833
Income (loss) before equity in undistributed income of subsidiary	(54	) 58	1,495
Equity in undistributed income of subsidiary	151,445	141,041	132,980
Net income	151,391	141,099	134,475
Preferred stock dividends	9,750	9,750	9,750
Net income available to common stockholders	\$141,641	\$131,349	\$124,725

Table of Contents

## Statements of Cash Flows

	Year ended December 31,		
	2016	2015	2014
	(in thousands)		
<b>Operating Activities</b>			
Net income	\$151,391	\$141,099	\$134,475
Adjustments to reconcile net income to net cash used in operating activities:			
Equity in undistributed income of subsidiary	(151,445 )	(141,041 )	(132,980 )
Amortization	101	100	101
Increase in other assets	(10 )	(2,223 )	(2,221 )
Excess tax benefits from stock-based compensation arrangements	(2,013 )	(1,499 )	(2,929 )
Increase in other liabilities	165	(209 )	74
Net cash used in operating activities of continuing operations	(1,811 )	(3,773 )	(3,480 )
<b>Investing Activities</b>			
Investments in and advances to subsidiaries	(57,000 )	(110,000 )	(100,000 )
Net cash used in investing activities	(57,000 )	(110,000 )	(100,000 )
<b>Financing Activities</b>			
Proceeds from sale of stock related to stock-based awards	(2,481 )	(1,239 )	(2,203 )
Proceeds from sale of common stock	236,467	—	256,223
Preferred dividends paid	(9,750 )	(9,750 )	(9,750 )
Net other borrowings	—	—	(15,000 )
Excess tax benefits from stock-based compensation arrangements	2,013	1,499	2,929
Net cash provided by (used in) financing activities	226,249	(9,490 )	232,199
Net increase (decrease) in cash and cash equivalents	167,438	(123,263 )	128,719
Cash and cash equivalents at beginning of year	53,061	176,324	47,605
Cash and cash equivalents at end of year	\$220,499	\$53,061	\$176,324

## (19) Related Party Transactions

See Note 8 for a description of deposits from related parties.

## (20) 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 2016 and 2015, we entered into certain interest rate derivative positions that were 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.

During 2016 and 2015, we also entered into loan purchase commitment contracts with mortgage originators to purchase residential mortgage loans at a future date, as well as forward sales commitment contracts to sell residential mortgage loans at a future date.



Table of Contents

The notional amounts and estimated fair values of interest rate derivative positions outstanding at December 31, 2016 and 2015 presented in the following table (in thousands):

	December 31, 2016			December 31, 2015		
	Notional Amount	Estimated Fair Value		Notional Amount	Estimated Fair Value	
Asset Derivative		Liability Derivative	Asset Derivative		Liability Derivative	
Non-hedging interest rate derivatives:						
Financial institution counterparties:						
Commercial loan/lease interest rate swaps	\$1,144,367	\$1,754	\$25,421	\$976,389	\$—	\$33,851
Commercial loan/lease interest rate caps	210,996	819	—	194,304	1,441	—
Customer counterparties:						
Commercial loan/lease interest rate swaps	1,144,367	25,421	1,754	976,389	33,851	—
Commercial loan/lease interest rate caps	210,996	—	819	194,304	—	1,441
Economic hedging interest rate derivatives:						
Loan purchase commitments	237,805	1,351	—	62,835	—	109
Forward sale commitments	1,218,000	10,287	—	143,200	—	19
Gross derivatives		39,632	27,994		35,292	35,420
Offsetting derivative assets/liabilities		(1,754)	(1,754)		—	—
Net derivatives included in the consolidated balance sheets		\$37,878	\$26,240		\$35,292	\$35,420

The weighted-average receive and pay interest rates for interest rate swaps outstanding at December 31, 2016 and 2015 were as follows:

	December 31, 2016				December 31, 2014			
	Weighted-Average Interest Rate		Weighted-Average Interest Rate		Weighted-Average Interest Rate		Weighted-Average Interest Rate	
	Received	Paid	Received	Paid	Received	Paid	Received	Paid
Non-hedging interest rate swaps	3.17	%	4.58	%	2.96	%	4.72	%

The weighted-average strike rate for outstanding interest rate caps was 2.45% at December 31, 2016 and 2.34% at December 31, 2015.

Our credit exposure on derivative instruments is limited to the net favorable value and interest payments by each counterparty. In such cases collateral may be required from the counterparties involved if the net value of the derivative instruments exceed a nominal amount considered to be immaterial. Our credit exposure, net of any collateral pledged, was approximately \$37.9 million at December 31, 2016 and approximately \$35.3 million at December 31, 2015, 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 December 31, 2016 and December 31, 2015, we had \$24.8 million and \$37.1 million in cash collateral pledged for these derivatives, all of which was included in interest-bearing deposits.

**(21) Stockholders' Equity**

In January 2014, we completed a sale of 1.9 million shares of our common stock in a public offering. Net proceeds from the sale totaled \$106.5 million. The net proceeds of the offering were available to the Company for general corporate purposes, including retirement of \$15.0 million of short-term debt that was outstanding at December 31, 2013, and additional capital to support continued loan growth.

On November 12, 2014, we completed a sale of 2.5 million shares of our common stock in a public offering. Net proceeds from the sale totaled \$149.6 million. The additional equity was used for general corporate purposes and additional capital to support continued loan growth.

On December 2, 2016, we completed a sale of 3.45 million shares of our common stock in a public offering. Net proceeds from the sale totaled \$236.4 million. The additional equity will be used for general corporate purposes,

including repayment of \$20.0 million of short-term debt and as additional capital to support continued loan growth.  
(22) Quarterly Financial Data (unaudited)

92

---

Table of Contents

The tables below summarize our quarterly financial information for the years December 31, 2016 and 2015 (in thousands except per share and average share data):

	2016 Selected Quarterly Financial Data			
	Fourth	Third	Second	First
Interest income	\$188,671	\$182,492	\$172,442	\$159,803
Interest expense	17,448	15,753	15,373	15,020
Net interest income	171,223	166,739	157,069	144,783
Provision for credit losses	9,000	22,000	16,000	30,000
Net interest income after provision for credit losses	162,223	144,739	141,069	114,783
Non-interest income	18,835	16,716	13,932	11,297
Non-interest expense	106,523	94,799	94,255	86,820
Income before income taxes	74,535	66,656	60,746	39,260
Income tax expense	26,149	23,931	21,866	14,132
Net income	48,386	42,725	38,880	25,128
Preferred stock dividends	2,437	2,438	2,437	2,438
Net income available to common stockholders	\$45,949	\$40,287	\$36,443	\$22,690
Basic earnings per share:	\$0.97	\$0.88	\$0.79	\$0.49
Diluted earnings per share:	\$0.96	\$0.87	\$0.78	\$0.49
Average shares				
Basic	47,156,000	45,981,000	45,924,000	45,889,000
Diluted	47,760,000	46,510,000	46,438,000	46,354,000

	2015 Selected Quarterly Financial Data			
	Fourth	Third	Second	First
Interest income	\$154,820	\$153,856	\$153,374	\$140,908
Interest expense	12,632	11,808	11,089	10,899
Net interest income	142,188	142,048	142,285	130,009
Provision for credit losses	14,000	13,750	14,500	11,000
Net interest income after provision for credit losses	128,188	128,298	127,785	119,009
Non-interest income	11,320	11,380	12,771	12,267
Non-interest expense	87,042	81,688	81,276	76,517
Income before income taxes	52,466	57,990	59,280	54,759
Income tax expense	17,713	20,876	21,343	19,709
Net income	34,753	37,114	37,937	35,050
Preferred stock dividends	2,437	2,438	2,437	2,438
Net income available to common stockholders	\$32,316	\$34,676	\$35,500	\$32,612
Basic earnings per share:	\$0.70	\$0.76	\$0.78	\$0.71
Diluted earnings per share:	\$0.70	\$0.75	\$0.76	\$0.70
Average shares				
Basic	45,856,000	45,828,000	45,790,000	45,759,000
Diluted	46,480,000	46,471,000	46,443,000	46,368,000

## (23) New Accounting Standards

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



Table of Contents

2014-09 was originally effective for annual and interim periods beginning after December 15, 2016; however, the FASB issued ASU 2015-14 - "Revenue from Contracts with Customers (Topic 606) - Deferral of the Effective Date" which deferred the effective date of ASU 2014-09 by one year to annual and interim periods beginning after December 15, 2017. The guidance does not apply to revenue associated with financial instruments, including loans and securities that are accounted for under other GAAP, which comprises a significant portion of our revenue stream. Adoption of ASU 2014-09 may require us to amend how we recognize certain recurring revenue streams related to trust fees, which are recorded in non-interest income; however, we do not expect adoption of ASU 2014-09 to have a material impact on our consolidated financial statements and disclosures. We plan to adopt the revenue recognition guidance in the first quarter of 2018 with a cumulative effect adjustment to opening retained earnings, if management deems such adjustment significant. Our implementation efforts to date include identification of revenue streams within the scope of the guidance, and we have begun review of revenue contracts.

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. ASU 2014-12 became effective for us on January 1, 2016 and did not have a significant impact on our consolidated financial statements.

ASU 2015-01 "Income Statement - Extraordinary and Unusual Items (Subtopic 225-20) - Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items" ("ASU 2015-01") eliminates from U.S. GAAP the concept of extraordinary items, which required separate classification, presentation and disclosure in the income statement. ASU 2015-01 became effective for us on January 1, 2016 and did not have a significant impact on our consolidated financial statements.

ASU 2015-03 "Interest - Imputation of Interest (Subtopic 835-30) - Simplifying the Presentation of Debt Issuance Costs" ("ASU 2015-03") requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. Prior to the issuance of ASU 2015-03, debt issuance costs were required to be presented as deferred charge assets, separate from the related debt liability. ASU 2015-03 does not change the recognition and measurement requirements for debt issuance costs. We adopted ASU 2015-03 effective January 1, 2016 and applied its provisions retrospectively. The adoption of ASU 2015-03 resulted in \$5.3 million of unamortized debt issuance costs related to our subordinated notes being reclassified from other assets to subordinated notes within the consolidated balance sheets as of December 31, 2015, respectively. Other than this reclassification, the adoption of ASU 2015-03 did not have a material impact on our consolidated financial statements.

ASU 2015-05 "Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40) - Customer's Accounting for Fees Paid in a Cloud Computing Arrangement" ("ASU 2015-05") provides guidance to customers about whether a cloud computing arrangement includes a software license. If the arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If the arrangement does not include a software license, the customer should account for the arrangement as a service contract. ASU 2015-05 became effective for us on January 1, 2016 and did not have a significant impact on our consolidated financial statements.

ASU 2015-15 "Interest - Imputation of Interest (Subtopic 835-30) - Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements - Amendments to SEC Paragraphs Pursuant to Staff Announcement at June 18, 2015 EITF Meeting ("ASU 2015-15") adds SEC paragraphs confirming that, given the absence of authoritative guidance within ASU 2015-03 for debt issuance costs related to line-of-credit arrangements, the SEC staff would not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. ASU 2015-15 was effective when issued and did not have a significant impact on our consolidated financial statements.

ASU 2016-02 "Leases (Topic 842)" ("ASU 2016-02") requires that lessees and lessors recognize lease assets and lease liabilities on the balance sheet and disclose key information about leasing arrangements. ASU 2016-02 is effective for

public companies for annual periods beginning after December 15, 2018, including interim periods within those fiscal years. We have not yet selected a transition method as we are in the process of determining the effect of the standard on our consolidated financial statements and disclosures.

ASU 2016-09 "Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payments Accounting" ("ASU 2016-09") amended guidance with the intent to simplify accounting for share-based payment transaction, including the income tax consequences and classification of awards. Among other items, the update requires excess tax benefits and deficiencies to be recognized as a component of income taxes within the income statement rather than other comprehensive income as required in current guidance. ASU 2016-09 is effective for public companies for annual periods beginning after December 31, 2016 and is not expected to have a significant impact on our consolidated financial statements.

Table of Contents

ASU 2016-13 "Financial Instruments - Credit Losses (Topic 326)" ("ASU 2016-13") requires an entity to utilize a new impairment model known as the current expected credit loss ("CECL") model to estimate its lifetime "expected credit loss" and record an allowance that, when deducted from the amortized cost basis of the financial asset, presents the net amount expected to be collected on the financial asset. The CECL model is expected to result in more timely recognition of credit losses. ASU 2016-13 also requires new disclosures for financial assets measured at amortized cost, loans and available-for-sale debt securities. ASU 2016-13 is effective for public companies for annual periods beginning after December 15, 2019, including interim periods within those fiscal years. Entities will apply the standard's provisions as a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is adopted. We are currently evaluating the impact adoption of ASU 2016-13 will have on our consolidated financial statements and disclosures.

ASU 2016-15 "Statement of Cash Flows (Topic 230)" ("ASU 2016-15") is intended to reduce the diversity in practice around how certain transactions are classified within the statement of cash flows. ASU 2016-15 is effective for public companies for annual periods beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted with retrospective application. We are currently evaluating the impact adoption of ASU 2016-15 will have on our consolidated financial statements.

Table of Contents

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. 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(e) 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.

Management's Report on Internal Control over Financial Reporting

The management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting. Our internal control over financial reporting is a process designed under the supervision of our Chief Executive Officer and Chief Financial Officer to provide reasonable assurance regarding the reliability of financial reporting and the preparation of our financial statements for external purposes in accordance with generally accepted accounting principles.

As of December 31, 2016, management assessed the effectiveness of the Company's internal control over financial reporting based on the criteria for effective internal control over financial reporting established in "Internal Control—Integrated Framework (2013)," issued by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission. Based on the assessment, management determined that the Company maintained effective internal control over financial reporting as of December 31, 2016.

Ernst & Young LLP, the independent registered public accounting firm that audited the consolidated financial statements of the Company included in this Annual Report on Form 10-K, has issued an attestation report on the effectiveness of the Company's internal control over financial reporting as of December 31, 2016. The report, which expresses an unqualified opinion on the effectiveness of the Company's internal control over financial reporting as of December 31, 2016, is included in this Item under the heading "Report of Independent Registered Public Accounting Firm."



Table of Contents

Report of Independent Registered Public Accounting Firm  
The Board of Directors and Shareholders of  
Texas Capital Bancshares, Inc.

We have audited Texas Capital Bancshares, Inc.'s internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). Texas Capital Bancshares Inc.'s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

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

In our opinion, Texas Capital Bancshares Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Texas Capital Bancshares, Inc. as of December 31, 2016 and 2015, and the related consolidated statements of income and other comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2016 and our report dated February 17, 2017 expressed an unqualified opinion thereon.

Dallas, Texas  
February 17, 2017

Table of Contents

ITEM 9B. OTHER INFORMATION

None.

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Information required by this item is set forth in our definitive proxy materials regarding our annual meeting of stockholders to be held April 18, 2017, which proxy materials will be filed with the SEC no later than March 9, 2017.

ITEM 11. EXECUTIVE COMPENSATION

Information required by this item is set forth in our definitive proxy materials regarding our annual meeting of stockholders to be held April 18, 2017, which proxy materials will be filed with the SEC no later than March 9, 2017.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

Information required by this item is set forth in our definitive proxy materials regarding our annual meeting of stockholders to be held April 18, 2017, which proxy materials will be filed with the SEC no later than March 9, 2017.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Information required by this item is set forth in our definitive proxy materials regarding our annual meeting of stockholders to be held April 18, 2017, which proxy materials will be filed with the SEC no later than March 9, 2017.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

Information required by this item is set forth in our definitive proxy materials regarding our annual meeting of stockholders to be held April 18, 2017, which proxy materials will be filed with the SEC no later than March 9, 2017.

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a) Documents filed as part of this report

(1) All financial statements

Independent Registered Public Accounting Firm's Report of Ernst & Young LLP

(2) All financial statements required by Item 8

Independent Registered Public Accounting Firm's Report of Ernst & Young LLP

Table of Contents

(3) Exhibits

- 3.1 Certificate of Incorporation, which is incorporated by reference to Exhibit 3.1 to our registration statement on Form 10 dated August 24, 2000
- 3.2 Certificate of Amendment of Certificate of Incorporation, which is incorporated by reference to Exhibit 3.2 to our registration statement on Form 10 dated August 24, 2000
- 3.3 Certificate of Amendment of Certificate of Incorporation, which is incorporated by reference to Exhibit 3.3 to our registration statement on Form 10 dated August 24, 2000
- 3.4 Certificate of Amendment of Certificate of Incorporation, which is incorporated by reference to Exhibit 3.4 to our registration statement on Form 10 dated August 24, 2000
- 3.5 Amended and Restated Bylaws of Texas Capital Bancshares, Inc. which is incorporated by reference to Exhibit 3.5 to our registration statement on Form 10 dated August 24, 2000
- 3.6 First Amendment to Amended and Restated Bylaws of Texas Capital Bancshares, Inc. which is incorporated by reference to Current Report on Form 8-K dated July 18, 2007
- 3.7 Certificate of Designation of 6.50% Non-Cumulative Perpetual Preferred Stock, Series A, which is incorporated by reference to Exhibit 4.1 to our Current Report on form 8-K dated March 28, 2013
- 3.8 Form of Preferred Stock Certificate for 6.50% Non-Cumulative Perpetual Preferred Stock, Series A, which is incorporated by reference to Exhibit 4.2 to our Current report on Form 8-K dated March 28, 2013
- 4.1 Placement Agreement by and between Texas Capital Bancshares Statutory Trust I and SunTrust Capital Markets, Inc., which is incorporated by reference to our Current Report on Form 8-K dated December 4, 2002
- 4.2 Certificate of Trust of Texas Capital Bancshares Statutory Trust I, dated November 12, 2002 which is incorporated by reference to our Current Report on Form 8-K dated December 4, 2002
- 4.3 Amended and Restated Declaration of Trust by and among State Street Bank and Trust Company of Connecticut, National Association, Texas Capital Bancshares, Inc. and Joseph M. Grant, Raleigh Hortenstine III and Gregory B. Hultgren, dated November 19, 2002 which is incorporated by reference to our Current Report on Form 8-K dated December 4, 2002
- 4.4 Indenture dated November 19, 2002 which is incorporated by reference to our Current Report on Form 8-K dated December 4, 2002
- 4.5 Guarantee Agreement between Texas Capital Bancshares, Inc. and State Street Bank and Trust of Connecticut, National Association dated November 19, 2002, which is incorporated by reference to our Current Report on Form 8-K dated December 4, 2002
- 4.6 Placement Agreement by and among Texas Capital Bancshares, Inc., Texas Capital Statutory Trust II and Sandler O'Neill & Partners, L.P., which is incorporated by reference to our Current Report Form 8-K dated June 11, 2003
- 4.7 Certificate of Trust of Texas Capital Statutory Trust II, which is incorporated by reference to our Current Report on Form 8-K dated June 11, 2003
- 4.8 Amended and Restated Declaration of Trust by and among Wilmington Trust Company, Texas Capital Bancshares, Inc., and Joseph M. Grant and Gregory B. Hultgren, dated April 10, 2003, which is incorporated by reference to our Current Report on Form 8-K dated June 11, 2003
- 4.9 Indenture between Texas Capital Bancshares, Inc. and Wilmington Trust Company, dated April 10, 2003, which is incorporated by reference to our Current Report on Form 8-K dated June 11, 2003
- 4.10 Guarantee Agreement between Texas Capital Bancshares, Inc. and Wilmington Trust Company, dated April 10, 2003, which is incorporated by reference to our Current Report on Form 8-K dated June 11, 2003

Table of Contents

- 4.11 Amended and Restated Declaration of Trust for Texas Capital Statutory Trust III by and among Wilmington Trust Company, as Institutional Trustee and Delaware Trustee, Texas Capital Bancshares, Inc. as Sponsor, and the Administrators named therein, dated as of October 6, 2005, which is incorporated by reference to our Current Report on Form 8-K dated October 13, 2005
- 4.12 Indenture between Texas Capital Bancshares, Inc., as Issuer, and Wilmington Trust Company, as Trustee, for Fixed/Floating Rate Junior Subordinated Deferrable Interest Debentures, dated as of October 6, 2005, which is incorporated by reference to our Current Report on Form 8-K dated October 13, 2005
- 4.13 Guarantee Agreement between Texas Capital Bancshares, Inc. and Wilmington Trust Company, dated as of October 6, 2005, which is incorporated by reference to our Current Report on Form 8-K dated October 13, 2005
- 4.14 Amended and Restated Declaration of Trust for Texas Capital Statutory Trust IV by and among Wilmington Trust Company, as Institutional Trustee and Delaware Trustee, Texas Capital Bancshares, Inc. as Sponsor, and the Administrators named therein, dated as of April 28, 2006, which is incorporated by reference to our Current Report on Form 8-K dated May 3, 2006
- 4.15 Indenture between Texas Capital Bancshares, Inc., as Issuer, and Wilmington Trust Company, as Trustee, for Floating Rate Junior Subordinated Deferrable Interest Debentures dated as of April 28, 2006, which is incorporated by reference to our Current Report on Form 8-K dated May 3, 2006
- 4.16 Guarantee Agreement between Texas Capital Bancshares, Inc. and Wilmington Trust Company, dated as of April 28, 2006, which is incorporated by reference to our Current Report on Form 8-K dated May 3, 2006
- 4.17 Amended and Restated Trust Agreement for Texas Capital Statutory Trust V by and among Wilmington Trust Company, as Property Trustee and Delaware Trustee, Texas Capital Bancshares, Inc., as Depositor, and the Administrative Trustees named therein, dated as of September 29, 2006, which is incorporated by reference to our Current Report on Form 8-K dated October 5, 2006
- 4.18 Junior Subordinated Indenture between Texas Capital Bancshares, Inc. and Wilmington Trust Company, as Trustee, for Floating Rate Junior Subordinated Note dated as of September 29, 2006, which is incorporated by reference to our Current Report on Form 8-K dated October 5, 2006
- 4.19 Guarantee Agreement between Texas Capital Bancshares, Inc. and Wilmington Trust Company, dated as of September 29, 2006, which is incorporated by reference to our Current Report on Form 8-K dated October 5, 2006
- 4.20 Subordinated Indenture between Texas Capital Bancshares, Inc. and U.S. Bank National Association, as Trustee, dated September 21, 2012, which is incorporated by reference to our Current Report on Form 8-K dated September 18, 2012
- 4.21 Issuing and Paying Agency Agreement, dated January 31, 2014, between Texas Capital Bank, N.A., as Issuer, and U.S. Bank National Association, as Agent, which is incorporated by reference to our Current Report on Form 8-K dated January 31, 2014.
- 4.22 Form of Global 5.25% Subordinated Note due 2026, which is incorporated by reference to our Current Report on Form 8-K dated January 31, 2014.

Table of Contents

- Retirement Transition Agreement and Release dated June 10, 2013, between Texas Capital Bancshares, Inc. and George F. Jones, Jr., which is incorporated by reference to Exhibit 99.2 to our Current Report on Form 8-K dated June 11, 2013+
- 10.1 Amendment to Performance Award Agreements under the Texas Capital Bancshares, Inc. 2010 Long-Term Incentive Plan between George Jones and the Company with respect to the Performance Units described therein dated January 10, 2011, February 21, 2012 and March 2013 and the Stock Appreciation Rights Agreement between George Jones and the Company dated April 24, 2006, which is incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K dated January 3, 2014+
- 10.2 Restricted Stock Unit Award Agreement under the Texas Capital Bancshares, Inc. 2010 Long-Term Incentive Plan between George Jones and the Company (2017 vesting), which is incorporated by reference to Exhibit 10.3 to our Current Report on Form 8-K dated January 3, 2014+
- 10.3 Restricted Stock Unit Award Agreement under the Texas Capital Bancshares, Inc. 2010 Long-Term Incentive Plan between George Jones and the Company (2018 vesting), which is incorporated by reference to Exhibit 10.3 to our Current Report on Form 8-K dated January 3, 2014+
- 10.4 Amended and Restated Executive Employment Agreement between C. Keith Cargill and Texas Capital Bancshares, Inc. dated December 18, 2014, which is incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K dated December 18, 2014+
- 10.5 Form of Amended and Restated Executive Employment Agreement for executive officers of Texas Capital Bancshares, Inc., which is incorporated by reference to Exhibit 10.2 to our Current Report on Form 8-K dated December 18, 2014+
- 10.6 Form of Indemnity Agreement for directors and officers of Texas Capital Bancshares, Inc., which is incorporated by reference to Exhibit 10.14 to our Annual Report on Form 10-K dated February 21, 2014+
- 10.7 Texas Capital Bancshares, Inc. 2005 Long-Term Incentive Plan, which is incorporated by reference to our registration statement on Form S-8 dated June 3, 2005+
- 10.8 Texas Capital Bancshares, Inc. 2006 Employee Stock Purchase Plan, which is incorporated by reference to our registration statement on Form S-8 dated February 3, 2006+
- 10.9 Texas Capital Bancshares, Inc. 2010 Long-Term Incentive Plan, which is incorporated by reference to our registration statement on Form S-8 dated May 19, 2010+
- 10.10 Texas Capital Bancshares, Inc. 2015 Long-Term Incentive Plan, which is incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K dated May 21, 2015+
- 10.11 Form of Restricted Stock Unit Award Agreement under the Texas Capital Bancshares, Inc. 2010 Long-Term Incentive Plan, which is incorporated by reference to Exhibit 10.19 to our Annual Report on Form 10-K dated February 21, 2014+
- 10.12 Form of Stock Appreciation Rights Agreement under the Texas Capital Bancshares, Inc. 2010 Long-Term Incentive Plan, which is incorporated by reference to Exhibit 10.20 to our Annual Report on Form 10-K dated February 21, 2014+
- 10.13 Form of Performance Award Agreement under the Texas Capital Bancshares, Inc. 2010 Long-Term Incentive Plan, which is incorporated by reference to Exhibit 10.21 to our Annual Report on Form 10-K dated February 21, 2014+
- 10.14 Form of Restricted Stock Unit Award Agreement for directors under the Texas Capital Bancshares, Inc. 2015 Long-Term Incentive Plan, which is incorporated by reference to Exhibit 10.2 to our Quarterly Report on Form 10-Q dated July 23, 2015+
- 10.15 Form of Restricted Stock Unit Award Agreement for executive officers under the Texas Capital Bancshares, Inc. 2015 Long-Term Incentive Plan, which is incorporated by reference to Exhibit 10.3 to our Quarterly Report on Form 10-Q dated July 23, 2015+
- 10.16 Special Retention Restricted Stock Unit Award Agreement between Julie Anderson and Texas Capital Bancshares, Inc. dated May 17, 2016, which is incorporated by reference to Exhibit 10.1 to our Quarterly Report on Form 10-Q dated July 21, 2016+
- 10.17

- Form of Performance Award Agreement for Executive Officers under the Texas Capital Bancshares, Inc. 2015  
10.18 Long-Term Incentive Plan, which is incorporated by reference to Exhibit 10.1 to our Quarterly Report on Form  
10-Q dated October 20, 2016+  
10.19 Texas Capital Bancshares, Inc. Nonqualified Deferred Compensation Plan+\*

101

---

Table of Contents

21	Subsidiaries of the Registrant*
23.1	Consent of Ernst & Young LLP*
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Exchange Act*
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Exchange Act*
32.1	Section 1350 Certification of Chief Executive Officer**
32.2	Section 1350 Certification of Chief Financial Officer**
101.INS	XBRL Instance Document*
101.SCH	XBRL Taxonomy Extension Schema Document*
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document*
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document*
101.LAB	XBRL Taxonomy Extension Label Linkbase Document*
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document*

\* Filed herewith

\*\*Furnished herewith

+Management contract or compensatory plan arrangement

102

---

Table of Contents

SIGNATURES

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

Date: February 17, 2017 TEXAS CAPITAL BANCSHARES, INC.

By: /S/ C. KEITH CARGILL  
C. Keith Cargill  
President and Chief Executive Officer

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

Date: February 17, 2017 /S/ LARRY L. HELM

Larry L. Helm  
Chairman of the Board and Director

Date: February 17, 2017 /S/ PETER BARTHLOW

Peter Bartholow  
Chief Financial Officer, and Director  
(principal financial officer)

Date: February 17, 2017 /S/ JULIE ANDERSON

Julie Anderson  
Controller and Chief Accounting Officer  
(principal accounting officer)

Date: February 17, 2017 /S/ JAMES H. BROWNING

James H. Browning  
Director

Date: February 17, 2017 /S/ PRESTON M. GEREN III

Preston M. Geren III  
Director

Date: February 17, 2017 /S/ CHARLES S. HYLE

Charles S. Hyle  
Director

Date: February 17, 2017 /S/ ELYSIA H. RAGUSA

Elysia H. Ragusa  
Director

Date: February 17, 2017 /S/ STEVEN P. ROSENBERG

Steven P. Rosenberg  
Director

Date: February 17, 2017 /S/ ROBERT W. STALLINGS

Robert W. Stallings  
Director

Date: February 17, 2017 /S/ DALE W. TREMBLAY

Dale W. Tremblay



Director

Date: February 17, 2017 /S/ IAN J. TURPIN

Ian J. Turpin

Director

Date: February 17, 2017 /S/ PATRICIA A. WATSON

Patricia A. Watson

Director