TEXAS CAPITAL BANCSHARES INC/TX
Form 10-K
February 17, 2017
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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, Dallas, Texas, U.S.A.	75201
(Address of principal executive officers)	(Zip Code)

214/932-6600
(Registrant's telephone number, including area code)
N/A
(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)
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 ý 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 ý
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý ¨ No
Indicate by check mark 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"

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

Large Accelerated Filer x   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 ý

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.

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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

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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.

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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.

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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 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.

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.

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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 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, 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 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 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. 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.

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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 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.

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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.

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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 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.

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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;

- 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 MSRs 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

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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

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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 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

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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

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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.

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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.

	Price Per Share	
Quarter Ended	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

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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

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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

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	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	46,239,21[illegible]	45,808,440	43,236,344	40,864,225	39,046,340
Diluted	46,765,90[illegible]	46,437,872	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 %

(1) The consolidated operating data and consolidated balance sheet data presented above for the five most recent fiscal 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.

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(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.

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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,” “exp “intends,” “seeks,” “likely,” “targeted,” “continue,” “remain,” “will,” “should,” “may” and other similar expressions are intend 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.

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- 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 MSRs related to these loans and related interest rate risk resulting from retaining MSRs, 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 MSRs 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 MSRs. 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

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$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

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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,					
	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.

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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)
Assets									
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		
Liabilities and stockholders’ equity									
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.

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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

(1) Other non-interest income includes such items as letter of credit fees, gain on sale of loans held for sale, servicing 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

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

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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.

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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	%

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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	%

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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

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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 of Relationships	Committed	Outstanding	Number of Relationships	Committed	Outstanding
$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 Balance		2015 Average 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

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

	Remaining Maturities of Selected Loans			
(in thousands)	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.

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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

(1) If these loans had been current throughout their terms, interest and fees on loans would have increased by 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.

(3) At December 31, 2016, 2015 and 2014, there was no valuation allowance recorded against the OREO balance. 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.

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.

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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.

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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

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	x

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(1) If these loans had been current throughout their terms, interest and fees on loans would have increased by 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.

(3) At December 31, 2016, 2015 and 2014, we did not have a valuation allowance recorded against the OREO balance. 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

	December 31, 2016		2015		2014		2013		2012	
(in thousands except percentage data)	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.

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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

	December 31,		
(In thousands)	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

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Liquidity and Capital Resources

In general terms, liquidity is a measurement of our ability to meet our cash needs. Our objective in managing our liquidity is to maintain our ability to meet loan commitments, 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):

	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,								
	2016			2015			2014		
	Balance	Rate(3)	Maximum Outstanding at Any Month End	Balance	Rate(3)	Maximum Outstanding at Any Month End	Balance	Rate(3)	Maximum Outstanding at Any Month End
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%	
Total borrowings	$2,109,575		$2,117,280	$1,643,051		$1,643,051	$1,192,681		$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.

(2) 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 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.

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

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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 Within Three Years	After Three But Within Five Years	After Five Years	Total
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

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.

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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

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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
Assets:					
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
Liabilities					
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.

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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.

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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Consolidated Statements of Income and Other Comprehensive Income — Years ended December 31, 2016, 2015 and 2014	55
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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

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TEXAS CAPITAL BANCSHARES, INC.
CONSOLIDATED BALANCE SHEETS

	December 31,	
(in thousands except per share data)	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.

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

	Year ended December 31,		
(In thousands except per share data)	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)

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.

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TEXAS CAPITAL BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	Preferred Stock		Common Stock		Additional Paid-in	Retained	Treasury Stock		Accumulated Other Comprehensive	
(In thousands except share data)	Shares	Amount	Shares	Amount	Capital	Earnings	Shares	Amount	Income	Total
Balance at December 31, 2013	6,000,000	$150,000	41,036,787	$410	$448,208	$496,112	(417)	$(8)	$1,628	$1,096,350
Comprehensive income:										
Net income	—	—	—	—	—	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.

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TEXAS CAPITAL BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year ended December 31,		
(In thousands)	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.

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(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

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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.

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 men