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Independent Bank Group, Inc.
Form 10-Q
October 25, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q
(Mark One)

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.
For the quarterly period ended September 30, 2018.

or
 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 001-35854

Independent Bank Group, Inc.

(Exact name of registrant as specified in its charter)

Texas

13-4219346

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

1600 Redbud Boulevard, Suite 400

75069-3257

McKinney, Texas

(Address of principal executive offices)

(Zip Code)

(972) 562-9004

(Registrant's telephone number, including area code)

Not applicable

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or such shorter periods that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards pursuant to Section 13(a) of the Exchange Act.

Indicate by a check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Applicable Only to Corporate Issuers

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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practical date.

Common Stock, Par Value \$0.01 Per Share – 30,477,648 shares as of October 23, 2018.

INDEPENDENT BANK GROUP, INC. AND SUBSIDIARIES
Form 10-Q
September 30, 2018

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Signatures

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Independent Bank Group, Inc. and Subsidiaries

Consolidated Balance Sheets

September 30, 2018 (unaudited) and December 31, 2017

(Dollars in thousands, except share information)

	September 30, 2018	December 31, 2017
Assets		
Cash and due from banks	\$149,641	\$187,574
Interest-bearing deposits in other banks	140,529	243,528
Cash and cash equivalents	290,170	431,102
Certificates of deposit held in other banks	1,225	12,985
Securities available for sale, at fair value	760,995	763,002
Loans held for sale (includes \$15,964 carried at fair value at September 30, 2018)	27,730	39,202
Loans, net	7,658,989	6,432,273
Premises and equipment, net	156,320	147,835
Other real estate owned	4,610	7,126
Federal Home Loan Bank (FHLB) of Dallas stock and other restricted stock	26,617	29,184
Bank-owned life insurance (BOLI)	128,679	113,170
Deferred tax asset	14,565	9,763
Goodwill	721,784	621,458
Core deposit intangible, net	46,533	43,244
Other assets	53,247	34,119
Total assets	\$9,891,464	\$8,684,463
Liabilities and Stockholders' Equity		
Deposits:		
Noninterest-bearing	\$2,235,377	\$1,907,770
Interest-bearing	5,547,475	4,725,052
Total deposits	7,782,852	6,632,822
FHLB advances	345,000	530,667
Other borrowings	137,207	136,911
Junior subordinated debentures	27,803	27,654
Other liabilities	31,418	20,391
Total liabilities	8,324,280	7,348,445
Commitments and contingencies		
Stockholders' equity:		
Preferred stock (0 and 0 shares outstanding, respectively)	—	—
Common stock (30,477,648 and 28,254,893 shares outstanding, respectively)	305	283
Additional paid-in capital	1,313,981	1,151,990
Retained earnings	267,118	184,232
Accumulated other comprehensive loss	(14,220)	(487)
Total stockholders' equity	1,567,184	1,336,018
Total liabilities and stockholders' equity	\$9,891,464	\$8,684,463
See Notes to Consolidated Financial Statements		

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Independent Bank Group, Inc. and Subsidiaries

Consolidated Statements of Income

Three and Nine Months Ended September 30, 2018 and 2017 (unaudited)

(Dollars in thousands, except per share information)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
Interest income:				
Interest and fees on loans	\$103,104	\$79,325	\$277,993	\$208,263
Interest on taxable securities	3,840	2,539	10,244	5,606
Interest on nontaxable securities	1,103	1,124	3,475	2,657
Interest on interest-bearing deposits and other	1,242	1,684	2,773	3,968
Total interest income	109,289	84,672	294,485	220,494
Interest expense:				
Interest on deposits	17,380	8,033	40,006	20,043
Interest on FHLB advances	3,121	1,749	7,854	4,271
Interest on repurchase agreements and other borrowings	2,100	1,716	6,299	5,137
Interest on junior subordinated debentures	420	317	1,182	819
Total interest expense	23,021	11,815	55,341	30,270
Net interest income	86,268	72,857	239,144	190,224
Provision for loan losses	1,525	1,873	6,950	6,368
Net interest income after provision for loan losses	84,743	70,984	232,194	183,856
Noninterest income:				
Service charges on deposit accounts	3,589	3,677	10,607	9,364
Mortgage banking revenue	5,111	4,569	12,134	10,855
Gain on sale of loans	—	351	—	351
Loss on sale of branch	—	(127)	—	(127)
Gain (loss) on sale of other real estate	95	—	213	(36)
(Loss) gain on sale of securities available for sale	(115)	—	(349)	52
Gain (loss) on sale of premises and equipment	220	(21)	123	(15)
Increase in cash surrender value of BOLI	831	778	2,328	1,959
Other	3,018	2,903	7,281	5,305
Total noninterest income	12,749	12,130	32,337	27,708
Noninterest expense:				
Salaries and employee benefits	30,114	25,684	82,072	69,610
Occupancy	6,613	6,380	18,295	16,399
Data processing	2,989	2,546	7,861	6,449
FDIC assessment	760	1,077	2,213	3,156
Advertising and public relations	583	380	1,300	994
Communications	810	771	2,544	2,098
Other real estate owned expenses, net	62	61	271	223
Impairment of other real estate	—	917	85	1,037
Core deposit intangible amortization	1,519	1,409	4,243	3,311
Professional fees	1,175	1,273	3,427	3,212
Acquisition expense, including legal	1,682	2,428	5,671	8,247
Other	6,348	4,978	18,789	12,524
Total noninterest expense	52,655	47,904	146,771	127,260

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Income before taxes	44,837	35,210	117,760	84,304
Income tax expense	9,141	11,696	23,465	26,985
Net income	\$35,696	\$23,514	\$94,295	\$57,319
Basic earnings per share	\$1.17	\$0.85	\$3.22	\$2.31
Diluted earnings per share	\$1.17	\$0.84	\$3.21	\$2.30

See Notes to Consolidated Financial Statements

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Independent Bank Group, Inc. and Subsidiaries
 Consolidated Statements of Comprehensive Income
 Three and Nine Months Ended September 30, 2018 and 2017 (unaudited)
 (Dollars in thousands)

	Three Months Ended September 30, 2018		Nine Months Ended September 30, 2017	
Net income	\$35,696	\$23,514	\$94,295	\$57,319
Other comprehensive income (loss) before tax:				
Change in net unrealized gains (losses) on available for sale securities during the year	(5,259)	(219)	(17,438)	7,095
Reclassification for amount realized through sales of securities available for sale included in net income	115	—	349	(52)
Other comprehensive income (loss) before tax	(5,144)	(219)	(17,089)	7,043
Income tax expense (benefit)	(1,081)	(77)	(3,589)	2,465
Other comprehensive income (loss), net of tax	(4,063)	(142)	(13,500)	4,578
Comprehensive income	\$31,633	\$23,372	\$80,795	\$61,897
See Notes to Consolidated Financial Statements				

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Independent Bank Group, Inc. and Subsidiaries
Consolidated Statements of Changes in Stockholders' Equity
Nine Months Ended September 30, 2018 and 2017 (unaudited)
(Dollars in thousands, except for par value, share and per share information)

	Preferred Stock \$.01 Par Value 10 million shares authorized	Common Stock \$.01 Par Value 100 million shares authorized	Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Total
Balance, December 31, 2017	\$ —	28,254,893	\$ 283	\$ 1,151,990	\$ 184,232	\$ (487) \$ 1,336,018
Cumulative effect of accounting change	—	—	—	—	233	(233) —
Net income	—	—	—	—	94,295	— 94,295
Other comprehensive loss, net of tax	—	—	—	—	—	(13,500) (13,500)
Stock issued for acquisition of bank, net of offering costs of \$209	—	2,071,981	21	157,033	—	— 157,054
Restricted stock forfeited	—	(3,845)	—	—	—	— —
Restricted stock granted	—	127,712	1	(1)	—	— —
Stock based compensation expense	—	—	—	4,496	—	— 4,496
Exercise of warrants	—	26,907	—	463	—	— 463
Cash dividends (\$0.40 per share)	—	—	—	—	(11,642)	— (11,642)
Balance, September 30, 2018	\$ —	30,477,648	\$ 305	\$ 1,313,981	\$ 267,118	\$ (14,220) \$ 1,567,184
Balance, December 31, 2016	\$ —	18,870,312	\$ 189	\$ 555,325	\$ 117,951	\$ (1,100) \$ 672,365
Net income	—	—	—	—	57,319	— 57,319
Other comprehensive income, net of tax	—	—	—	—	—	4,578 4,578
Stock issued for acquisition of bank, net of offering costs of \$942	—	8,804,699	88	565,112	—	— 565,200
Restricted stock forfeited	—	(67)	—	—	—	— —
Restricted stock granted	—	126,730	1	(1)	—	— —
Stock based compensation expense	—	—	—	3,442	—	— 3,442
Exercise of warrants	—	3,203	—	55	—	— 55
Cash dividends (\$0.30 per share)	—	—	—	—	(7,450)	— (7,450)
Balance, September 30, 2017	\$ —	27,804,877	\$ 278	\$ 1,123,933	\$ 167,820	\$ 3,478 \$ 1,295,509

See Notes to Consolidated Financial Statements

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Independent Bank Group, Inc. and Subsidiaries
Consolidated Statements of Cash Flows
Nine Months Ended September 30, 2018 and 2017 (unaudited)
(Dollars in thousands)

	Nine Months Ended September 30,	
	2018	2017
Cash flows from operating activities:		
Net income	\$94,295	\$ 57,319
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation expense	6,324	6,203
Accretion of income recognized on acquired loans	(9,386)	(4,293)
Amortization of core deposit intangibles	4,243	3,311
Amortization of premium on securities, net	2,768	2,633
Amortization of discount and origination costs on borrowings	475	366
Stock based compensation expense	4,496	3,442
Excess tax benefit on restricted stock vested	(632)	(1,272)
FHLB stock dividends	(538)	(308)
Loss (gain) on sale of securities available for sale	349	(52)
(Gain) loss on sale of premises and equipment	(123)	15
Gain on sale of loans	—	(351)
Loss on sale of branch	—	127
(Gain) loss on sale of other real estate owned	(213)	36
Impairment of other real estate	85	1,037
Deferred tax expense	2,130	3,329
Provision for loan losses	6,950	6,368
Increase in cash surrender value of BOLI	(2,328)	(1,959)
Originations of loans held for sale	(293,756)	(291,330)
Proceeds from sale of loans held for sale	305,228	288,053
Net change in other assets	(15,883)	(2,537)
Net change in other liabilities	1,121	103
Net cash provided by operating activities	105,605	70,240
Cash flows from investing activities:		
Proceeds from maturities, calls and pay downs of securities available for sale	2,213,168	1,390,770
Proceeds from sale of securities available for sale	42,727	17,227
Purchases of securities available for sale	(2,249,373)	(1,497,707)
Purchases of certificates of deposits held in other banks	—	(1,960)
Proceeds from maturities of certificates of deposit held in other banks	11,760	—
Proceeds from sale of loans	—	3,867
Purchase of bank owned life insurance contracts	(5,000)	—
Purchases of FHLB stock and other restricted stock	(6,144)	(48)
Proceeds from redemptions of FHLB stock and other restricted stock	12,606	8,956
Net loans originated held for investment	(587,348)	(386,896)
Originations of mortgage warehouse purchase loans	(3,869,234)	(2,365,799)
Proceeds from pay-offs of mortgage warehouse purchase loans	3,883,661	2,327,560
Additions to premises and equipment	(24,497)	(11,626)

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Proceeds from sale of premises and equipment	14,479	15
Proceeds from sale of other real estate owned	3,054	5,648
Capitalized additions to other real estate	—	(1,032)
Cash received from acquired bank	44,723	148,444
Cash paid in connection with acquisition	(31,016)	(17,773)
Selling costs paid in connection with branch sale	—	(62)
Net cash transferred in branch sale	—	(11,765)
Net cash used in investing activities	(546,434)	(392,181)

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Independent Bank Group, Inc. and Subsidiaries
 Consolidated Statements of Cash Flows (Continued)
 Nine Months Ended September 30, 2018 and 2017 (unaudited)
 (Dollars in thousands)

	Nine Months Ended September 30, 2018	2017
Cash flows from financing activities:		
Net increase in demand deposits, money market and savings accounts	375,045	635,877
Net increase (decrease) in time deposits	181,907	(144,785)
Proceeds from FHLB advances	1,110,000	100,000
Repayments of FHLB advances	(1,355,667)	(59)
Net change in repurchase agreements	—	(2,765)
Proceeds from exercise of common stock warrants	463	55
Offering costs paid in connection with acquired bank	(209)	(942)
Dividends paid	(11,642)	(7,450)
Net cash provided by financing activities	299,897	579,931
Net change in cash and cash equivalents	(140,932)	257,990
Cash and cash equivalents at beginning of year	431,102	505,027
Cash and cash equivalents at end of period	\$ 290,170	\$ 763,017

See Notes to Consolidated Financial Statements

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Independent Bank Group, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (unaudited)

(Dollars in thousands, except for share and per share information)

Note 1. Summary of Significant Accounting Policies

Nature of Operations: Independent Bank Group, Inc. (IBG) through its subsidiary, Independent Bank, a Texas state banking corporation (Bank) (collectively known as the Company), provides a full range of banking services to individual and corporate customers in the North, Central and Southeast, Texas areas and along the Colorado Front Range, through its various branch locations in those areas. The Company is engaged in traditional community banking activities, which include commercial and retail lending, deposit gathering, investment and liquidity management activities. The Company's primary deposit products are demand deposits, money market accounts and certificates of deposit, and its primary lending products are commercial business and real estate, real estate mortgage and consumer loans.

Basis of Presentation: The accompanying consolidated financial statements include the accounts of IBG, its wholly-owned subsidiaries, the Bank, IBG Adriatica Holdings, Inc. (Adriatica) and Carlile Capital, LLC and the Bank's wholly-owned subsidiaries, IBG Real Estate Holdings, Inc., IBG Real Estate Holdings II, Inc., IBG Aircraft Company III, Preston Grand, Inc., CFRH II, LLC, McKinney Avenue Holdings, Inc. and its wholly owned subsidiary, McKinney Avenue Holdings SPE 1, Inc. Adriatica, CFRH II, LLC, McKinney Avenue Holdings, Inc. and its subsidiary are currently not active entities. On June 1, 2018, the Company acquired Integrity Bancshares, Inc. (Integrity) and its wholly owned subsidiary, Integrity Bank, SSB, Houston, Texas. Integrity has been merged into the Company and dissolved and Integrity Bank has been merged with the Bank as of acquisition date. See Note 11, Business Combinations for more details of the Integrity acquisition.

All material intercompany transactions and balances have been eliminated in consolidation. In addition, the Company wholly-owns IB Trust I (Trust I), IB Trust II (Trust II), IB Trust III (Trust III), IB Centex Trust I (Centex Trust I), Community Group Statutory Trust I (CGI Trust I), Northstar Statutory Trust II (Northstar Trust II) and Northstar Statutory Trust III (Northstar Trust III). The Trusts were formed to issue trust preferred securities and do not meet the criteria for consolidation.

The consolidated interim financial statements are unaudited, but include all adjustments, which, in the opinion of management, are necessary for a fair presentation of the results of the periods presented. All such adjustments were of a normal and recurring nature. These financial statements should be read in conjunction with the financial statements and the notes thereto in the Company's Annual Report on Form 10-K for the year ended December 31, 2017. The consolidated balance sheet at December 31, 2017 has been derived from the audited financial statements as of that date, but does not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements.

Segment Reporting: The Company has one reportable segment. The Company's chief operating decision-maker uses consolidated results to make operating and strategic decisions.

Subsequent events: Companies are required to evaluate events and transactions that occur after the balance sheet date but before the date the financial statements are issued. They must recognize in the financial statements the effect of all events or transactions that provide additional evidence of conditions that existed at the balance sheet date, including the estimates inherent in the financial statement preparation process. Entities shall not recognize the impact of events or transactions that provide evidence about conditions that did not exist at the balance sheet date but arose after that date. The Company has evaluated subsequent events through the date of filing these financial statements with the Securities and Exchange Commission (SEC) and noted no subsequent events requiring financial statement recognition or disclosure, except as disclosed in Note 12.

Earnings per share: Basic earnings per common share are net income available to common shareholders divided by the weighted average number of common shares outstanding during the period. The unvested share-based payment awards that contain rights to non forfeitable dividends are considered participating securities for this calculation.

Diluted earnings per common share include the dilutive effect of additional potential common shares issuable under stock warrants. The participating nonvested common stock was not included in dilutive shares as it was anti-dilutive for the three and nine months ended September 30, 2018 and 2017. Proceeds from the assumed exercise of dilutive stock warrants are assumed to be used to repurchase common stock at the average market price.

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Independent Bank Group, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (unaudited)

(Dollars in thousands, except for share and per share information)

The following table presents a reconciliation of net income available to common shareholders and the number of shares used in the calculation of basic and diluted earnings per common share.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Basic earnings per share:				
Net income	\$35,696	\$ 23,514	\$94,295	\$ 57,319
Less:				
Undistributed earnings allocated to participating securities	262	181	729	555
Dividends paid on participating securities	36	24	104	83
Net income available to common shareholders	\$35,398	\$ 23,309	\$93,462	\$ 56,681
Weighted-average basic shares outstanding	30,219,567	27,555,978	29,035,724	24,585,473
Basic earnings per share	\$1.17	\$ 0.85	\$3.22	\$ 2.31
Diluted earnings per share:				
Net income available to common shareholders	\$35,398	\$ 23,309	\$93,462	\$ 56,681
Total weighted-average basic shares outstanding	30,219,567	27,555,978	29,035,724	24,585,473
Add dilutive stock warrants	90,114	103,800	91,292	105,317
Total weighted-average diluted shares outstanding	30,309,681	27,659,778	29,127,016	24,690,790
Diluted earnings per share	\$1.17	\$ 0.84	\$3.21	\$ 2.30
Anti-dilutive participating securities	62,588	77,498	112,797	145,925

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Independent Bank Group, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (unaudited)

(Dollars in thousands, except for share and per share information)

Note 2. Statement of Cash Flows

As allowed by the accounting standards, the Company has chosen to report on a net basis its cash receipts and cash payments for time deposits accepted and repayments of those deposits, and loans made to customers and principal collections on those loans. The Company uses the indirect method to present cash flows from operating activities.

Other supplemental cash flow information is presented below:

	Nine Months Ended September 30,	
	2018	2017

Cash transactions:

Interest expense paid	\$55,084	\$31,113
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Income taxes paid	\$17,159	\$21,911
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Noncash transactions:

Transfers of loans to other real estate owned	\$410	\$750
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Transfer of bank premises to other real estate	\$—	\$2,716
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Supplemental schedule of noncash investing activities from branch sales is as follows:

	Nine Months Ended September 30, 2017	
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Noncash assets transferred:

Loans, including accrued interest	\$—	\$5,439
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Total assets	\$—	\$5,439
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Noncash liabilities transferred:

Deposits, including accrued interest	\$—	\$17,509
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Other liabilities	—	28
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Total liabilities	\$—	\$17,537
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Cash and cash equivalents transferred in branch sale	\$—	\$101
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Deposit premium received	\$—	\$333
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Cash paid to buyer, net of deposit premium	\$—	\$11,664
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Independent Bank Group, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (unaudited)

(Dollars in thousands, except for share and per share information)

Supplemental schedule of noncash investing activities from acquisitions is as follows:

	Nine Months Ended September 30,	
	2018	2017
Noncash assets acquired		
Certificates of deposit held in other banks	\$—	\$11,025
Securities available for sale	24,721	336,540
Restricted stock	3,357	11,110
Loans	651,769	1,384,210
Premises and equipment	4,863	63,166
Other real estate owned	—	11,124
Goodwill	100,326	362,431
Core deposit intangibles	7,532	36,717
Bank owned life insurance	8,181	53,213
Other assets	6,393	25,197
Total assets	\$807,142	\$2,294,733
Noncash liabilities assumed:		
Deposits	\$593,078	\$1,825,181
Repurchase agreements	—	18,003
FHLB advances	60,000	—
Junior subordinated debt	—	9,359
Other liabilities	10,508	6,719
Total liabilities	\$663,586	\$1,859,262
Cash and cash equivalents acquired from acquisitions	\$44,723	\$148,444
Cash paid to shareholders of acquired banks	\$31,016	\$17,773
Fair value of common stock issued to shareholders of acquired bank	\$157,263	\$566,142

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Independent Bank Group, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (unaudited)

(Dollars in thousands, except for share and per share information)

Note 3. Securities Available for Sale

Securities available for sale have been classified in the consolidated balance sheets according to management's intent.

The amortized cost of securities and their approximate fair values at September 3