

Hilltop Holdings Inc.
Form 10-Q
April 25, 2019
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2019

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number: 1-31987

Hilltop Holdings Inc.

(Exact name of registrant as specified in its charter)

Maryland
(State or other jurisdiction of incorporation or
organization)

84-1477939
(I.R.S. Employer Identification No.)

2323 Victory Avenue, Suite 1400

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Dallas, TX

75219

(Address of principal executive offices)

(Zip Code)

(214) 855-2177

(Registrant's telephone number, including area code)

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 for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 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 the 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

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 provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

The number of shares of the registrant's common stock outstanding at April 25, 2019 was 93,983,247.

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HILLTOP HOLDINGS INC.

FORM 10-Q

FOR THE QUARTER ENDED MARCH 31, 2019

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HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share data)

(Unaudited)

	March 31, 2019	December 31, 2018
Assets		
Cash and due from banks	\$ 313,192	\$ 644,073
Federal funds sold	438	400
Assets segregated for regulatory purposes	156,851	133,993
Securities purchased under agreements to resell	65,205	61,611
Securities:		
Trading, at fair value	703,295	745,466
Available for sale, at fair value (amortized cost of \$1,021,221 and \$886,799, respectively)	1,019,851	875,658
Held to maturity, at amortized cost (fair value of \$365,781 and \$341,124, respectively)	369,865	351,012
Equity, at fair value	19,343	19,679
	2,112,354	1,991,815
Loans held for sale	1,059,280	1,393,246
Loans held for investment, net of unearned income	7,011,679	6,930,458
Allowance for loan losses	(58,809)	(59,486)
Loans held for investment, net	6,952,870	6,870,972
Broker-dealer and clearing organization receivables	1,651,199	1,440,287
Premises and equipment, net	210,333	237,373
Operating lease right-of-use assets	108,806	—
Other assets	591,442	580,362
Goodwill	291,435	291,435
Other intangible assets, net	35,965	38,005
Total assets	\$ 13,549,370	\$ 13,683,572
Liabilities and Stockholders' Equity		
Deposits:		
Noninterest-bearing	\$ 2,490,144	\$ 2,560,750
Interest-bearing	5,807,975	5,975,406
Total deposits	8,298,119	8,536,156
Broker-dealer and clearing organization payables	1,490,227	1,294,925

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Short-term borrowings	914,525	1,065,807
Securities sold, not yet purchased, at fair value	69,354	81,667
Notes payable	225,372	228,872
Operating lease liabilities	118,452	—
Junior subordinated debentures	67,012	67,012
Other liabilities	351,178	435,240
Total liabilities	11,534,239	11,709,679
Commitments and contingencies (see Notes 13 and 14)		
Stockholders' equity:		
Hilltop stockholders' equity:		
Common stock, \$0.01 par value, 125,000,000 shares authorized; 93,821,450 and 93,610,217 shares issued and outstanding at March 31, 2019 and December 31, 2018, respectively	938	936
Additional paid-in capital	1,491,585	1,489,816
Accumulated other comprehensive loss	(1,062)	(8,627)
Retained earnings	499,452	466,737
Deferred compensation employee stock trust, net	827	825
Employee stock trust (10,683 and 11,672 shares, at cost, at March 31, 2019 and December 31, 2018, respectively)	(213)	(217)
Total Hilltop stockholders' equity	1,991,527	1,949,470
Noncontrolling interests	23,604	24,423
Total stockholders' equity	2,015,131	1,973,893
Total liabilities and stockholders' equity	\$ 13,549,370	\$ 13,683,572

See accompanying notes.

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HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

(Unaudited)

	Three Months Ended March 31,	
	2019	2018
Interest income:		
Loans, including fees	\$ 110,870	\$ 99,944
Securities borrowed	16,859	16,300
Securities:		
Taxable	15,616	10,953
Tax-exempt	1,498	1,772
Other	5,197	4,391
Total interest income	150,040	133,360
Interest expense:		
Deposits	17,106	8,675
Securities loaned	14,738	13,739
Short-term borrowings	5,471	4,043
Notes payable	2,641	2,497
Junior subordinated debentures	1,001	822
Other	152	164
Total interest expense	41,109	29,940
Net interest income	108,931	103,420
Provision (recovery) for loan losses	951	(1,807)
Net interest income after provision (recovery) for loan losses	107,980	105,227
Noninterest income:		
Net gains from sale of loans and other mortgage production income	96,139	105,767
Mortgage loan origination fees	21,873	20,626
Securities commissions and fees	35,969	38,717
Investment and securities advisory fees and commissions	20,160	18,354
Net insurance premiums earned	33,203	34,315
Other	45,124	17,364
Total noninterest income	252,468	235,143
Noninterest expense:		
Employees' compensation and benefits	189,898	182,600
Occupancy and equipment, net	28,023	27,830
Professional services	22,942	24,704

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Loss and loss adjustment expenses	14,926	15,532
Other	53,296	57,536
Total noninterest expense	309,085	308,202
Income before income taxes	51,363	32,168
Income tax expense	11,586	7,488
Net income	39,777	24,680
Less: Net income attributable to noncontrolling interest	991	239
Income attributable to Hilltop	\$ 38,786	\$ 24,441
Earnings per common share:		
Basic	\$ 0.41	\$ 0.25
Diluted	\$ 0.41	\$ 0.25
Weighted average share information:		
Basic	93,669	95,985
Diluted	93,669	96,146

See accompanying notes.

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HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands)

(Unaudited)

	Three Months Ended March 31,	
	2019	2018
Net income	\$ 39,777	\$ 24,680
Other comprehensive income:		
Net unrealized gains (losses) on securities available for sale, net of tax of \$2,208 and \$(1,893), respectively	7,549	(6,703)
Reclassification adjustment for gains (losses) included in net income, net of tax of \$5 and \$0, respectively	16	—
Comprehensive income	47,342	17,977
Less: comprehensive income attributable to noncontrolling interest	991	239
Comprehensive income applicable to Hilltop	\$ 46,351	\$ 17,738

See accompanying notes.

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HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(in thousands)

(Unaudited)

		Additional	Accumulated		Deferred	Employee		Total	
Common Stock		Paid-in	Other	Comprehensive	Compensation	Stock Trust	Stock Trust	Hilltop	Noncontrolling
Shares	Amount	Capital	Loss	Retained Earnings	Employee Stock Trust, Net	Shares	Amount	Stockholders' Equity	Interest
95,982	\$ 960	\$ 1,526,369	\$ (394)	\$ 384,545	\$ 848	12	\$ (247)	\$ 1,912,081	\$ 2,726
—	—	—	—	24,441	—	—	—	24,441	239
—	—	—	(6,703)	—	—	—	—	(6,703)	—
—	—	2,164	—	—	—	—	—	2,164	—
5	—	124	—	—	—	—	—	124	—
129	1	(693)	—	—	—	—	—	(692)	—
(68)	(1)	(1,097)	—	(608)	—	—	—	(1,706)	—
—	—	—	—	(6,719)	—	—	—	(6,719)	—
—	—	—	—	—	9	(1)	(7)	2	—
—	—	—	(2,601)	2,601	—	—	—	—	—

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g	—	—	—	—	—	—	—	—	(501)	
rch	96,048	\$ 960	\$ 1,526,867	\$ (9,698)	\$ 404,260	\$ 857	11	\$ (254)	\$ 1,922,992	\$ 2,464
,	93,610	\$ 936	\$ 1,489,816	\$ (8,627)	\$ 466,737	\$ 825	11	\$ (217)	\$ 1,949,470	\$ 24,423
	—	—	—	—	38,786	—	—	—	38,786	991
ve	—	—	—	7,565	—	—	—	—	7,565	—
n	—	—	2,354	—	—	—	—	—	2,354	—
ck	8	—	140	—	—	—	—	—	140	—
rd										
k										
	203	2	(725)	—	—	—	—	—	(723)	—
k	—	—	—	—	(7,464)	—	—	—	(7,464)	—
n	—	—	—	—	—	2	—	4	6	—
ote	—	—	—	—	1,393	—	—	—	1,393	—
g	—	—	—	—	—	—	—	—	—	(1,810)
rch	93,821	\$ 938	\$ 1,491,585	\$ (1,062)	\$ 499,452	\$ 827	11	\$ (213)	\$ 1,991,527	\$ 23,604

See accompanying notes.

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HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(Unaudited)

	Three Months Ended March 31,	
	2019	2018
Operating Activities		
Net income	\$ 39,777	\$ 24,680
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision (recovery) for loan losses	951	(1,807)
Depreciation, amortization and accretion, net	(1,563)	1,577
Net change in fair value of equity securities	(1,256)	572
Deferred income taxes	527	(534)
Other, net	2,616	2,590
Net change in securities purchased under agreements to resell	(3,594)	(58,441)
Net change in trading securities	42,171	(25,466)
Net change in broker-dealer and clearing organization receivables	(124,407)	(164,957)
Net change in other assets	(8,824)	(2,949)
Net change in broker-dealer and clearing organization payables	119,673	217,443
Net change in other liabilities	(43,919)	(108,306)
Net change in securities sold, not yet purchased	(12,313)	22,730
Net gains from sales of loans	(96,139)	(105,767)
Loans originated for sale	(2,596,880)	(3,021,516)
Proceeds from loans sold	3,009,282	3,405,633
Net cash provided by operating activities	326,102	185,482
Investing Activities		
Proceeds from maturities and principal reductions of securities held to maturity	6,340	14,095
Proceeds from sales, maturities and principal reductions of securities available for sale	37,604	44,925
Proceeds from sales, maturities and principal reductions of equity securities	1,815	15
Purchases of securities held to maturity	(25,243)	(14,848)
Purchases of securities available for sale	(172,511)	(116,393)
Purchases of equity securities	(223)	(217)
Net change in loans held for investment	(159,202)	48,859
Purchases of premises and equipment and other assets	(8,454)	(4,271)
Proceeds from sales of premises and equipment and other real estate owned	5,892	4,487
Net cash received from Federal Home Loan Bank and Federal Reserve Bank stock	7,172	9,716

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Net cash used in investing activities	(306,810)	(13,632)
Financing Activities		
Net change in deposits	(162,408)	(19,231)
Net change in short-term borrowings	(151,282)	(142,099)
Proceeds from notes payable	134,639	69,808
Payments on notes payable	(138,160)	(75,799)
Payments to repurchase common stock	—	(1,706)
Dividends paid on common stock	(7,464)	(6,719)
Net cash distributed to noncontrolling interest	(1,810)	(501)
Taxes paid on employee stock awards netting activity	(723)	(689)
Other, net	(69)	(177)
Net cash used in financing activities	(327,277)	(177,113)
Net change in cash and cash equivalents	(307,985)	(5,263)
Cash, cash equivalents and restricted cash, beginning of period	778,466	673,960
Cash, cash equivalents and restricted cash, end of period	\$ 470,481	\$ 668,697
Reconciliation of Cash, Cash Equivalents and Restricted Cash to Consolidated Balance Sheets		
Cash and due from banks	\$ 313,192	\$ 470,127
Federal funds sold	438	400
Assets segregated for regulatory purposes	156,851	198,170
Total cash, cash equivalents and restricted cash	\$ 470,481	\$ 668,697
Supplemental Disclosures of Cash Flow Information		
Cash paid for interest	\$ 39,297	\$ 28,294
Cash paid for income taxes, net of refunds	\$ (270)	\$ 542
Supplemental Schedule of Non-Cash Activities		
Derecognition of construction in progress related to build-to-suit lease obligations	\$ 29,195	\$ —
Conversion of loans to other real estate owned	\$ 1,578	\$ 2,496
Additions to mortgage servicing rights	\$ 1,861	\$ 6,661

See accompanying notes.

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements

(Unaudited)

1. Summary of Significant Accounting and Reporting Policies

Nature of Operations

Hilltop Holdings Inc. (“Hilltop” and, collectively with its subsidiaries, the “Company”) is a financial holding company registered under the Bank Holding Company Act of 1956. The Company’s primary line of business is to provide business and consumer banking services from offices located throughout Texas through PlainsCapital Bank (the “Bank”). In addition, the Company provides an array of financial products and services through its broker-dealer, mortgage origination and insurance subsidiaries.

The Company, headquartered in Dallas, Texas, provides its products and services through three primary business units, PlainsCapital Corporation (“PCC”), Hilltop Securities Holdings LLC (“Securities Holdings”) and National Lloyds Corporation (“NLC”). PCC is a financial holding company that provides, through its subsidiaries, traditional banking, wealth and investment management and treasury management services primarily in Texas and residential mortgage lending throughout the United States. Securities Holdings is a holding company that provides, through its subsidiaries, investment banking and other related financial services, including municipal advisory, sales, trading and underwriting of taxable and tax-exempt fixed income securities, equity trading, clearing, securities lending, structured finance and retail brokerage services throughout the United States. NLC is a property and casualty insurance holding company that provides, through its subsidiaries, fire and homeowners insurance to low value dwellings and manufactured homes primarily in Texas and other areas of the southern United States.

Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States (“GAAP”), and in conformity with the rules and regulations of the Securities and Exchange Commission (the “SEC”). In the opinion of management, these financial statements contain all adjustments necessary for a fair statement of the results of the interim periods presented. Accordingly, the financial statements do not include all of the information and footnotes required by GAAP for complete financial statements and should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2018 (“2018 Form 10-K”). Results for interim periods are not necessarily indicative of results to be expected for a full year or any future period.

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, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Estimates regarding the allowance for loan losses, the fair values of financial instruments, reserves for losses and loss adjustment expenses (“LAE”), the mortgage loan indemnification liability, and the potential impairment of assets are particularly subject to change. The Company has applied its critical accounting policies and estimation methods consistently in all periods presented in these consolidated financial statements.

Hilltop owns 100% of the outstanding stock of PCC. PCC owns 100% of the outstanding stock of the Bank and 100% of the membership interest in Hilltop Opportunity Partners LLC, formerly known as PlainsCapital Equity, LLC, a merchant bank utilized to facilitate investments in companies engaged in non-financial activities. The Bank owns 100% of the outstanding stock of PrimeLending, a PlainsCapital Company (“PrimeLending”).

PrimeLending owns a 100% membership interest in PrimeLending Ventures Management, LLC (“Ventures Management”), which holds an ownership interest in and is the managing member of certain affiliated business arrangements (“ABAs”).

PCC also owns 100% of the outstanding common securities of PCC Statutory Trusts I, II, III and IV (the “Trusts”), which are not included in the consolidated financial statements under the requirements of the Variable Interest Entities

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

("VIE") Subsections of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") because the primary beneficiaries of the Trusts are not within the consolidated group.

Hilltop has a 100% membership interest in Securities Holdings, which operates through its wholly owned subsidiaries, Hilltop Securities Inc. ("Hilltop Securities"), Hilltop Securities Independent Network Inc. ("HTS Independent Network") (collectively, the "Hilltop Broker-Dealers") and Hilltop Securities Asset Management, LLC. Hilltop Securities is a broker-dealer registered with the SEC and Financial Industry Regulatory Authority ("FINRA") and a member of the New York Stock Exchange ("NYSE"), HTS Independent Network is an introducing broker-dealer that is also registered with the SEC and FINRA, and Hilltop Securities Asset Management, LLC is a registered investment adviser under the Investment Advisers Act of 1940.

Hilltop also owns 100% of NLC, which operates through its wholly owned subsidiaries, National Lloyds Insurance Company ("NLIC") and American Summit Insurance Company ("ASIC").

In addition, Hilltop owns 100% of the membership interest in each of HTH Hillcrest Project LLC ("HTH Project LLC") and Hilltop Investments I, LLC. Hilltop Investments I, LLC owns 50% of the membership interest in HTH Diamond Hillcrest Land LLC ("Hillcrest Land LLC") which is consolidated under the aforementioned VIE Subsections of the ASC. These entities are related to the Hilltop Plaza investment discussed in detail in Note 13 to the consolidated financial statements and are collectively referred to as the "Hilltop Plaza Entities."

The consolidated financial statements include the accounts of the above-named entities. Intercompany transactions and balances have been eliminated. Noncontrolling interests have been recorded for minority ownership in entities that are not wholly owned and are presented in compliance with the provisions of Noncontrolling Interest in Subsidiary Subsections of the ASC.

Certain reclassifications have been made to the prior period consolidated financial statements to conform with the current period presentation, including reclassifications due to the adoption of new accounting pronouncements. As previously disclosed in the Company's Form 10-Q for the period ended September 30, 2018, filed with the SEC on October 25, 2018, the quarterly report on Form 10-Q for the period ended March 31, 2018, filed with the SEC on April 26, 2018, incorrectly included the change in assets segregated for regulatory purposes in the operating section of the statements of cash flows. Previously disclosed net changes in assets segregated for regulatory purposes of (\$11.6) million for the three months ended March 31, 2018, should have been excluded from the cash flows from operating activities and the beginning-of-period and end-of-period balances of assets segregated for regulatory purposes are

included in total cash, cash equivalents and restricted cash in accordance with Accounting Standards Update (“ASU”) 2016-18. Accordingly, net cash provided by operating activities for the three months ended March 31, 2018, originally reported as \$173.9 million, is \$185.5 million. In preparing these consolidated financial statements, subsequent events were evaluated through the time the financial statements were issued. Financial statements are considered issued when they are widely distributed to all stockholders and other financial statement users, or filed with the SEC.

Significant accounting policies are detailed in Note 1 to the consolidated financial statements included in the Company’s 2018 Form 10-K. As a result of the adoption of ASU 2016-02 and related amendments and technical corrections (collectively, the “Leasing Standard”), the Company has included a new significant accounting policy related to lease accounting as summarized below.

Leases

The Company determines if an arrangement is a lease at inception. Operating leases with a term of greater than one year are included in operating lease right-of-use (“ROU”) assets and operating lease liabilities on the Company’s consolidated balance sheets. Finance leases are included in premises and equipment and other liabilities on the Company’s consolidated balance sheets. The Company has lease agreements with lease and nonlease components, which are generally accounted for as a single lease component. Leases of low-value assets are assessed on a lease-by-lease basis to determine the need for balance sheet capitalization.

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

ROU assets represent the Company's right to use an underlying asset for the lease term and lease liabilities represent its obligation to make lease payments arising from the lease. Operating lease ROU assets and liabilities are recognized on the lease commencement date based on the present value of lease payments over the lease term. As most of the Company's leases do not provide an implicit rate, the Company uses the incremental borrowing rate commensurate with the lease term based on the information available at the lease commencement date in determining the present value of lease payments. No significant judgments or assumptions were involved in developing the estimated operating lease liabilities as the Company's operating lease liabilities largely represent the future rental expenses associated with operating leases, and the incremental borrowing rates are based on publicly available interest rates. The operating lease ROU asset also includes any lease payments made and excludes lease incentives. The Company's lease terms may include options to extend or terminate the lease. These options to extend or terminate are assessed on a lease-by-lease basis, and the ROU assets and lease liabilities are adjusted when it is reasonably certain that an option will be exercised. Rental expense for lease payments is recognized on a straight-line basis over the lease term and is included in occupancy and equipment, net within our consolidated statements of operations.

2. Recently Issued Accounting Standards

Accounting Standards Adopted During 2019

In July 2018, the FASB issued ASU 2018-09 which clarifies, corrects and makes minor improvements to a wide variety of topics in the ASC. The amendments make the ASC easier to understand and apply by eliminating inconsistencies and providing clarifications. The transition and effective dates are based on the facts and circumstances of each amendment, with some amendments becoming effective upon issuance of the ASU, and others becoming effective for annual periods beginning after December 15, 2018. The Company adopted the amendments as of January 1, 2019, which did not have a material effect on the Company's consolidated financial statements.

In August 2017, the FASB issued ASU 2017-12 which provides targeted improvements to accounting for hedging activities. The purpose of the amendment is to better align a company's risk management activities with its financial reporting for hedging relationships, to simplify the hedge accounting requirements and to improve the disclosures of hedging arrangements. The amendment is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2018. The Company adopted the standard on January 1, 2019. The Company has not historically applied hedge accounting to its derivative transactions, so the provisions of the amendment did not

have a material effect on the Company's consolidated financial statements.

In February 2016, the FASB issued the Leasing Standard, which is codified in ASC 842, Leases, and is intended to increase transparency and comparability among organizations and require lessees to record an ROU asset and a liability representing the obligation to make lease payments for long-term leases. Accounting by lessors remains largely unchanged. The Company adopted the standard on January 1, 2019, using the modified retrospective transition under the option to apply the Leasing Standard at its effective date without adjusting the prior period comparative financial statements. The Company elected the package of practical expedients to not reassess: (i) whether any existing contracts are or contain a lease, (ii) the lease classification of any existing leases and (iii) initial direct costs related to existing leases. The Company also elected to apply an additional practical expedient to include both the lease and nonlease components of all leases as a single component and account for it as a lease. The Company implemented internal controls and key system functionality to enable the preparation of financial information upon adoption. The implementation of the Leasing Standard had a material impact on our consolidated balance sheets but did not have a material impact on our consolidated statements of operations. On January 1, 2019, the Company recorded operating lease liabilities of \$121.8 million and ROU assets of \$111.9 million upon adoption of the Leasing Standard. The lease liabilities (at their present value) represent predominantly all of the future minimum lease payments required under operating leases. The balance sheet effects of the new lease accounting standard also impacted regulatory capital ratios, performance ratios and other measures which are dependent upon asset or liability balances. In addition, the Company reassessed its accounting ownership of the Hilltop Plaza assets under construction as of January 1, 2019, under the build-to-suit provisions of ASC 842 and concluded it is not the accounting owner. As such, the assets and liabilities of the project were derecognized during the first quarter of 2019, with the \$1.4 million offset representing deferred expenses

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

recognized on the project to date through January 1, 2019, recorded as an increase to retained earnings. Refer to Note 13 for more details regarding the Hilltop Plaza transaction.

Accounting Standards Issued But Not Yet Adopted

In August 2018, the FASB issued ASU 2018-15 which aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software licenses). The accounting for the service element of a hosting arrangement that is a service contract is not affected by the amendments in this update. The amendment also includes presentation and disclosure provisions regarding capitalized implementation costs. The amendment is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2019. Early adoption is permitted. The Company is currently evaluating the provisions of the amendment and the impact on its future consolidated financial statements.

In August 2018, the FASB issued ASU 2018-13 which includes various removals, modifications and additions to existing guidance regarding fair value disclosures. The amendments are effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2019. Early adoption is permitted. The Company is currently evaluating the provisions of the amendments but does not expect the amendments to have a material impact on its future consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13 which sets forth a “current expected credit loss” (CECL) model which requires entities to measure all credit losses expected over the life of an exposure (or pool of exposures) for financial instruments held at the reporting date based on historical experience, current conditions and reasonable and supportable forecasts. The new standard, which is codified in ASC 326, Financial Instruments – Credit Losses, replaces the existing incurred loss model and is applicable to the measurement of credit losses on financial assets measured at amortized cost and applies to some off-balance sheet credit exposures. The new standard also requires enhanced disclosures to help financial statement users better understand significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an entity’s portfolio. The new standard is effective for annual periods, and interim reporting periods within those annual periods, beginning after December 15, 2019 with a cumulative-effect adjustment to retained earnings as of the beginning of the reporting period of adoption. The Company does not intend to adopt the provisions of the new standard early. The Company’s cross-functional team is continuing the implementation and testing of new credit forecasting models and a credit scoring system that will be utilized to estimate the likelihood of default and loss severity as a part of its credit loss estimation methodology in accordance with the new standard. In addition, the Company continues to identify and assess key interpretive policy issues, as well as design and build new or modified policies and procedures that will be used to calculate its credit loss

reserves. However, the magnitude of the change in allowance for loan losses and other credit losses upon adoption will depend on, among other things, the portfolio composition and quality at the adoption date, as well as economic conditions and forecasts at that time.

3. Acquisition

BORO Acquisition

On August 1, 2018, in an effort to expand its Houston-area banking operations, the Company acquired privately-held The Bank of River Oaks (“BORO”) in an all-cash transaction (the “BORO Acquisition”). Pursuant to the terms of the definitive agreement, the Company paid cash in the aggregate amount of \$85 million to the shareholders and option holders of BORO. The operations of BORO are included in the Bank’s operating results beginning August 1, 2018. BORO’s results of operations prior to the acquisition date are not included in the Company’s consolidated operating results.

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Notes to Consolidated Financial Statements (continued)

(Unaudited)

The BORO Acquisition was accounted for using the acquisition method of accounting, and accordingly, purchased assets, including identifiable intangible assets, and assumed liabilities were recorded at their respective acquisition date fair values. The resulting fair values of the identifiable assets acquired and liabilities assumed from BORO at August 1, 2018 are summarized in the following table (in thousands).

Cash and due from banks	\$ 21,756
Securities	60,477
Loans held for investment	326,618
Other assets	25,912
Total identifiable assets acquired	434,763
Deposits	376,393
Short-term borrowings	10,000
Other liabilities	2,996
Total liabilities assumed	389,389
Net identifiable assets acquired	45,374
Goodwill resulting from the acquisition	39,627
Net assets acquired	\$ 85,001

The goodwill of \$39.6 million resulting from the BORO Acquisition represents the inherent long-term value expected from the business opportunities created from combining BORO with the Company. The Company used significant estimates and assumptions to value the identifiable assets acquired and liabilities assumed. The amount of goodwill recorded in connection with the Company's acquisition of BORO is not deductible for tax purposes.

Included within the fair value of other assets in the table above are \$10.0 million of identifiable core deposits intangible assets recorded in connection with the BORO Acquisition which are being amortized on an accelerated basis over an estimated useful life of six years. The fair value of the core deposit intangible assets was estimated using the net cost savings method, a variation of the income approach. This involved the use of the following significant assumptions: cost of deposits, customer attrition rate, and discount rate.

In connection with the BORO Acquisition, the Company acquired loans both with and without evidence of credit quality deterioration since origination. The acquired loans were initially recorded at fair value with no carryover of any allowance for loan losses. Acquired loans were segregated between those considered to be purchased credit impaired ("PCI") loans and those without credit impairment at acquisition.

The following table presents details on acquired loans at the acquisition date (in thousands).

	Loans, excluding	PCI	Total Loans Held for
	PCI Loans	Loans	Investment
Commercial real estate	\$ 119,188	\$ 5,350	\$ 124,538
1 - 4 family residential	55,487	39	55,526
Construction and land development	37,134	—	37,134
Commercial and industrial	98,259	2,127	100,386
Consumer	9,021	13	9,034
Total	\$ 319,089	\$ 7,529	\$ 326,618

The following table presents information about the PCI loans at acquisition (in thousands).

Contractually required principal and interest payments	\$ 10,730
Nonaccretable difference	2,859
Cash flows expected to be collected	7,871
Accretable difference	342
Fair value of loans acquired with a deterioration of credit quality	\$ 7,529

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Notes to Consolidated Financial Statements (continued)

(Unaudited)

The following table presents information about the acquired loans without credit impairment at acquisition (in thousands).

Contractually required principal and interest payments	\$ 381,551
Contractual cash flows not expected to be collected	15,286
Fair value at acquisition	319,089

4. Fair Value Measurements

Fair Value Measurements and Disclosures

The Company determines fair values in compliance with The Fair Value Measurements and Disclosures Topic of the ASC (the “Fair Value Topic”). The Fair Value Topic defines fair value, establishes a framework for measuring fair value in GAAP and expands disclosures about fair value measurements. The Fair Value Topic defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. The Fair Value Topic assumes that transactions upon which fair value measurements are based occur in the principal market for the asset or liability being measured. Further, fair value measurements made under the Fair Value Topic exclude transaction costs and are not the result of forced transactions.

The Fair Value Topic includes a fair value hierarchy that classifies fair value measurements based upon the inputs used in valuing the assets or liabilities that are the subject of fair value measurements. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs, as indicated below.

- Level 1 Inputs: Unadjusted quoted prices in active markets for identical assets or liabilities that the Company can access at the measurement date.
- Level 2 Inputs: Observable inputs other than Level 1 prices. Level 2 inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, yield curves, prepayment speeds, default rates, credit risks and loss severities), and inputs that are derived from or corroborated by market data, among others.
- Level 3 Inputs: Unobservable inputs that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities. Level 3 inputs include pricing models and discounted cash flow techniques, among others.

Fair Value Option

The Company has elected to measure substantially all of PrimeLending's mortgage loans held for sale and retained mortgage servicing rights ("MSR") asset at fair value, under the provisions of the Fair Value Option. The Company elected to apply the provisions of the Fair Value Option to these items so that it would have the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. At March 31, 2019 and December 31, 2018, the aggregate fair value of PrimeLending's mortgage loans held for sale accounted for under the Fair Value Option was \$0.93 billion and \$1.26 billion, respectively, and the unpaid principal balance of those loans was \$0.90 billion and \$1.21 billion, respectively. The interest component of fair value is reported as interest income on loans in the accompanying consolidated statements of operations.

The Company holds a number of financial instruments that are measured at fair value on a recurring basis, either by the application of the Fair Value Option or other authoritative pronouncements. The fair values of those instruments are determined primarily using Level 2 inputs. Those inputs include quotes from mortgage loan investors and derivatives

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Notes to Consolidated Financial Statements (continued)

(Unaudited)

dealers and data from independent pricing services. The fair value of loans held for sale is determined using an exit price method.

The following tables present information regarding financial assets and liabilities measured at fair value on a recurring basis (in thousands).

	Level 1	Level 2	Level 3	Total
	Inputs	Inputs	Inputs	Fair Value
March 31, 2019				
Trading securities	\$ 2,122	\$ 701,173	\$ —	\$ 703,295
Available for sale securities	—	1,019,851	—	1,019,851
Equity securities	19,343	—	—	19,343
Loans held for sale	—	870,363	57,844	928,207
Derivative assets	—	53,176	—	53,176
MSR asset	—	—	62,049	62,049
Securities sold, not yet purchased	37,462	31,892	—	69,354
Derivative liabilities	—	29,726	—	29,726

	Level 1	Level 2	Level 3	Total
	Inputs	Inputs	Inputs	Fair Value
December 31, 2018				
Trading securities	\$ 7,947	\$ 737,519	\$ —	\$ 745,466
Available for sale securities	—	875,658	—	875,658
Equity securities	19,679	—	—	19,679
Loans held for sale	—	1,207,311	50,464	1,257,775
Derivative assets	—	35,010	—	35,010
MSR asset	—	—	66,102	66,102
Securities sold, not yet purchased	33,000	48,667	—	81,667
Derivative liabilities	—	26,355	—	26,355

The following tables include a rollforward for those financial instruments measured at fair value using Level 3 inputs (in thousands).

Total Gains or Losses

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					(Realized or Unrealized)		
	Balance at	Purchases/	Sales/	Transfers into	Included in	Included in Other	Balance at
	Beginning of	Additions	Reductions	Level 3	Net Income	Comprehensive	End of Period
	Period					Income (Loss)	
Three months ended March 31, 2019							
Loans held for sale	\$ 50,464	\$ 15,427	\$ (6,976)	1,037	\$ (2,108)	\$ —	\$ 57,844
MSR asset	66,102	1,861	—	—	(5,914)	—	62,049
Total	\$ 116,566	\$ 17,288	\$ (6,976)	\$ 1,037	\$ (8,022)	\$ —	\$ 119,893
Three months ended March 31, 2018							
Loans held for sale	\$ 36,972	\$ 12,479	\$ (3,975)	—	\$ (1,993)	\$ —	\$ 43,483
MSR asset	54,714	6,661	—	—	2,582	—	63,957
Total	\$ 91,686	\$ 19,140	\$ (3,975)	\$ —	\$ 589	\$ —	\$ 107,440

All net realized and unrealized gains (losses) in the tables above are reflected in the accompanying consolidated financial statements. The unrealized gains (losses) relate to financial instruments still held at March 31, 2019.

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(Unaudited)

For Level 3 financial instruments measured at fair value on a recurring basis at March 31, 2019 and December 31, 2018, the significant unobservable inputs used in the fair value measurements were as follows.

Financial instrument	Valuation Technique	Unobservable Inputs	Range (Weighted-Average)	
			March 31, 2019	December 31, 2018
Loans held for sale	Discounted cash flows /	Projected price	94 - 96 % (95 %)	95 - 97 % (95 %)
	Market comparable			
MSR asset	Discounted cash flows	Constant prepayment rate	11.72 %	9.62 %
		Discount rate	11.11 %	10.99 %

The fair value of certain loans held for sale that cannot be sold through normal sale channels or are non-performing is measured using Level 3 inputs. The fair value of such loans is generally based upon estimates of expected cash flows using unobservable inputs, including listing prices of comparable assets, uncorroborated expert opinions, and/or management's knowledge of underlying collateral.

The MSR asset, which is included in other assets within the Company's consolidated balance sheets, is reported at fair value using Level 3 inputs. The MSR asset is valued by projecting net servicing cash flows, which are then discounted to estimate the fair value. The fair value of the MSR asset is impacted by a variety of factors. Prepayment rates and discount rates, the most significant unobservable inputs, are discussed further in Note 7 to the consolidated financial statements.

The Company had no transfers between Levels 1 and 2 during the periods presented. Any transfers are based on changes in the observability and/or significance of the valuation inputs and are assumed to occur at the beginning of the quarterly reporting period in which they occur.

The following table presents those changes in fair value of instruments recognized in the consolidated statements of operations that are accounted for under the Fair Value Option (in thousands).

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	Three Months Ended March 31, 2019			Three Months Ended March 31, 2018		
	Net	Other	Total	Net	Other	Total
	Gains	Noninterest	Changes in		Noninterest	Changes in
	(Losses)	Income	Fair Value	Gains (Losses)	Income	Fair Value
Loans held for sale	\$ (13,324)	\$ —	\$ (13,324)	\$ (14,880)	\$ —	\$ (14,880)
MSR asset	(5,914)	—	(5,914)	2,582	—	2,582

The Company also determines the fair value of certain assets and liabilities on a non-recurring basis. In particular, the fair value of all assets acquired and liabilities assumed in an acquisition of a business are determined at their respective acquisition date fair values. In addition, facts and circumstances may dictate a fair value measurement when there is evidence of impairment. Assets and liabilities measured on a non-recurring basis include the items discussed below.

Impaired Loans — The Company reports individually impaired loans based on the underlying fair value of the collateral through specific allowances within the allowance for loan losses. PCI loans were acquired by the Company upon completion of the merger with PCC (the “PlainsCapital Merger”), the FDIC-assisted transaction whereby the Bank acquired certain assets and assumed certain liabilities of Edinburg, Texas-based First National Bank (“FNB”) on September 13, 2013 (the “FNB Transaction”), the acquisition of SWS Group, Inc. (“SWS”) in a stock and cash transaction (the “SWS Merger”), whereby SWS’s banking subsidiary, Southwest Securities, FSB, was merged into the Bank, and the BORO Acquisition (collectively, the “Bank Transactions”). The fair value of PCI loans was determined using Level 3 inputs, including estimates of expected cash flows that incorporated significant unobservable inputs regarding default rates, loss severity rates assuming default, prepayment speeds on acquired loans accounted for in pools (“Pooled Loans”), and estimated collateral values.

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Notes to Consolidated Financial Statements (continued)

(Unaudited)

Estimates for these significant unobservable inputs and the resulting weighted average expected loss on PCI loans were as follows.

	PCI Loans PlainsCapital Merger		FNB Transaction		SWS Merger		BORO Acquisition	
March 31, 2019								
Weighted average default rate	82	%	31	%	72	%	63	%
Weighted average loss severity rate	59	%	12	%	28	%	42	%
Weighted average prepayment speed	0	%	6	%	0	%	0	%
Resulting weighted average expected loss on PCI loans	48	%	4	%	20	%	26	%
	PCI Loans PlainsCapital Merger		FNB Transaction		SWS Merger		BORO Acquisition	
December 31, 2018								
Weighted average default rate	81	%	34	%	71	%	63	%
Weighted average loss severity rate	59	%	12	%	28	%	42	%
Weighted average prepayment speed	0	%	6	%	0	%	0	%
Resulting weighted average expected loss on PCI loans	48	%	4	%	20	%	26	%

The Company obtains updated appraisals of the fair value of collateral securing impaired collateral dependent loans at least annually, in accordance with regulatory guidelines. The Company also reviews the fair value of such collateral on a quarterly basis. If the quarterly review indicates that the fair value of the collateral may have deteriorated, the Company orders an updated appraisal of the fair value of the collateral. Because the Company obtains updated appraisals when evidence of a decline in the fair value of collateral exists, it typically does not adjust appraised values.

Other Real Estate Owned — The Company determines fair value primarily using independent appraisals of other real estate owned (“OREO”) properties. The resulting fair value measurements are classified as Level 2 inputs. At March 31, 2019 and December 31, 2018, the estimated fair value of OREO was \$23.1 million and \$27.6 million, respectively, and the underlying fair value measurements utilized Level 2 inputs. The amounts are included in other assets within the consolidated balance sheets. During the reported periods, all fair value measurements for OREO subsequent to initial recognition utilized Level 2 inputs.

The following table presents information regarding certain assets and liabilities measured at fair value on a non-recurring basis for which a change in fair value has been recorded during reporting periods subsequent to initial recognition (in thousands).

	Level 1	Level 2	Level 3	Total	Total Gains (Losses) for the	
	Inputs	Inputs	Inputs	Fair Value	Three Months Ended March 31,	2018
March 31, 2019					2019	
Impaired loans held for investment	\$ —	\$ —	\$ 70,963	\$ 70,963	\$ 100	\$ (123)
Other real estate owned	—	14,865	—	14,865	(494)	(1,106)

The Fair Value of Financial Instruments Subsection of the ASC requires disclosure of the fair value of financial assets and liabilities, including the financial assets and liabilities previously discussed. There have been changes to the methods for determining estimated fair value for financial assets and liabilities as described in detail in Note 3 to the consolidated financial statements included in the Company's 2018 Form 10-K.

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(Unaudited)

The following tables present the carrying values and estimated fair values of financial instruments not measured at fair value on either a recurring or non-recurring basis (in thousands).

	Carrying Amount	Estimated Fair Value			Total
		Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	
March 31, 2019					
Financial assets:					
Cash and cash equivalents	\$ 313,630	\$ 313,630	\$ —	\$ —	\$ 313,630
Assets segregated for regulatory purposes	156,851	156,851	—	—	156,851
Securities purchased under agreements to resell	65,205	—	65,205	—	65,205
Held to maturity securities	369,865	—	365,781	—	365,781
Loans held for sale	131,073	—	131,073	—	131,073
Loans held for investment, net	6,952,870	—	491,857	6,646,402	7,138,259
Broker-dealer and clearing organization receivables	1,651,199	—	1,651,199	—	1,651,199
Other assets	72,777	—	71,577	1,200	72,777
Financial liabilities:					
Deposits	8,298,119	—	8,295,435	—	8,295,435
Broker-dealer and clearing organization payables	1,490,227	—	1,490,227	—	1,490,227
Short-term borrowings	914,525	—	914,525	—	914,525
Debt	292,384	—	290,179	—	290,179
Other liabilities	5,518	—	5,518	—	5,518

	Carrying Amount	Estimated Fair Value			Total
		Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	
December 31, 2018					
Financial assets:					
Cash and cash equivalents	\$ 644,473	\$ 644,473	\$ —	\$ —	\$ 644,473
Assets segregated for regulatory purposes	133,993	133,993	—	—	133,993
Securities purchased under agreements to resell	61,611	—	61,611	—	61,611

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Held to maturity securities	351,012	—	341,124	—	341,124
Loans held for sale	135,471	—	135,471	—	135,471
Loans held for investment, net	6,870,972	—	578,363	6,445,810	7,024,173
Broker-dealer and clearing organization receivables	1,440,287	—	1,440,287	—	1,440,287
Other assets	69,720	—	68,573	1,147	69,720
Financial liabilities:					
Deposits	8,536,155	—	8,528,947	—	8,528,947
Broker-dealer and clearing organization payables	1,294,925	—	1,294,925	—	1,294,925
Short-term borrowings	1,065,807	—	1,065,807	—	1,065,807
Debt	295,884	—	293,685	—	293,685
Other liabilities	3,482	—	3,482	—	3,482

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(Unaudited)

The Company held equity investments other than securities of \$37.8 million and \$35.8 million at March 31, 2019 and December 31, 2018, respectively, which are included within other assets in the consolidated balance sheets. Of the \$37.8 million of such equity investments held at March 31, 2019, \$21.7 million do not have readily determinable fair values and each is measured at cost, less any impairment, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer. The following table presents the adjustments to the carrying value of these investments during the periods presented (in thousands).

	Three Months Ended March 31,	
	2019	2018
Balance, beginning of period	\$ 20,376	\$ 22,946
Additional investments	1,398	—
Upward adjustments	101	272
Impairments and downward adjustments	(197)	(1,312)
Dispositions	—	—
Balance, end of period	\$ 21,677	\$ 21,906

5. Securities

The fair value of trading securities is summarized as follows (in thousands).

	March 31,	December
	2019	31, 2018

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U.S. Treasury securities	\$ 2,121	\$ 7,945
U.S. government agencies:		
Bonds	1,485	1,494
Residential mortgage-backed securities	334,090	309,455
Commercial mortgage-backed securities	2,225	4,239
Collateralized mortgage obligations	119,178	206,813
Corporate debt securities	67,442	59,293
States and political subdivisions	134,572	126,748
Unit investment trusts	33,276	19,913
Private-label securitized product	5,520	5,680
Other	3,386	3,886
Totals	\$ 703,295	\$ 745,466

The Hilltop Broker-Dealers enter into transactions that represent commitments to purchase and deliver securities at prevailing future market prices to facilitate customer transactions and satisfy such commitments. Accordingly, the Hilltop Broker-Dealers' ultimate obligations may exceed the amount recognized in the financial statements. These securities, which are carried at fair value and reported as securities sold, not yet purchased in the consolidated balance sheets, had a value of \$69.4 million and \$81.7 million at March 31, 2019 and December 31, 2018, respectively.

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Notes to Consolidated Financial Statements (continued)

(Unaudited)

The amortized cost and fair value of available for sale and held to maturity securities are summarized as follows (in thousands).

March 31, 2019	Available for Sale			Fair Value
	Amortized Cost	Unrealized Gains	Unrealized Losses	
U.S. Treasury securities	\$ 10,554	\$ 89	\$ (26)	\$ 10,617
U.S. government agencies:				
Bonds	85,415	819	(223)	86,011
Residential mortgage-backed securities	472,203	2,589	(3,705)	471,087
Commercial mortgage-backed securities	11,648	334	(20)	11,962
Collateralized mortgage obligations	343,765	1,250	(4,250)	340,765
Corporate debt securities	49,196	925	(19)	50,102
States and political subdivisions	48,440	911	(44)	49,307
Totals	\$ 1,021,221	\$ 6,917	\$ (8,287)	\$ 1,019,851

December 31, 2018	Available for Sale			Fair Value
	Amortized Cost	Unrealized Gains	Unrealized Losses	
U.S. Treasury securities	\$ 11,552	\$ 30	\$ (44)	\$ 11,538
U.S. government agencies:				
Bonds	85,492	552	(433)	85,611
Residential mortgage-backed securities	391,428	608	(6,962)	385,074
Commercial mortgage-backed securities	11,703	189	(120)	11,772
Collateralized mortgage obligations	281,450	385	(5,436)	276,399
Corporate debt securities	53,614	268	(580)	53,302
States and political subdivisions	51,560	608	(206)	51,962
Totals	\$ 886,799	\$ 2,640	\$ (13,781)	\$ 875,658

March 31, 2019	Held to Maturity			Fair Value
	Amortized Cost	Unrealized Gains	Unrealized Losses	
U.S. Treasury securities	\$ 9,932	\$ 12	\$ —	\$ 9,944
U.S. government agencies:				
Bonds	39,018	—	(691)	38,327
Residential mortgage-backed securities	21,154	22	(26)	21,150

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Commercial mortgage-backed securities	112,056	1,187	(474)	112,769
Collateralized mortgage obligations	137,053	9	(3,488)	133,574
States and political subdivisions	50,652	264	(899)	50,017
Totals	\$ 369,865	\$ 1,494	\$ (5,578)	\$ 365,781

	Held to Maturity			Fair Value
	Amortized Cost	Unrealized Gains	Unrealized Losses	
December 31, 2018				
U.S. Treasury securities	\$ 9,903	\$ 3	\$ —	\$ 9,906
U.S. government agencies:				
Bonds	39,018	—	(1,479)	37,539
Residential mortgage-backed securities	21,903	—	(263)	21,640
Commercial mortgage-backed securities	87,065	271	(1,462)	85,874
Collateralized mortgage obligations	142,474	—	(5,000)	137,474
States and political subdivisions	50,649	91	(2,049)	48,691
Totals	\$ 351,012	\$ 365	\$ (10,253)	\$ 341,124

Additionally, the Company had unrealized net gains of \$0.5 million and unrealized net losses of \$0.9 million from equity securities with fair values of \$19.3 million and \$19.7 million held at March 31, 2019 and December 31, 2018,

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respectively. The Company recognized net gains of \$1.3 million and net losses of \$0.6 million, respectively, during the three months ended March 31, 2019 and 2018, respectively, due to changes in the fair value of equity securities still held at the balance sheet date. During the three months ended March 31, 2019 and 2018, net gains recognized from equity securities sold were nominal.

Information regarding available for sale, held to maturity and equity securities that were in an unrealized loss position is shown in the following tables (dollars in thousands).

	March 31, 2019			December 31, 2018		
	Number of Securities	Fair Value	Unrealized Losses	Number of Securities	Fair Value	Unrealized Losses
Available for Sale						
U.S. treasury securities:						
Unrealized loss for less than twelve months	1	\$ 986	\$ 3	1	\$ 981	\$ 6
Unrealized loss for twelve months or longer	2	2,572	23	3	3,556	39
	3	3,558	26	4	4,537	45
U.S. government agencies:						
Bonds:						
Unrealized loss for less than twelve months	—	—	—	3	24,772	5
Unrealized loss for twelve months or longer	3	30,678	223	3	30,472	428
	3	30,678	223	6	55,244	433
Residential mortgage-backed securities:						
Unrealized loss for less than twelve months	2	16,539	53	8	66,791	432
Unrealized loss for twelve months or longer	26	176,090	3,652	27	194,228	6,530
	28	192,629	3,705	35	261,019	6,962
Commercial mortgage-backed securities:						
Unrealized loss for less than twelve months	—	—	—	—	—	—
Unrealized loss for twelve months or longer	1	5,048	20	1	4,953	120

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	1	5,048	20	1	4,953	120
Collateralized mortgage obligations:						
Unrealized loss for less than twelve months	11	65,779	191	11	44,394	498
Unrealized loss for twelve months or longer	32	153,288	4,059	28	140,483	4,938
	43	219,067	4,250	39	184,877	5,436
Corporate debt securities:						
Unrealized loss for less than twelve months	—	—	—	8	16,256	282
Unrealized loss for twelve months or longer	2	3,961	19	8	15,665	297
	2	3,961	19	16	31,921	579
States and political subdivisions:						
Unrealized loss for less than twelve months	3	353	—	29	8,590	27
Unrealized loss for twelve months or longer	15	6,737	44	18	9,029	179
	18	7,090	44	47	17,619	206
Total available for sale:						
Unrealized loss for less than twelve months	17	83,657	247	60	161,784	1,250
Unrealized loss for twelve months or longer	81	378,374	8,040	88	398,386	12,531
	98	\$ 462,031	\$ 8,287	148	\$ 560,170	\$ 13,781

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

	March 31, 2019			December 31, 2018		
	Number of Securities	Fair Value	Unrealized Losses	Number of Securities	Fair Value	Unrealized Losses
Held to Maturity						
U.S. government agencies:						
Bonds:						
Unrealized loss for less than twelve months	—	\$ —	\$ —	—	\$ —	\$ —
Unrealized loss for twelve months or longer	4	38,327	691	4	37,539	1,479
	4	38,327	691	4	37,539	1,479
Residential mortgage-backed securities:						
Unrealized loss for less than twelve months	—	—	—	1	8,411	89
Unrealized loss for twelve months or longer	3	12,908	26	3	13,229	174
	3	12,908	26	4	21,640	263
Commercial mortgage-backed securities:						
Unrealized loss for less than twelve months	1	10,469	8	1	4,973	27
Unrealized loss for twelve months or longer	7	36,387	466	13	59,670	1,435
	8	46,856	474	14	64,643	1,462
Collateralized mortgage obligations:						
Unrealized loss for less than twelve months	—	—	—	1	2,051	26
Unrealized loss for twelve months or longer	22	128,077	3,488	24	135,423	4,974
	22	128,077	3,488	25	137,474	5,000
States and political subdivisions:						
Unrealized loss for less than twelve months	2	736	9	9	6,431	56
Unrealized loss for twelve months or longer	59	26,174	890	86	32,909	1,993

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	61	26,910	899	95	39,340	2,049
Total held to maturity:						
Unrealized loss for less than twelve months	3	11,205	17	12	21,866	198
Unrealized loss for twelve months or longer	95	241,873	5,561	130	278,770	10,055
	98	\$ 253,078	\$ 5,578	142	\$ 300,636	\$ 10,253
Equity						
Common and preferred stock:						
Unrealized loss for less than twelve months	—	—	—	—	—	—
Unrealized loss for twelve months or longer	—	—	—	—	—	—
	—	\$ —	\$ —	—	\$ —	\$ —

During the three months ended March 31, 2019 and 2018, the Company did not record any other-than-temporary impairment (“OTTI”). While some of the securities held in the Company’s investment portfolio have decreased in value since the date of acquisition, the severity of loss and the duration of the loss position are not significant enough to warrant OTTI of the securities. Factors considered in the Company’s analysis include the reasons for the unrealized loss position, the severity and duration of the unrealized loss position, credit worthiness, and forecasted performance of the investee. The Company does not intend to sell, nor does the Company believe that it is likely that the Company will be required to sell, these securities before the recovery of the cost basis.

Expected maturities may differ from contractual maturities because certain borrowers may have the right to call or prepay obligations with or without penalties. The amortized cost and fair value of securities, excluding trading and equity securities, at March 31, 2019 are shown by contractual maturity below (in thousands).

	Available for Sale Amortized		Held to Maturity Amortized	
	Cost	Fair Value	Cost	Fair Value
Due in one year or less	\$ 42,520	\$ 42,498	\$ 11,329	\$ 11,342
Due after one year through five years	90,202	91,604	25,730	25,347
Due after five years through ten years	40,668	41,050	4,902	4,875
Due after ten years	20,215	20,885	57,641	56,724
	193,605	196,037	99,602	98,288
Residential mortgage-backed securities	472,203	471,087	21,154	21,150
Collateralized mortgage obligations	343,765	340,765	137,053	133,574
Commercial mortgage-backed securities	11,648	11,962	112,056	112,769
	\$ 1,021,221	\$ 1,019,851	\$ 369,865	\$ 365,781

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

The Company recognized net gains of \$8.1 million and net losses of \$4.8 million from its trading portfolio during the three months ended March 31, 2019 and 2018, respectively. In addition, the Hilltop Broker-Dealers realized net gains from structured product trading activities of \$25.3 million and \$17.0 million during the three months ended March 31, 2019 and 2018, respectively. All such realized net gains and losses are recorded as a component of other noninterest income within the consolidated statements of operations.

Securities with a carrying amount of \$576.2 million and \$612.3 million (with a fair value of \$572.3 million and \$600.0 million, respectively) at March 31, 2019 and December 31, 2018, respectively, were pledged by the Bank to secure public and trust deposits, federal funds purchased and securities sold under agreements to repurchase, and for other purposes as required or permitted by law. Substantially all of these pledged securities were included in our available for sale and held to maturity securities portfolios at March 31, 2019 and December 31, 2018.

Mortgage-backed securities and collateralized mortgage obligations consist primarily of Government National Mortgage Association (“GNMA”), Federal National Mortgage Association (“FNMA”) and Federal Home Loan Mortgage Corporation (“FHLMC”) pass-through and participation certificates. GNMA securities are guaranteed by the full faith and credit of the United States, while FNMA and FHLMC securities are fully guaranteed by those respective United States government-sponsored agencies, and conditionally guaranteed by the full faith and credit of the United States.

At March 31, 2019 and December 31, 2018, NLC had investments on deposit in custody for various state insurance departments with aggregate carrying values of \$9.3 million and \$9.5 million, respectively.

6. Loans Held for Investment and Allowance for Loan Losses

The loans acquired in the FNB Transaction were subject to loss-share agreements with the FDIC. During the fourth quarter of 2018, the Bank and the FDIC entered into a Termination Agreement pursuant to which all rights and obligations of the Bank and the FDIC under the FDIC loss-share agreements were resolved and terminated. Accordingly, loans which were previously referred to as either “covered loans” if covered by the loss-share agreements or otherwise “non-covered loans” are now collectively referred to as “loans held for investment.” Disclosures associated with loans that were previously covered by the FDIC loss-share agreements during the three months ended March 31, 2018 are included in the “covered” portfolio segment in the applicable tables that follow. The majority of the loans previously covered by the FDIC loss-share agreements are comprised primarily of commercial real estate and 1-4

family residential loans. Loans held for investment summarized by portfolio segment are as follows (in thousands).

	March 31, 2019	December 31, 2018
Commercial real estate	\$ 2,939,855	\$ 2,940,120
Commercial and industrial	1,493,436	1,508,451
Construction and land development	995,698	932,909
1-4 family residential	696,209	679,263
Mortgage warehouse	350,896	243,806
Consumer	43,728	47,546
Broker-dealer (1)	491,857	578,363
	7,011,679	6,930,458
Allowance for loan losses	(58,809)	(59,486)
Total loans held for investment, net of allowance	\$ 6,952,870	\$ 6,870,972

(1) Primarily represents margin loans to customers and correspondents associated with broker-dealer segment operations.

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

In connection with the Bank Transactions, the Company acquired loans both with and without evidence of credit quality deterioration since origination. The following table presents the carrying values and the outstanding balances of PCI loans (in thousands).

	March 31, 2019	December 31, 2018
Carrying amount	\$ 90,571	\$ 93,072
Outstanding balance	164,753	172,808

Changes in the accretable yield for PCI loans were as follows (in thousands).

	Three Months Ended March 31,	
	2019	2018
Balance, beginning of period	\$ 80,693	\$ 98,846
Additions	—	—
Reclassifications from nonaccretable difference, net (1)	534	7,129
Disposals of loans	(366)	(289)
Accretion	(8,689)	(12,000)
Balance, end of period	\$ 72,172	\$ 93,686

- (1) Reclassifications from nonaccretable difference are primarily due to net increases in expected cash flows in the quarterly recasts. Reclassifications to nonaccretable difference occur when accruing loans are moved to non-accrual and expected cash flows are no longer predictable and the accretable yield is eliminated.

The remaining nonaccretable difference for PCI loans was \$63.8 million and \$64.2 million at March 31, 2019 and December 31, 2018, respectively.

Impaired loans exhibit a clear indication that the borrower's cash flow may not be sufficient to meet principal and interest payments, which generally occurs when a loan is 90 days past due unless the asset is both well secured and in the process of collection. Impaired loans include non-accrual loans, troubled debt restructurings ("TDRs"), PCI loans and partially charged-off loans.

The amounts shown in the following tables include loans accounted for on an individual basis, as well as acquired Pooled Loans. For Pooled Loans, the recorded investment and the related allowance consider impairment measured at the pool level. Impaired loans, segregated between those considered to be PCI loans and those without credit impairment at acquisition, are summarized by class in the following tables (in thousands).

March 31, 2019	Unpaid Contractual Principal Balance	Recorded Investment with No Allowance	Recorded Investment with Allowance	Total Recorded Investment	Related Allowance
PCI					
Commercial real estate:					
Non-owner occupied	\$ 36,025	\$ 5,452	\$ 7,596	\$ 13,048	\$ 1,251
Owner occupied	34,222	6,227	8,027	14,254	545
Commercial and industrial	27,636	4,918	1,287	6,205	54
Construction and land development	9,457	33	266	299	61
1-4 family residential	101,570	40,573	16,187	56,760	1,548
Mortgage warehouse	—	—	—	—	—
Consumer	1,937	5	—	5	—
Broker-dealer	—	—	—	—	—
	210,847	57,208	33,363	90,571	3,459
Non-PCI					
Commercial real estate:					
Non-owner occupied	206	199	—	199	—
Owner occupied	5,103	3,962	—	3,962	—
Commercial and industrial	22,788	9,932	327	10,259	73
Construction and land development	1,580	950	510	1,460	12
1-4 family residential	9,099	7,301	—	7,301	—
Mortgage warehouse	—	—	—	—	—
Consumer	146	38	—	38	—
Broker-dealer	—	—	—	—	—
	38,922	22,382	837	23,219	85
	\$ 249,769	\$ 79,590	\$ 34,200	\$ 113,790	\$ 3,544

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

December 31, 2018	Unpaid Contractual Principal Balance	Recorded Investment with No Allowance	Recorded Investment with Allowance	Total Recorded Investment	Related Allowance
PCI					
Commercial real estate:					
Non-owner occupied	\$ 42,668	\$ 5,549	\$ 7,540	\$ 13,089	\$ 1,125
Owner occupied	36,246	11,657	2,967	14,624	304
Commercial and industrial	27,403	5,491	1,068	6,559	72
Construction and land development	10,992	74	390	464	92
1-4 family residential	106,503	646	57,681	58,327	1,299
Mortgage warehouse	—	—	—	—	—
Consumer	2,185	9	—	9	—
Broker-dealer	—	—	—	—	—
	225,997	23,426	69,646	93,072	2,892
Non-PCI					
Commercial real estate:					
Non-owner occupied	—	—	—	—	—
Owner occupied	5,231	4,098	—	4,098	—
Commercial and industrial	22,277	9,891	1,740	11,631	721
Construction and land development	3,430	2,711	535	3,246	31
1-4 family residential	8,695	6,922	—	6,922	—
Mortgage warehouse	—	—	—	—	—
Consumer	149	42	—	42	—
Broker-dealer	—	—	—	—	—
	39,782	23,664	2,275	25,939	752
	\$ 265,779	\$ 47,090	\$ 71,921	\$ 119,011	\$ 3,644

Average recorded investment in impaired loans is summarized by class in the following table (in thousands).

	Three Months Ended March 31,	
	2019	2018
Commercial real estate:		
Non-owner occupied	\$ 13,168	\$ 13,734

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Owner occupied	18,469	22,033
Commercial and industrial	17,327	23,946
Construction and land development	2,735	1,954
1-4 family residential	64,655	4,904
Mortgage warehouse		
Consumer	47	121
Broker-dealer	—	—
Covered	—	89,203
	\$ 116,401	\$ 155,895

Non-accrual loans, excluding those classified as held for sale, are summarized by class in the following table (in thousands).

	March 31, 2019	December 31, 2018
Commercial real estate:		
Non-owner occupied	\$ 1,370	\$ 1,226
Owner occupied	3,962	4,098
Commercial and industrial	13,350	14,870
Construction and land development	1,473	3,278
1-4 family residential	7,395	7,026
Mortgage warehouse	—	—
Consumer	38	41
Broker-dealer	—	—
	\$ 27,588	\$ 30,539

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

At March 31, 2019 and December 31, 2018, non-accrual loans included PCI loans of \$4.6 million and \$4.9 million, respectively, for which discount accretion has been suspended because the extent and timing of cash flows from these PCI loans can no longer be reasonably estimated. In addition to the non-accrual loans in the table above, \$3.3 million and \$3.4 million of real estate loans secured by residential properties and classified as held for sale were in non-accrual status at March 31, 2019 and December 31, 2018, respectively.

Interest income, including recoveries and cash payments, recorded on impaired loans was \$0.4 million and \$0.2 million during the three months ended March 31, 2019 and 2018, respectively. Except as noted above, PCI loans are considered to be performing due to the application of the accretion method.

The Bank classifies loan modifications as TDRs when it concludes that it has both granted a concession to a debtor and that the debtor is experiencing financial difficulties. Loan modifications are typically structured to create affordable payments for the debtor and can be achieved in a variety of ways. The Bank modifies loans by reducing interest rates and/or lengthening loan amortization schedules. The Bank may also reconfigure a single loan into two or more loans (“A/B Note”). The typical A/B Note restructure results in a “bad” loan which is charged off and a “good” loan or loans, the terms of which comply with the Bank’s customary underwriting policies. The debt charged off on the “bad” loan is not forgiven to the debtor.

The Bank did not grant any TDRs during three months ended March 31, 2019 or 2018. At March 31, 2019 and December 31, 2018, the Bank had nominal unadvanced commitments to borrowers whose loans have been restructured in TDRs.

There were no TDRs granted during the twelve months preceding March 31, 2019. The following table presents information regarding TDRs granted during the twelve months preceding March 31, 2018, for which a payment was at least 30 days past due (dollars in thousands).

Twelve Months Preceding March 31, 2018		
Number of	Balance at	Balance at

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	Loans	Extension	End of Period
Commercial real estate:			
Non-owner occupied	—	\$ —	\$ —
Owner occupied	—	—	—
Commercial and industrial	—	—	—
Construction and land development	1	655	595
1-4 family residential	—	—	—
Mortgage warehouse	—	—	—
Consumer	—	—	—
Broker-dealer	—	—	—
	1	\$ 655	\$ 595

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

An analysis of the aging of the Company's loan portfolio is shown in the following tables (in thousands).

	Loans Past Due 30-59 Days	Loans Past Due 60-89 Days	Loans Past Due 90 Days or More	Total Past Due Loans	Current Loans	PCI Loans	Total Loans	Accruing (Non-PCI) Past Due 90 Days or More
March 31, 2019								
Commercial real estate:								
Non-owner occupied	\$ 979	\$ —	\$ 199	\$ 1,178	\$ 1,713,901	\$ 13,048	\$ 1,728,127	\$ —
Owner occupied	3,294	—	2,955	6,249	1,191,225	14,254	1,211,728	—
Commercial and industrial	4,894	4,752	9,107	18,753	1,468,478	6,205	1,493,436	3
Construction and land development	134	13	—	147	995,252	299	995,698	—
1-4 family residential	5,345	1,742	2,799	9,886	629,563	56,760	696,209	—
Mortgage warehouse	—	—	—	—	350,896	—	350,896	—
Consumer	123	460	—	583	43,140	5	43,728	—
Broker-dealer	—	—	—	—	491,857	—	491,857	—
	\$ 14,769	\$ 6,967	\$ 15,060	\$ 36,796	\$ 6,884,312	\$ 90,571	\$ 7,011,679	\$ 3
December 31, 2018								
Commercial real estate:								
Non-owner occupied	\$ 1,174	\$ 199	\$ —	\$ 1,373	\$ 1,708,160	\$ 13,089	\$ 1,722,622	\$ —
Owner occupied	1,364	—	4,173	5,537	1,197,337	14,624	1,217,498	75
	1,792	1,049	11,051	13,892	1,488,000	6,559	1,508,451	3

Commercial and industrial								
Construction and land development	3,549	—	—	3,549	928,896	464	932,909	—
1-4 family residential	5,987	2,484	1,950	10,421	610,515	58,327	679,263	—
Mortgage warehouse	—	—	—	0	243,806	—	243,806	—
Consumer	254	147	—	401	47,136	9	47,546	—
Broker-dealer	—	—	—	—	578,363	—	578,363	—
	\$ 14,120	\$ 3,879	\$ 17,174	\$ 35,173	\$ 6,802,213	\$ 93,072	\$ 6,930,458	\$ 78

In addition to the loans shown in the tables above, PrimeLending had \$77.0 million and \$83.1 million of loans included in loans held for sale (with an aggregate unpaid principal balance of \$78.1 million and \$84.0 million, respectively) that were 90 days past due and accruing interest at March 31, 2019 and December 31, 2018, respectively. These loans are guaranteed by U.S. government agencies and include loans that are subject to repurchase, or have been repurchased, by PrimeLending.

Management tracks credit quality trends on a quarterly basis related to: (i) past due levels, (ii) non-performing asset levels, (iii) classified loan levels, (iv) net charge-offs, and (v) general economic conditions in state and local markets.

The Company utilizes a risk grading matrix to assign a risk grade to each of the loans in its portfolio with the exception of broker-dealer margin loans. A risk rating is assigned based on an assessment of the borrower's management, collateral position, financial capacity, and economic factors. The general characteristics of the various risk grades are described below.

Pass – “Pass” loans present a range of acceptable risks to the Company. Loans that would be considered virtually risk-free are rated Pass – low risk. Loans that exhibit sound standards based on the grading factors above and present a reasonable risk to the Company are rated Pass – normal risk. Loans that exhibit a minor weakness in one or more of the grading criteria but still present an acceptable risk to the Company are rated Pass – high risk.

Special Mention – “Special Mention” loans have potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in a deterioration of the repayment prospects for the loans and weaken the Company's credit position at some future date. Special Mention loans are not adversely classified and do not expose the Company to sufficient risk to require adverse classification.

Substandard – “Substandard” loans are inadequately protected by the current sound worth and paying capacity of the obligor or the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Company will sustain

some loss if the deficiencies are not corrected. Many substandard loans are considered impaired.

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

PCI – “PCI” loans exhibited evidence of credit deterioration at acquisition that made it probable that all contractually required principal payments would not be collected.

The following tables present the internal risk grades of loans, as previously described, in the portfolio by class (in thousands).

March 31, 2019	Pass	Special Mention	Substandard	PCI	Total
Commercial real estate:					
Non-owner occupied	\$ 1,671,428	\$ 5,957	\$ 37,694	\$ 13,048	\$ 1,728,127
Owner occupied	1,168,015	—	29,459	14,254	1,211,728
Commercial and industrial	1,421,541	479	65,211	6,205	1,493,436
Construction and land development	993,927	—	1,472	299	995,698
1-4 family residential	620,547	382	18,520	56,760	696,209
Mortgage warehouse	350,896	—	—	—	350,896
Consumer	43,595	—	128	5	43,728
Broker-dealer	491,857	—	—	—	491,857
	\$ 6,761,806	\$ 6,818	\$ 152,484	\$ 90,571	\$ 7,011,679

December 31, 2018	Pass	Special Mention	Substandard	PCI	Total
Commercial real estate:					
Non-owner occupied	\$ 1,673,424	\$ —	\$ 36,109	\$ 13,089	\$ 1,722,622
Owner occupied	1,175,225	2,083	25,566	14,624	1,217,498
Commercial and industrial	1,433,227	15,320	53,345	6,559	1,508,451
Construction and land development	929,130	—	3,315	464	932,909
1-4 family residential	601,264	393	19,279	58,327	679,263
Mortgage warehouse	243,806	—	—	—	243,806
Consumer	47,416	—	121	9	47,546
Broker-dealer	578,363	—	—	—	578,363
	\$ 6,681,855	\$ 17,796	\$ 137,735	\$ 93,072	\$ 6,930,458

Allowance for Loan Losses

The allowance for loan losses is subject to regulatory examinations and determinations as to adequacy, which may take into account such factors as the methodology used to calculate the allowance and the size of the allowance. The Company's analysis of the level of the allowance for loan losses to ensure that it is appropriate for the estimated credit losses in the portfolio consistent with the Interagency Policy Statement on the Allowance for Loan and Lease Losses and the Receivables and Contingencies Topics of the ASC is described in detail in Note 5 to the consolidated financial statements included in the Company's 2018 Form 10-K.

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

Changes in the allowance for loan losses, distributed by portfolio segment, are shown below (in thousands).

	Balance, beginning of period	Provision (recovery) for loan losses	Loans charged off	Recoveries on charged off loans	Balance, end of period
Three Months Ended March 31, 2019					
Commercial real estate	\$ 27,100	\$ (255)	\$ —	\$ —	\$ 26,845
Commercial and industrial	21,980	458	(1,818)	648	21,268
Construction and land development	6,061	(153)	—	—	5,908
1-4 family residential	3,956	389	(28)	14	4,331
Mortgage warehouse	—	—	—	—	—
Consumer	267	586	(454)	10	409
Broker-dealer	122	(74)	—	—	48
Total	\$ 59,486	\$ 951	\$ (2,300)	\$ 672	\$ 58,809

	Balance, beginning of period	Provision (recovery) for loan losses	Loans charged off	Recoveries on charged off loans	Balance, end of period
Three Months Ended March 31, 2018					
Commercial real estate	\$ 26,413	\$ 780	\$ —	\$ —	\$ 27,193
Commercial and industrial	23,674	(1,696)	(1,183)	2,474	23,269
Construction and land development	7,844	(395)	—	—	7,449
1-4 family residential	2,362	(277)	(6)	28	2,107
Mortgage warehouse	—	—	—	—	—
Consumer	311	(34)	(13)	12	276
Broker-dealer	353	(276)	—	—	77
Covered	2,729	91	—	3	2,823
Total	\$ 63,686	\$ (1,807)	\$ (1,202)	\$ 2,517	\$ 63,194

The loan portfolio was distributed by portfolio segment and impairment methodology as shown below (in thousands).

Loans individually	Loans collectively evaluated for	PCI
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	evaluated for impairment	impairment	loans	Total
March 31, 2019				
Commercial real estate	\$ 3,581	\$ 2,908,972	\$ 27,302	\$ 2,939,855
Commercial and industrial	9,450	1,477,781	6,205	1,493,436
Construction and land development	1,358	994,041	299	995,698
1-4 family residential	608	638,841	56,760	696,209
Mortgage warehouse	—	350,896	—	350,896
Consumer	—	43,723	5	43,728
Broker-dealer	—	491,857	—	491,857
Total	\$ 14,997	\$ 6,906,111	\$ 90,571	\$ 7,011,679

	Loans individually evaluated for impairment	Loans collectively evaluated for impairment	PCI loans	Total
December 31, 2018				
Commercial real estate	\$ 3,909	\$ 2,908,498	\$ 27,713	\$ 2,940,120
Commercial and industrial	10,741	1,491,151	6,559	1,508,451
Construction and land development	3,241	929,204	464	932,909
1-4 family residential	—	620,936	58,327	679,263
Mortgage warehouse	—	243,806	—	243,806
Consumer	—	47,537	9	47,546
Broker-dealer	—	578,363	—	578,363
Total	\$ 17,891	\$ 6,819,495	\$ 93,072	\$ 6,930,458

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

The allowance for loan losses was distributed by portfolio segment and impairment methodology as shown below (in thousands).

	Loans individually evaluated for impairment	Loans collectively evaluated for impairment	PCI loans	Total
March 31, 2019				
Commercial real estate	\$ —	\$ 25,049	\$ 1,796	\$ 26,845
Commercial and industrial	73	21,141	54	21,268
Construction and land development	12	5,835	61	5,908
1-4 family residential	—	2,783	1,548	4,331
Mortgage warehouse	—	—	—	—
Consumer	—	409	—	409
Broker-dealer	—	48	—	48
Total	\$ 85	\$ 55,265	\$ 3,459	\$ 58,809

	Loans individually evaluated for impairment	Loans collectively evaluated for impairment	PCI loans	Total
December 31, 2018				
Commercial real estate	\$ —	\$ 25,671	\$ 1,429	\$ 27,100
Commercial and industrial	721	21,187	72	21,980
Construction and land development	31	5,938	92	6,061
1-4 family residential	—	2,657	1,299	3,956
Mortgage warehouse	—	—	—	—
Consumer	—	267	—	267
Broker-dealer	—	122	—	122
Total	\$ 752	\$ 55,842	\$ 2,892	\$ 59,486

7. Mortgage Servicing Rights

The following tables present the changes in fair value of the Company's MSR asset, as included in other assets within the consolidated balance sheets, and other information related to the serviced portfolio (dollars in thousands).

	Three Months Ended March 31,	
	2019	2018
Balance, beginning of period	\$ 66,102	\$ 54,714
Additions	1,861	6,661
Changes in fair value:		
Due to changes in model inputs or assumptions (1)	(5,033)	3,641
Due to customer payoffs	(881)	(1,059)
Balance, end of period	\$ 62,049	\$ 63,957

	March 31,		December 31,	
	2019		2018	
Mortgage loans serviced for others	\$ 5,077,800		\$ 5,086,461	
MSR asset as a percentage of serviced mortgage loans	1.22	%	1.30	%

(1) Primarily represents normal customer payments, changes in discount rates and prepayment speed assumptions, which are primarily affected by changes in interest rates and the refinement of other MSR model assumptions.

The key assumptions used in measuring the fair value of the Company's MSR asset were as follows.

	March 31,		December 31,	
	2019		2018	
Weighted average constant prepayment rate	11.72	%	10.51	%
Weighted average discount rate	11.11	%	11.11	%
Weighted average life (in years)	6.5		7.1	

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

A sensitivity analysis of the fair value of the Company's MSR asset to certain key assumptions is presented in the following table (in thousands).

	March 31, 2019	December 31, 2018
Constant prepayment rate:		
Impact of 10% adverse change	\$ (2,897)	\$ (2,512)
Impact of 20% adverse change	(5,664)	(4,980)
Discount rate:		
Impact of 10% adverse change	(2,434)	(2,677)
Impact of 20% adverse change	(4,677)	(5,139)

This sensitivity analysis presents the effect of hypothetical changes in key assumptions on the fair value of the MSR asset. The effect of such hypothetical change in assumptions generally cannot be extrapolated because the relationship of the change in one key assumption to the change in the fair value of the MSR asset is not linear. In addition, in the analysis, the impact of an adverse change in one key assumption is calculated independent of any impact on other assumptions. In reality, changes in one assumption may change another assumption.

Contractually specified servicing fees, late fees and ancillary fees earned of \$6.3 million and \$5.8 million during the three months ended March 31, 2019 and 2018, respectively, were included in net gains from sale of loans and other mortgage production income within the consolidated statements of operations.

8. Deposits

Deposits are summarized as follows (in thousands).

	March 31, 2019	December 31, 2018
Noninterest-bearing demand	\$ 2,490,144	\$ 2,560,750

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Interest-bearing:		
NOW accounts	1,388,860	1,358,196
Money market	2,502,889	2,725,541
Brokered - money market	5,000	5,000
Demand	330,968	393,685
Savings	185,015	184,700
Time	1,395,243	1,308,284
	\$ 8,298,119	\$ 8,536,156

9. Short-term Borrowings

Short-term borrowings are summarized as follows (in thousands).

	March 31, 2019	December 31, 2018
Federal funds purchased	\$ 132,800	\$ 100,100
Securities sold under agreements to repurchase	560,725	576,707
Federal Home Loan Bank	—	200,000
Short-term bank loans	221,000	189,000
	\$ 914,525	\$ 1,065,807

Federal funds purchased and securities sold under agreements to repurchase generally mature daily, on demand, or on some other short-term basis. The Bank and the Hilltop Broker-Dealers execute transactions to sell securities under agreements to repurchase with both customers and other broker-dealers. Securities involved in these transactions are held by the Bank, the Hilltop Broker-Dealers or a third-party dealer.

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

Information concerning federal funds purchased and securities sold under agreements to repurchase is shown in the following tables (dollars in thousands).

	Three Months Ended March 31,			
	2019		2018	
Average balance during the period	\$ 654,117		\$ 678,723	
Average interest rate during the period	2.63	%	1.50	%
	March 31, 2019		December 31, 2018	
Average interest rate at end of period	2.47	%	2.43	%
Securities underlying the agreements at end of period:				
Carrying value	\$ 562,897		\$ 587,609	
Estimated fair value	\$ 598,304		\$ 618,231	

Federal Home Loan Bank (“FHLB”) short-term borrowings mature over terms not exceeding 365 days and are collateralized by FHLB Dallas stock, nonspecified real estate loans and certain specific commercial real estate loans. Other information regarding FHLB short-term borrowings is shown in the following tables (dollars in thousands).

	Three Months Ended March 31,			
	2019		2018	
Average balance during the period	\$ 4,167		\$ 26,111	
Average interest rate during the period	2.65	%	2.03	%
	March 31, 2019		December 31, 2018	
Average interest rate at end of period	0.00	%	2.65	%

The Hilltop Broker-Dealers use short-term bank loans periodically to finance securities owned, margin loans to customers and correspondents, and underwriting activities. Interest on the borrowings varies with the federal funds rate. The weighted average interest rate on the borrowings at March 31, 2019 and December 31, 2018 was 3.29% and

3.35%, respectively.

10. Notes Payable

Notes payable consisted of the following (in thousands).

	March 31, 2019	December 31, 2018
Senior Notes due April 2025, net of discount of \$1,353 and \$1,393, respectively	\$ 148,647	\$ 148,607
FHLB notes, including premium of \$203 and \$222, respectively, with maturities ranging from September 2020 to June 2030	4,284	4,391
NLIC note payable due May 2033	10,000	10,000
NLIC note payable due September 2033	10,000	10,000
ASIC note payable due April 2034	7,500	7,500
Insurance company line of credit due December 31, 2019	—	—
Ventures Management lines of credit due May 2019	44,941	48,374
	\$ 225,372	\$ 228,872

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

11. Leases

Hilltop and its subsidiaries lease space, primarily for corporate offices, branch facilities and automated teller machines, under both operating and finance leases. Certain of the Company's leases have options to extend, with the longest extension option being ten years, and some of the Company's leases include options to terminate within one year. The Company's leases contain customary restrictions and covenants. The Company has certain intercompany leases and subleases between its subsidiaries, and these transactions and balances have been eliminated in consolidation and are not reflected in the tables and information presented below.

Supplemental balance sheet information related to finance leases is as follows (in thousands).

	March 31, 2019
Finance leases:	
Premises and equipment	\$ 7,780
Accumulated depreciation	(3,736)
Premises and equipment, net	\$ 4,044

Operating lease rental cost and finance lease amortization of ROU assets is included within occupancy and equipment, net in the consolidated statements of operations. Finance lease interest expense is included within other interest expense in the consolidated statements of operations. The Company does not generally enter into leases which contain variable payments, other than due to the passage of time. The components of lease costs, including short-term lease costs, are as follows (in thousands).

	Three Months Ended March 31, 2019
Operating lease cost	\$ 10,531
Less operating lease and sublease income	(388)
Net operating lease cost	\$ 10,143

Finance lease cost:	
Amortization of lease assets	\$ 147
Interest on lease liabilities	152
Total finance lease cost	\$ 299

Supplemental cash flow information related to leases is as follows (in thousands):

	Three Months Ended March 31, 2019
Cash paid for amounts included in the measurement of lease liabilities:	
Operating cash flows from operating leases	\$ 8,220
Operating cash flows from finance leases	152
Financing cash flows from finance leases	144
Right-of-use assets obtained in exchange for new lease obligations:	
Operating leases	\$ 3,591
Finance leases	—

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

Information regarding the lease terms and discount rates of the Company's leases is as follows.

	March 31, 2019	
	Weighted Average	Weighted Average
Lease Classification	Remaining Lease Term (Years)	Discount Rate
Operating	5	5.18 %
Finance	8	4.77 %

Future minimum lease payments under the Leasing Standard as of March 31, 2019, under lease agreements that had commenced as of January 1, 2019, are presented below (in thousands).

	Operating leases	Finance Leases
2019	\$ 27,512	\$ 891
2020	31,127	1,197
2021	23,287	1,212
2022	17,922	1,241
2023	13,902	1,280
Thereafter	20,278	3,460
Total minimum lease payments	\$ 134,028	\$ 9,281
Less amount representing interest	(15,576)	(1,374)
Lease liabilities	\$ 118,452	\$ 7,907

The Company adopted the Leasing Standard on January 1, 2019, using the modified retrospective transition under the option to apply the new standard at its effective date without adjusting the prior period comparative financial statements. As such, disclosures for comparative periods under the predecessor standard, ASC 840, Leases, are required in the year of transition. Future minimum lease payments under ASC 840 as of December 31, 2018, under lease agreements that had commenced as of December 31, 2018, are presented below (in thousands).

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	Operating Leases	Capital Leases
2019	\$ 36,171	\$ 1,186
2020	29,109	1,197
2021	21,058	1,212
2022	16,386	1,241
2023	12,361	1,280
Thereafter	18,264	3,460
Total minimum lease payments	\$ 133,349	9,576
Amount representing interest		(1,221)
Present value of minimum lease payments		\$ 8,355

As of March 31, 2019, the Company had additional operating leases that have not yet commenced with future minimum lease payments of approximately \$38 million, primarily related to the Hilltop Plaza leases, as discussed in more detail in Note 13. These operating leases are expected to commence between April 2019 and December 2019 with lease terms ranging from three to ten years.

A related party is the lessor in an operating lease with the Bank. The Bank's minimum payment under the lease is \$0.5 million annually through 2028, for an aggregate remaining obligation of \$4.6 million at March 31, 2019.

12. Income Taxes

The Company applies an estimated annual effective rate to interim period pre-tax income to calculate the income tax provision for the quarter in accordance with the principal method prescribed by the accounting guidance established for computing income taxes in interim periods. The Company's effective tax rates were 22.6% and 23.3% during the three months ended March 31, 2019 and 2018, respectively, and approximated the applicable statutory rates for such periods.

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

13. Commitments and Contingencies

Legal Matters

The Company is subject to loss contingencies related to litigation, claims, investigations and legal and administrative cases and proceedings arising in the ordinary course of business. The Company evaluates these contingencies based on information currently available, including advice of counsel. The Company establishes accruals for those matters when a loss contingency is considered probable and the related amount is reasonably estimable. Any accruals are periodically reviewed and may be adjusted as circumstances change. A portion of the Company's exposure with respect to loss contingencies may be offset by applicable insurance coverage. In determining the amounts of any accruals or estimates of possible loss contingencies, the Company does not take into account the availability of insurance coverage, other than that provided by reinsurers in the insurance segment. When it is practicable, the Company estimates loss contingencies for possible litigation and claims, whether or not there is an accrued probable loss. When the Company is able to estimate such probable losses, and when it estimates that it is reasonably possible it could incur losses in excess of amounts accrued, the Company is required to make a disclosure of the aggregate estimation. As available information changes, however, the matters for which the Company is able to estimate, as well as the estimates themselves, will be adjusted accordingly.

Assessments of litigation and claims exposures are difficult due to many factors that involve inherent unpredictability. Those factors include the following: the varying stages of the proceedings, particularly in the early stages; unspecified, unsupported, or uncertain damages; damages other than compensatory, such as punitive damages; a matter presenting meaningful legal uncertainties, including novel issues of law; multiple defendants and jurisdictions; whether discovery has begun or is complete; whether meaningful settlement discussions have commenced; and whether the claim involves a class action and if so, how the class is defined. As a result of some of these factors, the Company may be unable to estimate reasonably possible losses with respect to some or all of the pending and threatened litigation and claims asserted against the Company.

While the final outcome of litigation and claims exposures is inherently unpredictable, management is currently of the opinion that the outcome of pending and threatened litigation will not have a material effect on the Company's business, consolidated financial position, results of operations or cash flows as a whole. However, in the event of unexpected future developments, it is reasonably possible that an adverse outcome in any matter could be material to the Company's business, consolidated financial position, results of operations or cash flows for any particular reporting period of occurrence.

Indemnification Liability Reserve

The mortgage origination segment may be responsible to agencies, investors, or other parties for errors or omissions relating to its representations and warranties that each loan sold meets certain requirements, including representations as to underwriting standards and the validity of certain borrower representations in connection with the loan. If determined to be at fault, the mortgage origination segment either repurchases the affected loan from or indemnifies the claimant against loss. The mortgage origination segment has established an indemnification liability reserve for such probable losses.

Generally, the mortgage origination segment first becomes aware that an agency, investor, or other party believes a loss has been incurred on a sold loan when it receives a written request from the claimant to repurchase the loan or reimburse the claimant's losses. Upon completing its review of the claimant's request, the mortgage origination segment establishes a specific claims reserve for the loan if it concludes its obligation to the claimant is both probable and reasonably estimable.

An additional reserve has been established for probable agency, investor or other party losses that may have been incurred, but not yet reported to the mortgage origination segment based upon a reasonable estimate of such losses. Factors considered in the calculation of this reserve include, but are not limited to, the total volume of loans sold

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

exclusive of specific claimant requests, actual claim settlements and the severity of estimated losses resulting from future claims, and the mortgage origination segment's history of successfully curing defects identified in claim requests. While the mortgage origination segment's sales contracts typically include borrower early payment default repurchase provisions, these provisions have not been a primary driver of claims to date, and therefore, are not a primary factor considered in the calculation of this reserve.

At both March 31, 2019 and December 31, 2018, the mortgage origination segment's indemnification liability reserve totaled \$10.7 million. The provision for indemnification losses was \$0.5 million and \$0.7 million during the three months ended March 31, 2019 and 2018, respectively.

The following tables provide for a rollforward of claims activity for loans put-back to the mortgage origination segment based upon an alleged breach of a representation or warranty with respect to a loan sold and related indemnification liability reserve activity (in thousands).

	Representation and Warranty Specific Claims Activity - Origination Loan Balance Three Months Ended March 31,	
	2019	2018
Balance, beginning of period	\$ 33,784	\$ 33,702
Claims made	3,182	6,989
Claims resolved with no payment	(5,687)	(5,861)
Repurchases	(1,167)	(2,089)
Indemnification payments	—	(420)
Balance, end of period	\$ 30,112	\$ 32,321

	Indemnification Liability Reserve Activity (1) Three Months Ended March 31,	
	2019	2018
Balance, beginning of period	\$ 10,701	\$ 23,472
Additions for new sales	489	728
Repurchases	(82)	(160)
Early payment defaults	(142)	(146)
Indemnification payments	(3)	(117)
Change in reserves for loans sold in prior years	(242)	(445)
Balance, end of period	\$ 10,721	\$ 23,332

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	March 31, 2019	December 31, 2018
Reserve for Indemnification Liability:		
Specific claims	\$ 916	\$ 676
Incurred but not reported claims	9,805	10,025
Total	\$ 10,721	\$ 10,701

(1) The Reserve for Indemnification Liability as of March 31, 2018 reflected \$10.2 million of specific claims related to an inquiry by the U.S. Department of Housing and Urban Development (“HUD”) and the U.S. Department of Justice which was resolved in the fourth quarter of 2018. The resolution of this matter is discussed in detail in Note 18 to the consolidated financial statements included in the Company’s 2018 Form 10-K.

Although management considers the total indemnification liability reserve to be appropriate, there may be changes in the reserve over time to address incurred losses due to unanticipated adverse changes in the economy and historical loss patterns, discrete events adversely affecting specific borrowers or industries, and/or actions taken by institutions or investors. The impact of such matters is considered in the reserving process when probable and estimable.

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Notes to Consolidated Financial Statements (continued)

(Unaudited)

Hilltop Plaza Investment

On July 31, 2018, Hillcrest Land LLC purchased approximately 1.7 acres of land in the City of University Park, Texas for \$38.5 million. Hillcrest Land LLC is owned equally between Hilltop Investments I, LLC, a wholly owned entity of Hilltop, and Diamond Ground, LLC, an affiliate of Mr. Gerald J. Ford, Chairman of the Board of Directors. Each of Hilltop Investments I, LLC and Diamond Ground, LLC contributed \$19.3 million to Hillcrest Land LLC to complete the purchase. As the voting rights of Hillcrest Land LLC are shared equally between the Company and Diamond Ground, LLC, there is no primary beneficiary, and Diamond Ground, LLC's interest in Hillcrest Land LLC has been reflected as a noncontrolling interest in the Company's consolidated financial statements. Therefore, the Company has consolidated Hillcrest Land LLC under the VIE model according to the "most-closely associated" test. The purchased land is included within premises and equipment, net in the consolidated balance sheets. Any income (loss) associated with Hillcrest Land LLC is included within other noninterest income in the consolidated statements of operations. Trusts for which Jeremy Ford, President and Chief Executive Officer, and the wife of Corey Prestidge, Executive Vice President, General Counsel and Secretary, are a beneficiary own 10.2% and 10.1%, respectively, of Diamond Ground, LLC.

In connection with the purchase of the land, Hillcrest Land LLC entered into a 99-year ground lease of the land with three tenants-in-common: SPC Park Plaza Partners LLC ("Park Plaza LLC"), an unaffiliated entity which received an undivided 50% leasehold interest; HTH Project LLC, a wholly owned subsidiary of Hilltop, which received an undivided 25% leasehold interest; and Diamond Hillcrest, LLC ("Diamond Hillcrest"), an entity owned by Mr. Gerald J. Ford, which received an undivided 25% leasehold interest (collectively, the "Co-Owners"). The ground lease is triple net. The base rent from the Co-Owners under the ground lease commences 18 months after the ground lease was signed at \$1.8 million per year and increases 1.0% per year each January 1 thereafter. The ground lease was classified as an operating lease, and the accounting commencement date was determined to be July 31, 2018, the date the land was available to the Co-Owners.

Concurrent with the ground lease, the Co-Owners entered into an agreement to purchase the improvements currently being constructed on the land, which is a mixed-use project containing a six-story building ("Hilltop Plaza"). HTH Project LLC and Diamond Hillcrest each own an undivided 25% interest in Hilltop Plaza. Park Plaza LLC owns the remaining undivided 50% interest in Hilltop Plaza. Park Plaza LLC has agreed to serve as the Co-Owner property manager under the Co-Owners Agreement; however, certain actions require unanimous approval of all Co-Owners. Funding for Hilltop Plaza includes a \$41.0 million construction loan from an unaffiliated third party bank, as well as cash contributions of \$5.3 million from each of HTH Project LLC and Diamond Hillcrest. HTH Project LLC's undivided interest in Hilltop Plaza is accounted for as an equity method investment as the tenants-in-common have joint control over decisions regarding Hilltop Plaza. The investment is included within other assets in the consolidated balance sheets and any income (loss) is included within other noninterest income in the consolidated statements of operations.

Hilltop and the Bank entered into leases for an aggregate of approximately 72,000 of the total 119,000 square feet of rentable space in Hilltop Plaza to serve as the headquarters for both companies. The two separate 129-month office and retail leases have combined total base rent of approximately \$35 million with the first nine months of rent abated. Move-in is expected in the fourth quarter of 2019. The office and retail leases were considered under the build-to-suit provisions of ASC 840, and the Company was determined to be the accounting owner of the project as its affiliate, HTH Project LLC, has an equity investment in the project. As such, the assets of Hilltop Plaza were recognized during the construction period through December 31, 2018, as costs were incurred to construct the asset, with a corresponding liability representing the costs paid for by the lessor (the Co-Owners). At December 31, 2018, the \$27.8 million of costs incurred to date were included within premises and equipment and other liabilities, respectively, in the consolidated balance sheets. The Company reassessed its accounting ownership of the Hilltop Plaza assets under construction as of January 1, 2019, under the build-to-suit provisions of the newly adopted Leasing Standard and concluded it is not the accounting owner. As such, the assets and liabilities of the project were derecognized on January 1, 2019, with the \$1.4 million offset representing deferred expenses recognized on the project to date through December 31, 2018, recorded as an increase to retained earnings.

All intercompany transactions associated with the Hilltop Plaza investment and the related transactions discussed above are eliminated in consolidation.

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

14. Financial Instruments with Off-Balance Sheet Risk

The Bank is party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit that involve varying degrees of credit and interest rate risk in excess of the amount recognized in the consolidated financial statements. Such financial instruments are recorded in the consolidated financial statements when they are funded or related fees are incurred or received. The contract amounts of those instruments reflect the extent of involvement (and therefore the exposure to credit loss) the Bank has in particular classes of financial instruments.

Commitments to extend credit are agreements to lend to a customer provided that the terms established in the contract are met. Commitments generally have fixed expiration dates and may require payment of fees. Because some commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Standby letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. These letters of credit are primarily issued to support public and private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan commitments to customers.

In the aggregate, the Bank had outstanding unused commitments to extend credit of \$2.3 billion at March 31, 2019 and outstanding financial and performance standby letters of credit of \$95.1 million at March 31, 2019.

The Bank uses the same credit policies in making commitments and standby letters of credit as it does for on-balance sheet instruments. The amount of collateral obtained, if deemed necessary, in these transactions is based on management's credit evaluation of the borrower. Collateral held varies but may include real estate, accounts receivable, marketable securities, interest-bearing deposit accounts, inventory, and property, plant and equipment.

In the normal course of business, the Hilltop Broker-Dealers execute, settle, and finance various securities transactions that may expose the Hilltop Broker-Dealers to off-balance sheet risk in the event that a customer or counterparty does not fulfill its contractual obligations. Examples of such transactions include the sale of securities not yet purchased by customers or for the accounts of the Hilltop Broker-Dealers, use of derivatives to support certain non-profit housing organization clients and to hedge changes in the fair value of certain securities, clearing agreements between the

Hilltop Broker-Dealers and various clearinghouses and broker-dealers, secured financing arrangements that involve pledged securities, and when-issued underwriting and purchase commitments.

15. Stock-Based Compensation

Pursuant to the Hilltop Holdings Inc. 2012 Equity Incentive Plan (the “2012 Plan”), the Company may grant nonqualified stock options, stock appreciation rights, restricted stock, restricted stock units (“RSUs”), performance awards, dividend equivalent rights and other awards to employees of the Company, its subsidiaries and outside directors of the Company. In the aggregate, 4,000,000 shares of common stock may be delivered pursuant to awards granted under the 2012 Plan. At March 31, 2019, 666,839 shares of common stock remained available for issuance pursuant to awards granted under the 2012 Plan, excluding shares that may be delivered pursuant to outstanding awards. Compensation expense related to the 2012 Plan was \$2.5 million and \$2.3 million during the three months ended March 31, 2019 and 2018, respectively.

During the three months ended March 31, 2019 and 2018, Hilltop granted 7,958 and 4,921 shares of common stock, respectively, pursuant to the 2012 Plan to certain non-employee members of the Company’s board of directors for services rendered to the Company.

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Notes to Consolidated Financial Statements (continued)

(Unaudited)

Restricted Stock Units

The following table summarizes information about nonvested RSU activity for the three months ended March 31, 2019 (shares in thousands).

	RSUs	Weighted Average Grant Date Fair Value
	Outstanding	
Balance, December 31, 2018	1,270	\$ 22.44
Granted	574	\$ 19.20
Vested/Released	(240)	\$ 16.32
Forfeited	(2)	\$ 24.72
Balance, March 31, 2019	1,602	\$ 21.24

Vested/Released RSUs include an aggregate of 36,553 shares withheld to satisfy employee statutory tax obligations during the three months ended March 31, 2019. Pursuant to certain RSU award agreements, an aggregate of 3,322 vested RSUs at March 31, 2019 require deferral of the settlement in shares and statutory tax obligations to a future date.

During the three months ended March 31, 2019, the Compensation Committee of the board of directors of the Company awarded certain executives and key employees an aggregate of 565,861 RSUs pursuant to the 2012 Plan. Of the RSUs granted during the three months ended March 31, 2019, 474,612 that were outstanding at March 31, 2019, are subject to time-based vesting conditions and generally cliff vest on the third anniversary of the grant date. Of the RSUs granted during the three months ended March 31, 2019, 91,249 that were outstanding at March 31, 2019, will cliff vest based upon the achievement of certain performance goals over a three-year period.

At March 31, 2019, in the aggregate, 1,350,926 of the outstanding RSUs are subject to time-based vesting conditions and generally cliff vest on the third anniversary of the grant date, and 250,177 outstanding RSUs cliff vest based upon the achievement of certain performance goals over a three-year period. At March 31, 2019, unrecognized compensation expense related to outstanding RSUs of \$20.6 million is expected to be recognized over a weighted average period of 1.83 years.

16. Regulatory Matters

Banking and Hilltop

PlainsCapital, which includes the Bank and PrimeLending, and Hilltop are subject to various regulatory capital requirements administered by federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory — and possibly additional discretionary — actions by regulators that, if undertaken, could have a direct, material effect on the consolidated financial statements. The regulations require PlainsCapital and Hilltop to meet specific capital adequacy guidelines that involve quantitative measures of assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The Company performs reviews of the classification and calculation of risk-weighted assets to ensure accuracy and compliance with the Basel III regulatory capital requirements as implemented by the Board of Governors of the Federal Reserve System. The capital classifications are also subject to qualitative judgments by the regulators about components, risk weightings and other factors. Quantitative measures established by regulation to ensure capital adequacy require the companies to maintain minimum amounts and ratios (set forth in the following table) of Tier 1 capital (as defined in the regulations) to total average assets (as defined), and minimum ratios of common equity Tier 1, Tier 1 and total capital (as defined) to risk-weighted assets (as defined).

In order to avoid limitations on capital distributions, including dividend payments, stock repurchases and certain discretionary bonus payments to executive officers, Basel III requires banking organizations to maintain a capital conservation buffer above minimum risk-based capital requirements measured relative to risk-weighted assets. The phase-in of the capital conservation buffer requirements began on January 1, 2016 for Hilltop and PlainsCapital, and the requirements were fully phased in as of January 1, 2019.

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The following tables show PlainsCapital's and Hilltop's actual capital amounts and ratios in accordance with Basel III compared to the regulatory minimum capital requirements including conservation buffer in effect at the end of the period and on a fully phased-in basis as if such requirements were currently in effect at December 31, 2018 (dollars in thousands). Based on actual capital amounts and ratios shown in the following table, PlainsCapital's ratios place it in the "well capitalized" (as defined) capital category under regulatory requirements.

	Actual Amount	Ratio	Minimum Capital Requirements Including Conservation Buffer In Effect at End of Period Ratio					Fully Phased In Ratio	To Be Well Capitalized Ratio
March 31, 2019									
Tier 1 capital (to average assets):									
PlainsCapital	\$ 1,195,051	12.61 %	4.0	%	4.0	%	4.0	%	5.0
Hilltop	1,718,119	13.22 %	4.0	%	4.0	%	4.0	%	N/A
Common equity Tier 1 capital (to risk-weighted assets):									
PlainsCapital	1,195,051	13.89 %	7.0	%	7.0	%	7.0	%	6.5
Hilltop	1,671,530	16.75 %	7.0	%	7.0	%	7.0	%	N/A
Tier 1 capital (to risk-weighted assets):									
PlainsCapital	1,195,051	13.89 %	8.5	%	8.5	%	8.5	%	8.0
Hilltop	1,718,119	17.22 %	8.5	%	8.5	%	8.5	%	N/A
Total capital (to risk-weighted assets):									
PlainsCapital	1,256,067	14.60 %	10.5	%	10.5	%	10.5	%	10.0
Hilltop	1,760,772	17.64 %	10.5	%	10.5	%	10.5	%	N/A

	Actual Amount	Ratio	Minimum Capital Requirements Including Conservation Buffer In Effect at End of Period Ratio					Fully Phased In Ratio	To Be Well Capitalized Ratio
December 31, 2018									

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Tier 1 capital (to average assets):								
PlainsCapital	\$ 1,183,447	12.47	%	4.0	%	4.0	%	5.0
Hilltop	1,680,364	12.53	%	4.0	%	4.0	%	N/A
Common equity Tier 1 capital (to risk-weighted assets):								
PlainsCapital	1,183,447	13.90	%	6.375	%	7.0	%	6.5
Hilltop	1,634,978	16.58	%	6.375	%	7.0	%	N/A
Tier 1 capital (to risk-weighted assets):								
PlainsCapital	1,183,447	13.90	%	7.875	%	8.5	%	8.0
Hilltop	1,680,364	17.04	%	7.875	%	8.5	%	N/A
Total capital (to risk-weighted assets):								
PlainsCapital	1,245,177	14.63	%	9.875	%	10.5	%	10.0
Hilltop	1,722,602	17.47	%	9.875	%	10.5	%	N/A

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

Broker-Dealer

Pursuant to the net capital requirements of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), Hilltop Securities has elected to determine its net capital requirements using the alternative method. Accordingly, Hilltop Securities is required to maintain minimum net capital, as defined in Rule 15c3-1 promulgated under the Exchange Act, equal to the greater of \$250,000 and \$1,000,000, respectively, or 2% of aggregate debit balances, as defined in Rule 15c3-3 promulgated under the Exchange Act. Additionally, the net capital rule of the NYSE provides that equity capital may not be withdrawn or cash dividends paid if resulting net capital would be less than 5% of the aggregate debit items. HTS Independent Network follows the primary (aggregate indebtedness) method, as defined in Rule 15c3-1 promulgated under the Exchange Act, which requires the maintenance of the larger of minimum net capital of \$250,000 or 1/15 of aggregate indebtedness.

At March 31, 2019, the net capital position of each of the Hilltop Broker-Dealers was as follows (in thousands).

	Hilltop Securities	HTS Independent Network
Net capital	\$ 221,082	\$ 3,028
Less: required net capital	9,722	250
Excess net capital	\$ 211,360	\$ 2,778
Net capital as a percentage of aggregate debit items	45.5	%
Net capital in excess of 5% aggregate debit items	\$ 196,777	

Under certain conditions, Hilltop Securities may be required to segregate cash and securities in a special reserve account for the benefit of customers under Rule 15c3-3 promulgated under the Exchange Act. Assets segregated under the provisions of the Exchange Act are not available for general corporate purposes. At March 31, 2019 and December 31, 2018, the Hilltop Broker-Dealers held cash of \$156.9 million and \$134.0 million, respectively, segregated in special reserve bank accounts for the benefit of customers. The Hilltop Broker-Dealers were not required to segregate cash and securities in special reserve accounts for the benefit of proprietary accounts of introducing broker-dealers at March 31, 2019 or December 31, 2018.

Mortgage Origination

As a mortgage originator, PrimeLending and its subsidiaries are subject to minimum net worth and liquidity requirements established by HUD and GNMA, as applicable. On an annual basis, PrimeLending and its subsidiaries submit audited financial statements to HUD and GNMA, as applicable, documenting their respective compliance with minimum net worth and liquidity requirements. As of March 31, 2019, PrimeLending and its subsidiaries' net worth and liquidity exceeded the amounts required by both HUD and GNMA, as applicable.

Insurance

The statutory financial statements of the Company's insurance subsidiaries, which are domiciled in the State of Texas, are presented on the basis of accounting practices prescribed or permitted by the Texas Department of Insurance. Texas has adopted the statutory accounting practices of the National Association of Insurance Commissioners ("NAIC") as the basis of its statutory accounting practices with certain differences that are not significant to the insurance company subsidiaries' statutory equity.

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

A summary of statutory capital and surplus and statutory net income of each insurance subsidiary is as follows (in thousands).

	March 31, 2019	December 31, 2018
Statutory capital and surplus:		
National Lloyds Insurance Company	\$ 62,106	\$ 78,637
American Summit Insurance Company	18,641	17,908

	Three Months Ended March 31, 2019	2018
Statutory net income:		
National Lloyds Insurance Company	\$ 3,417	\$ 3,767
American Summit Insurance Company	417	889

Regulations of the Texas Department of Insurance require insurance companies to maintain minimum levels of statutory surplus to ensure their ability to meet their obligations to policyholders. At March 31, 2019, the Company's insurance subsidiaries had statutory surplus in excess of the minimum required.

The NAIC has adopted a risk based capital (“RBC”) formula for insurance companies that establishes minimum capital requirements indicating various levels of available regulatory action on an annual basis relating to insurance risk, asset credit risk, interest rate risk and business risk. The RBC formula is used by the NAIC and certain state insurance regulators as an early warning tool to identify companies that require additional scrutiny or regulatory action. At March 31, 2019, the Company's insurance subsidiaries' RBC ratio exceeded the level at which regulatory action would be required.

17. Stockholders' Equity

Dividends

During the three months ended March 31, 2019 and 2018, the Company declared and paid cash dividends of \$0.08 and \$0.07 per common share, or \$7.5 million and \$6.7 million, respectively.

On April 25, 2019, the Company announced that its board of directors declared a quarterly cash dividend of \$0.08 per common share, payable on May 31, 2019, to all common stockholders of record as of the close of business on May 15, 2019.

Stock Repurchase Program

In January 2019, the Hilltop board of directors authorized a new stock repurchase program through January 2020, pursuant to which the Company is authorized to repurchase, in the aggregate, up to \$50.0 million of its outstanding common stock, inclusive of repurchases to offset dilution related to grants of stock-based compensation. The Company's stock repurchase program and related accounting policy are discussed in detail in Note 1 and Note 22 to the consolidated financial statements included in the Company's 2018 Form 10-K.

18. Derivative Financial Instruments

The Company uses various derivative financial instruments to mitigate interest rate risk. The Bank's interest rate risk management strategy involves effectively managing the re-pricing characteristics of certain assets and liabilities to mitigate potential adverse impacts from changes in interest rates on the Bank's net interest margin. PrimeLending has interest rate risk relative to interest rate lock commitments ("IRLCs") and its inventory of mortgage loans held for sale. PrimeLending is exposed to such interest rate risk from the time an IRLC is made to an applicant to the time the related mortgage loan is sold. To mitigate interest rate risk, PrimeLending executes forward commitments to sell mortgage-backed securities ("MBSs") and Eurodollar futures. Additionally, PrimeLending has interest rate risk relative to its MSR asset and uses derivative instruments, including interest rate swaps and U.S. Treasury bond futures and options to hedge this risk. The Hilltop Broker-Dealers use forward commitments to both purchase and sell MBSs to facilitate customer transactions and as a means to hedge related exposure to interest rate risk in certain inventory positions. Additionally,

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

Hilltop Securities uses both U.S. Treasury bond and Eurodollar futures to hedge changes in the fair value of their securities.

Non-Hedging Derivative Instruments and the Fair Value Option

As discussed in Note 4 to the consolidated financial statements, the Company has elected to measure substantially all mortgage loans held for sale at fair value under the provisions of the Fair Value Option. The election provides the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without applying complex hedge accounting provisions. The fair values of PrimeLending's IRLCs and forward commitments are recorded in other assets or other liabilities, as appropriate, and changes in the fair values of these derivative instruments are recorded as a component of net gains from sale of loans and other mortgage production income. The fair value of PrimeLending's derivative instruments increased \$18.2 million and \$10.0 million during the three months ended March 31, 2019 and 2018, respectively. These changes in fair value are attributable to changes in the volume of IRLCs, mortgage loans held for sale, commitments to purchase and sell MBSs and MSR assets, and changes in market interest rates. Changes in market interest rates also conversely affect the value of PrimeLending's mortgage loans held for sale and its MSR asset, which are measured at fair value under the Fair Value Option. The effect of the change in market interest rates on PrimeLending's loans held for sale and MSR asset is discussed in Note 4 to the consolidated financial statements. The fair values of the Hilltop Broker-Dealers' and the Bank's derivative instruments are recorded in other assets or other liabilities, as appropriate. The fair values of the Hilltop Broker-Dealers' derivative instruments decreased \$1.8 million and \$5.2 million during the three months ended March 31, 2019 and 2018, respectively, while the fair values of the Bank's derivative instruments decreased \$0.1 million and increased \$0.1 million during the three months ended March 31, 2019 and 2018, respectively.

Derivative positions are presented in the following table (in thousands).

	March 31, 2019		December 31, 2018	
	Notional Amount	Estimated Fair Value	Notional Amount	Estimated Fair Value
Derivative instruments:				
IRLCs	\$ 1,165,947	\$ 29,860	\$ 677,267	\$ 17,421
Customer-based written options	31,200	(9)	31,200	(49)
Customer-based purchased options	31,200	9	31,200	49
Commitments to purchase MBSs	2,506,084	11,677	2,359,630	10,467
Commitments to sell MBSs	4,040,254	(18,108)	3,711,477	(19,315)

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Interest rate swaps	7,735	21	15,104	82
U.S. Treasury bond futures and options (1)	373,900	—	367,200	—
Eurodollar futures (1)	912,000	—	104,000	—

(1) Changes in the fair value of these contracts are settled daily with the respective counterparties of PrimeLending and the Hilltop Broker-Dealers.

PrimeLending had cash collateral advances totaling \$13.1 million and \$11.9 million to offset net liability derivative positions on its commitments to sell MBSs at March 31, 2019 and December 31, 2018, respectively. In addition, PrimeLending and the Hilltop Broker-Dealers advanced cash collateral totaling \$3.5 million and \$3.4 million on U.S. Treasury bond futures and options and Eurodollar futures at March 31, 2019 and December 31, 2018, respectively. These amounts are included in other assets within the consolidated balance sheets.

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

19. Balance Sheet Offsetting

Certain financial instruments, including resale and repurchase agreements, securities lending arrangements and derivatives, may be eligible for offset in the consolidated balance sheets and/or subject to master netting arrangements or similar agreements. The following tables present the assets and liabilities subject to enforceable master netting arrangements, repurchase agreements, or similar agreements with offsetting rights (in thousands).

	Gross Amounts of Recognized Assets	Gross Amounts Offset in the Balance Sheet	Net Amounts of Assets Presented in the Balance Sheet	Gross Amounts Not Offset in the Balance Sheet Financial Instruments	Cash Collateral Net Pledged	Amount
March 31, 2019						
Securities borrowed:						
Institutional counterparties	\$ 1,540,803	\$ —	\$ 1,540,803	\$ (1,491,092)	\$ —	\$ 49,711
Interest rate options:						
Customer counterparties	9	—	9	—	—	9
Interest rate swaps:						
Institutional counterparties	43	—	43	—	—	43
Reverse repurchase agreements:						
Institutional counterparties	65,205	—	65,205	(64,818)	—	387
Forward MBS derivatives:						
Institutional counterparties	11,684	—	11,684	(11,684)	—	—
	\$ 1,617,744	\$ —	\$ 1,617,744	\$ (1,567,594)	\$ —	\$ 50,150
December 31, 2018						
Securities borrowed:						
	\$ 1,365,547	\$ —	\$ 1,365,547	\$ (1,307,121)	\$ —	\$ 58,426

Institutional
counterparties

Interest rate options:

Customer counterparties	49	—	49	—	—	49
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Interest rate swaps:

Institutional counterparties	88	—	88	—	—	88
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Reverse repurchase
agreements:

Institutional counterparties	61,611	—	61,611	(61,390)	—	221
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Forward MBS
derivatives:

Institutional counterparties	10,469	—	10,469	(10,469)	—	—
	\$ 1,437,764	\$ —	\$ 1,437,764	\$ (1,378,980)	\$ —	\$ 58,784

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

	Gross Amounts of Recognized Liabilities	Gross Amountsof Liabilities Offset in the Balance Sheet	Net Amounts Presented in the Balance Sheet	Gross Amounts Not Offset in the Balance Sheet Financial Instruments	Cash Collateral Net Pledged	Amount
March 31, 2019						
Securities loaned:						
Institutional counterparties	\$ 1,408,636	\$ —	\$ 1,408,636	\$ (1,366,198)	\$ —	\$ 42,438
Interest rate options:						
Institutional counterparties	9	—	9	—	—	9
Interest rate swaps:						
Institutional counterparties	22	—	22	—	—	22
Repurchase agreements:						
Institutional counterparties	504,537	—	504,537	(504,537)	—	—
Customer counterparties	56,188	—	56,188	(56,188)	—	—
Forward MBS derivatives:						
Institutional counterparties	18,615	(501)	18,114	(12,275)	—	5,839
	\$ 1,988,007	\$ (501)	\$ 1,987,506	\$ (1,939,198)	\$ —	\$ 48,308
December 31, 2018						
Securities loaned:						
Institutional counterparties	\$ 1,186,073	\$ —	\$ 1,186,073	\$ (1,136,033)	\$ —	\$ 50,040
Interest rate options:						
Institutional counterparties	49	—	49	—	—	49

Interest rate swaps:

Institutional counterparties	6	—	6	—	—	6
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Repurchase

agreements:

Institutional counterparties	533,441	—	533,441	(533,441)	—	—
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Customer

counterparties	43,266	—	43,266	(43,266)	—	—
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Forward MBS

derivatives:

Institutional counterparties	19,331	(15)	19,316	(7,728)	—	11,588
	\$ 1,782,166	\$ (15)	\$ 1,782,151	\$ (1,720,468)	\$ —	\$ 61,683

Secured Borrowing Arrangements

Secured Borrowings (Repurchase Agreements) — The Company participates in transactions involving securities sold under repurchase agreements, which are secured borrowings and generally mature one to thirty days from the transaction date or involve arrangements with no definite termination date. Securities sold under repurchase agreements are reflected at the amount of cash received in connection with the transactions. The Company may be required to provide additional collateral based on the fair value of the underlying securities, which is monitored on a daily basis.

Securities Lending Activities — The Company's securities lending activities include lending securities for other broker-dealers, lending institutions and its own clearing and retail operations. These activities involve lending securities to other broker-dealers to cover short sales, to complete transactions in which there has been a failure to deliver securities by the required settlement date and as a conduit for financing activities.

When lending securities, the Company receives cash or similar collateral and generally pays interest (based on the amount of cash deposited) to the other party to the transaction. Securities lending transactions are executed pursuant to written agreements with counterparties that generally require securities loaned to be marked-to-market on a daily basis. The Company receives collateral in the form of cash in an amount generally in excess of the fair value of securities loaned. The Company monitors the fair value of securities loaned on a daily basis, with additional collateral obtained or refunded, as necessary. Collateral adjustments are made on a daily basis through the facilities of various clearinghouses. The Company is a principal in these securities lending transactions and is liable for losses in the event of a failure of any other party to honor its contractual obligation. Management sets credit limits with each counterparty and reviews these limits regularly to monitor the risk level with each counterparty. The Company is subject to credit risk through its securities lending activities if securities prices decline rapidly because the value of the Company's collateral could fall below the amount of the indebtedness it secures. In rapidly appreciating markets, credit risk increases due to short positions. The Company's securities lending business subjects the Company to credit risk if a counterparty fails to

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

perform or if collateral securing its obligations is insufficient. In securities transactions, the Company is subject to credit risk during the period between the execution of a trade and the settlement by the customer.

The following tables present the remaining contractual maturities of repurchase agreement and securities lending transactions accounted for as secured borrowings (in thousands). The Company had no repurchase-to-maturity transactions outstanding at both March 31, 2019 and December 31, 2018.

	Remaining Contractual Maturities				Total
	Overnight and Continuous	Up to 30 Days	30-90 Days	Greater Than 90 Days	
March 31, 2019					
Repurchase agreement transactions:					
U.S. Treasury and agency securities	\$ 85,345	\$ —	\$ —	\$ —	\$ 85,345
Asset-backed securities	475,380	—	—	—	475,380
Securities lending transactions:					
Corporate securities	630	—	—	—	630
Equity securities	1,408,006	—	—	—	1,408,006
Total	\$ 1,969,361	\$ —	\$ —	\$ —	\$ 1,969,361

Gross amount of recognized liabilities for repurchase agreement and securities lending transactions in offsetting disclosure above	\$ 1,969,361
Amount related to agreements not included in offsetting disclosure above	\$ —

	Remaining Contractual Maturities				Total
	Overnight and Continuous	Up to 30 Days	30-90 Days	Greater Than 90 Days	
December 31, 2018					
Repurchase agreement transactions:					
U.S. Treasury and agency securities	\$ 131,848	\$ —	\$ —	\$ —	\$ 131,848
Asset-backed securities	444,859	—	—	—	444,859
Securities lending transactions:					

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Corporate securities	113	—	—	—	113
Equity securities	1,185,960	—	—	—	1,185,960
Total	\$ 1,762,780	\$ —	\$ —	\$ —	\$ 1,762,780

Gross amount of recognized liabilities for repurchase agreement and securities lending transactions in offsetting disclosure above	\$ 1,762,780
Amount related to agreements not included in offsetting disclosure above	\$ —

20. Broker-Dealer and Clearing Organization Receivables and Payables

Broker-dealer and clearing organization receivables and payables consisted of the following (in thousands).

	March 31, 2019	December 31, 2018
Receivables:		
Securities borrowed	\$ 1,540,803	\$ 1,365,547
Securities failed to deliver	19,855	16,300
Trades in process of settlement	72,850	32,993
Other	17,691	25,447
	\$ 1,651,199	\$ 1,440,287
Payables:		
Securities loaned	\$ 1,408,636	\$ 1,186,073
Correspondents	36,818	29,311
Securities failed to receive	39,313	75,015
Other	5,460	4,526
	\$ 1,490,227	\$ 1,294,925

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

21. Reserve for Losses and Loss Adjustment Expenses

A summary of NLC's reserve for unpaid losses and LAE, as included in other liabilities within the consolidated balance sheets, is as follows (in thousands).

	March 31, 2019	December 31, 2018
Reserve for unpaid losses and allocated LAE balance, net	\$ 17,318	\$ 16,498
Reinsurance recoverables on unpaid losses	2,506	3,214
Unallocated LAE	767	840
Reserve for unpaid losses and LAE balance, gross	\$ 20,591	\$ 20,552

A summary of claims loss reserve development activity is presented in the following table (dollars in thousands).

Accident Year	Three Months Ended March 31, 2019		March 31, 2019 Total of IBNR Reserves Plus Expected Development on Reported Claims	Cumulative Number of Reported Claims
	Paid	Incurred		
2015	\$ 86,607	\$ 86,963	\$ 169	20,583
2016	83,265	84,085	401	20,180
2017	86,553	87,771	776	20,737
2018	68,015	76,110	4,542	15,288
2019	6,570	13,316	2,257	3,545
Total	331,010	\$ 348,245		
	83		All outstanding reserves prior to 2015, net of reinsurance	
	\$ 17,318			

Reserve for unpaid losses and allocated
LAE, net of reinsurance

22. Reinsurance Activity

NLC limits the maximum net loss that can arise from large risks or risks in concentrated areas of exposure by reinsuring (ceding) certain levels of risk. Substantial amounts of business are ceded, and these reinsurance contracts do not relieve NLC from its obligations to policyholders. Such reinsurance includes quota share, excess of loss, catastrophe, and other forms of reinsurance on essentially all property and casualty lines of insurance. Net insurance premiums earned, losses and LAE and policy acquisition and other underwriting expenses are reported net of the amounts related to reinsurance ceded to other companies. Amounts recoverable from reinsurers related to the portions of the liability for losses and LAE and unearned insurance premiums ceded to them are reported as assets. Failure of reinsurers to honor their obligations could result in losses to NLC; consequently, allowances are established for amounts deemed uncollectible as NLC evaluates the financial condition of its reinsurers and monitors concentrations of credit risk arising from similar geographic regions, activities, or economic characteristics of the reinsurers to minimize its exposure to significant losses from reinsurer insolvencies. At March 31, 2019, total reinsurance recoverables and receivables had a carrying value of \$3.9 million, which is included in other assets within the consolidated balance sheets. There was no allowance for uncollectible accounts at March 31, 2019, based on NLC's quality requirements.

The effects of reinsurance on premiums written and earned are summarized as follows (in thousands).

	Three Months Ended March 31,			
	2019		2018	
	Written	Earned	Written	Earned
Premiums from direct business	\$ 30,790	\$ 31,737	\$ 33,085	\$ 33,368
Reinsurance assumed	3,129	3,191	3,042	3,000
Reinsurance ceded	(1,725)	(1,725)	(2,010)	(2,053)
Net premiums	\$ 32,194	\$ 33,203	\$ 34,117	\$ 34,315

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

The effects of reinsurance on incurred losses and LAE are as follows (in thousands).

	Three Months Ended March 31,	
	2019	2018
Losses and LAE incurred	\$ 14,985	\$ 13,452
Reinsurance recoverables	(59)	2,080
Net loss and LAE incurred	\$ 14,926	\$ 15,532

Catastrophic coverage

At March 31, 2019, NLC had catastrophic excess of loss reinsurance coverage of losses per event in excess of \$8 million retention by NLIC and \$1.5 million retention by ASIC. ASIC maintained an underlying layer of coverage, providing \$6.0 million of reinsurance coverage in excess of its \$2.0 million retention to bridge to the primary program. The reinsurance for NLIC and ASIC in excess of \$8 million is comprised of three layers of protection: \$17 million in excess of \$8 million retention and/or loss; \$30 million in excess of \$25 million loss; and \$50 million in excess of \$55 million loss. NLIC and ASIC retain no participation in any of the layers, beyond the first \$8 million and \$1.5 million, respectively. At March 31, 2019, total retention for any one catastrophe that affects both NLIC and ASIC was limited to \$8 million in the aggregate.

Effective January 1, 2019, NLC renewed its underlying excess of loss contract that provides \$10.0 million aggregate coverage in excess of NLC's per event retention of \$1.0 million and aggregate retention of \$15.0 million for sub-catastrophic events. As of January 1, 2019, NLC retains 37.5% participation in this coverage, up from 17.5% participation during 2018.

23. Segment and Related Information

The Company currently has four reportable business segments that are organized primarily by the core products offered to the segments' respective customers. These segments reflect the manner in which operations are managed and

the criteria used by the chief operating decision maker, the Company's President and Chief Executive Officer, to evaluate segment performance, develop strategy and allocate resources.

The banking segment includes the operations of the Bank, and since August 1, 2018, the operations acquired in the BORO Acquisition. The broker-dealer segment includes the operations of Securities Holdings, the mortgage origination segment is composed of PrimeLending and the insurance segment is composed of NLC.

Corporate includes certain activities not allocated to specific business segments. These activities include holding company financing and investing activities, merchant banking investment opportunities and management and administrative services to support the overall operations of the Company.

Balance sheet amounts not discussed previously and the elimination of intercompany transactions are included in "All Other and Eliminations." The following tables present certain information about reportable business segment revenues, operating results, goodwill and assets (in thousands).

Three Months Ended March 31, 2019	Mortgage					All Other and Hilltop	
	Banking	Broker-Dealer	Origination	Insurance	Corporate	Eliminations	Consolidated
Net interest income (expense)	\$ 92,690	\$ 12,850	\$ (467)	\$ 642	\$ (1,330)	\$ 4,546	\$ 108,931
Provision (recovery) for loan losses	1,025	(74)	—	—	—	—	951
Noninterest income	10,621	91,307	118,033	36,492	538	(4,523)	252,468
Noninterest expense	60,726	87,807	114,677	30,338	15,562	(25)	309,085
Income (loss) before income taxes	\$ 41,560	\$ 16,424	\$ 2,889	\$ 6,796	\$ (16,354)	\$ 48	\$ 51,363

Three Months	Mortgage					All Other and Hilltop	
	Banking	Broker-Dealer	Origination	Insurance	Corporate	Eliminations	Consolidated

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Ended March 31, 2018							
Net interest income							
(expense)	\$ 86,638	\$ 12,550	\$ 941	\$ 787	\$ (2,091)	\$ 4,595	\$ 103,420
Provision for loan losses	(1,531)	(276)	—	—	—	—	(1,807)
Noninterest income	10,180	68,547	127,102	35,018	(712)	(4,992)	235,143
Noninterest expense	59,370	77,776	130,704	31,013	9,403	(64)	308,202
Income (loss) before income taxes	\$ 38,979	\$ 3,597	\$ (2,661)	\$ 4,792	\$ (12,206)	\$ (333)	\$ 32,168

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Hilltop Holdings Inc. and Subsidiaries

Notes to Consolidated Financial Statements (continued)

(Unaudited)

	Banking	Broker-Dealer	Mortgage Origination	Insurance	Corporate	All Other and Eliminations	Hilltop Consolidated
March 31, 2019							
Goodwill	\$ 247,368	\$ 7,008	\$ 13,071	\$ 23,988	\$ —	\$ —	\$ 291,435
Total assets	\$ 9,748,950	\$ 3,333,574	\$ 1,348,924	\$ 252,857	\$ 2,275,342	\$ (3,410,277)	\$ 13,549,3
December 31, 2018							
Goodwill	\$ 247,368	\$ 7,008	\$ 13,071	\$ 23,988	\$ —	\$ —	\$ 291,435
Total assets	\$ 10,004,971	\$ 3,213,115	\$ 1,627,134	\$ 253,513	\$ 2,243,182	\$ (3,658,343)	\$ 13,683,5

24. Earnings per Common Share

Net earnings, less any preferred dividends accumulated for the period (whether or not declared), is allocated between the common stock and participating securities pursuant to the two-class method, if applicable. Basic earnings per common share is computed by dividing net earnings available to common stockholders by the weighted average number of common shares outstanding during the period, excluding participating nonvested restricted shares. The Company calculated basic earnings per common share using the treasury method instead of the two-class method since there were no instruments which qualified as participating securities during the three months ended March 31, 2019 or 2018.

Diluted earnings per common share is computed in a similar manner, except that first the denominator is increased to include the number of additional common shares that would have been outstanding if potentially dilutive common shares, excluding the participating securities, were issued using the treasury stock method. During the three months ended March 31, 2019 and 2018, RSUs were the only potentially dilutive non-participating instruments issued by Hilltop. Next, the Company determines and includes in the diluted earnings per common share calculation the more dilutive effect of the participating securities using the treasury stock method or the two-class method. Undistributed losses are not allocated to the nonvested share-based payment awards (the participating securities) under the two-class method as the holders are not contractually obligated to share in the losses of the Company.

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

	Three Months Ended March 31,	
	2019	2018
Basic earnings per share:		
Net earnings available to Hilltop common stockholders	\$ 38,786	\$ 24,441
Weighted average shares outstanding - basic	93,669	95,985
Basic earnings per common share	\$ 0.41	\$ 0.25
Diluted earnings per share:		
Income attributable to Hilltop	\$ 38,786	\$ 24,441
Weighted average shares outstanding - basic	93,669	95,985
Effect of potentially dilutive securities	—	161
Weighted average shares outstanding - diluted	93,669	96,146
Diluted earnings per common share	\$ 0.41	\$ 0.25

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SCHEDULE I – Insurance Incurred and Cumulative Paid Losses and Allocated Loss Adjustment Expenses,

Net of Reinsurance

(dollars in thousands)

Incurred Losses and Allocated Loss Adjustment Expenses, Net of Reinsurance						March 31, 2019	
						Total of Incurred But Not Reported Reserves Plus Development On	Cumulative Number of Reported Claims
Accident Year	March 31, 2019 2015	2016	2017	2018	2019	Reported Claims	Reported Claims
2015	\$ 89,646	\$ 88,477	\$ 87,262	\$ 86,961	\$ 86,963	\$ 169	20,583
2016		84,771	85,189	84,076	84,085	401	20,180
2017			87,899	88,025	87,771	776	20,737
2018				75,217	76,110	4,542	15,288
2019					13,316	2,257	3,545
					\$ 348,245		

Cumulative Paid Losses and Allocated Loss Adjustment Expenses, Net of Reinsurance							
Accident Year	March 31, 2019 2015	2016	2017	2018	2019		
2015	\$ 71,820	\$ 82,940	\$ 85,507	\$ 86,549	\$ 86,607		
2016		71,543	81,682	83,169	83,265		
2017			77,675	86,319	86,553		
2018				61,922	68,015		
2019					6,570		
Total					\$ 331,010		
All outstanding reserves prior to 2015, net of reinsurance					83		
Reserve for unpaid losses and allocated loss adjustment expenses, net of reinsurance					\$ 17,318		

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion should be read in conjunction with the consolidated historical financial statements and notes appearing elsewhere in this Quarterly Report on Form 10-Q (this "Quarterly Report") and the financial information set forth in the tables herein.

Unless the context otherwise indicates, all references in this Management's Discussion and Analysis of Financial Condition and Results of Operations, or MD&A, to the "Company," "we," "us," "our" or "ours" or similar words are to Hilltop Holdings Inc. and its direct and indirect wholly owned subsidiaries, references to "Hilltop" refer solely to Hilltop Holdings Inc., references to "PCC" refer to PlainsCapital Corporation (a wholly owned subsidiary of Hilltop), references to "Securities Holdings" refer to Hilltop Securities Holdings LLC (a wholly owned subsidiary of Hilltop), references to "Hilltop Securities" refer to Hilltop Securities Inc. (a wholly owned subsidiary of Securities Holdings), references to "HTS Independent Network" refer to Hilltop Securities Independent Network Inc. (a wholly owned subsidiary of Securities Holdings), Hilltop Securities and HTS Independent Network are collectively referred to as the "Hilltop Broker-Dealers", references to the "Bank" refer to PlainsCapital Bank (a wholly owned subsidiary of PCC), references to "FNB" refer to First National Bank, references to "SWS" refer to the former SWS Group, Inc., references to "PrimeLending" refer to PrimeLending, a PlainsCapital Company (a wholly owned subsidiary of the Bank) and its subsidiaries as a whole, references to "NLC" refer to National Lloyds Corporation (a wholly owned subsidiary of Hilltop) and its subsidiaries as a whole, references to "NLIC" refer to National Lloyds Insurance Company (a wholly owned subsidiary of NLC) and references to "ASIC" refer to American Summit Insurance Company (a wholly owned subsidiary of NLC).

FORWARD-LOOKING STATEMENTS

This Quarterly Report includes "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934 (the "Exchange Act"), as amended by the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical fact, included in this Quarterly Report that address results or developments that we expect or anticipate will or may occur in the future, and statements that are preceded by, followed by or include, words such as "anticipates," "believes," "could," "estimates," "expects," "forecasts," "goal," "intends," "may," "might," "plan," "probable," "projects," "seeks," "should," "would" or the negative of these words and phrases or similar words or phrases, including such things as our business strategy, our financial condition, our efforts to make, and the timing of, strategic acquisitions, the costs of integration of the operations of acquired businesses, our revenue, our liquidity and sources of funding, market trends, operations and business, taxes, information technology expenses, capital levels, mortgage servicing rights ("MSR") assets, stock repurchases, dividend payments, expectations concerning mortgage loan origination volume and interest rate compression, expected levels of refinancing as a percentage of total loan origination volume, projected losses on mortgage loans originated, loss estimates related to natural disasters, total expenses and cost savings expected from PrimeLending's cost reduction efforts, the effects of government regulation applicable to our operations, the appropriateness of, and changes in, our allowance for loan losses and provision for loan losses, anticipated investment yields, our expectations regarding accretion of discount on loans in future periods, the collectability of loans, cybersecurity incidents and the outcome of litigation are forward-looking statements.

These forward-looking statements are based on our beliefs, assumptions and expectations of our future performance taking into account all information currently available to us. These beliefs, assumptions and expectations are subject to risks and uncertainties and can change as a result of many possible events or factors, not all of which are known to us. If an event occurs, our business, business plan, financial condition, liquidity and results of operations may vary materially from those expressed in our forward-looking statements. Certain factors that could cause actual results to differ include, among others:

the credit risks of lending activities, including our ability to estimate loan losses as well as the effects of changes in the level of, and trends in, loan delinquencies and write-offs;

changes in the interest rate environment;

changes in general economic, market and business conditions in areas or markets where we compete, including changes in the price of crude oil;

· risks associated with concentration in real estate related loans;

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effectiveness of our data security controls in the face of cyber attacks;

severe catastrophic events in Texas and other areas of the southern United States;

- the effects of our indebtedness on our ability to manage our business successfully, including the restrictions imposed by the indenture governing our indebtedness;
- cost and availability of capital;
- changes in state and federal laws, regulations or policies affecting one or more of our business segments, including changes in regulatory fees, deposit insurance premiums, capital requirements and the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”);

changes in key management;

competition in our banking, broker-dealer, mortgage origination and insurance segments from other banks and financial institutions as well as investment banking and financial advisory firms, mortgage bankers, asset-based non-bank lenders, government agencies and insurance companies;

legal and regulatory proceedings;

failure of our insurance segment reinsurers to pay obligations under reinsurance contracts;

risks associated with merger and acquisition integration; and

our ability to use excess capital in an effective manner.

For a more detailed discussion of these and other factors that may affect our business and that could cause the actual results to differ materially from those anticipated in these forward-looking statements, see “Risk Factors” in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2018 (“2018 Form 10-K”), which was filed with the Securities and Exchange Commission (the “SEC”) on February 15, 2019, this Item 2, “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” Part II, Item 1A, “Risk Factors” herein and other filings we have made with the SEC. We caution that the foregoing list of factors is not exhaustive, and new factors may emerge, or changes to the foregoing factors may occur, that could impact our business. All subsequent written and oral forward-looking statements concerning our business attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements above. We do not undertake any obligation to update any forward-looking statement, whether written or oral, relating to the matters discussed in this Quarterly Report except to the extent required by federal securities laws.

OVERVIEW

We are a financial holding company registered under the Bank Holding Company Act of 1956. Our primary line of business is to provide business and consumer banking services from offices located throughout Texas through the Bank. We also provide an array of financial products and services through our broker-dealer, mortgage origination and insurance segments. The following includes additional details regarding the financial products and services provided

by each of our primary business units.

PCC. PCC is a financial holding company that provides, through its subsidiaries, traditional banking and wealth, investment and treasury management services primarily in Texas and residential mortgage loans throughout the United States.

Securities Holdings. Securities Holdings is a holding company that provides, through its subsidiaries, investment banking and other related financial services, including municipal advisory, sales, trading and underwriting of taxable and tax-exempt fixed income securities, equity trading, clearing, securities lending, structured finance and retail brokerage services throughout the United States.

NLC. NLC is a property and casualty insurance holding company that provides, through its subsidiaries, fire and homeowners insurance to low value dwellings and manufactured homes primarily in Texas and other areas of the southern United States.

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During the three months ended March 31, 2019, our net income to common stockholders was \$38.8 million, or \$0.41 per diluted share. We declared total common dividends of \$0.08 per share during the three months ended March 31, 2019, which resulted in a dividend payout ratio of 19.32%. Dividend payout ratio is defined as cash dividends declared per common share divided by basic earnings per common share.

We reported \$51.4 million of consolidated income before income taxes during the three months ended March 31, 2019, including the following contributions from our four reportable business segments.

- The banking segment contributed \$41.6 million of income before income taxes during the three months ended March 31, 2019;
- The broker-dealer segment contributed \$16.4 million of income before income taxes during the three months ended March 31, 2019;
- The mortgage origination segment contributed \$2.9 million of income before income taxes during the three months ended March 31, 2019; and
- The insurance segment contributed \$6.8 million of income before income taxes during the three months ended March 31, 2019.

At March 31, 2019, on a consolidated basis, we had total assets of \$13.5 billion, total deposits of \$8.3 billion, total loans, including loans held for sale, of \$8.0 billion and stockholders' equity of \$2.0 billion.

Factors Affecting Results of Operations

Changes in Management

On February 21, 2019, we entered into a Separation and Release Agreement (the "Separation Agreement") with Alan B. White, our Vice Chairman and Co-Chief Executive Officer, in connection with his retirement effective April 1, 2019 (the "Retirement Date"). Pursuant to the Separation Agreement, effective as of the Retirement Date, Mr. White resigned from all positions with Hilltop and its subsidiaries, including, without limitation, Vice Chairman of our Board of Directors and Co-Chief Executive Officer of Hilltop. The Separation Agreement also provides that Mr. White's retention agreement by and between the Company and Mr. White, as amended, terminated on the Retirement Date, except for certain provisions that addressed, among other items, non-competition, non-solicitation, confidential information and arbitration. Effective April 1, 2019, Jeremy B. Ford became Hilltop's sole Chief Executive Officer, Chairman of the Executive Committee of the Board of Directors of Hilltop and the Chairman of the Bank. The Separation Agreement, in accordance with Mr. White's retention agreement, provided for aggregate payments of \$12.4 million to Mr. White, subject to any delay required under Section 409A of the Internal Revenue Code. During the first quarter of 2019, our financial results included the recognition within corporate of a pre-tax charge within employees' compensation and benefits of \$5.8 million associated with Mr. White's retirement, but we expect his retirement to reduce our employees' compensation and benefits expense in future periods.

On February 19, 2019, we entered into a retention agreement with Hill A. Feinberg (the "Feinberg Retention Agreement") to set forth the terms of his ongoing role with the Company. As disclosed in our current report on Form 8-K filed on December 12, 2018, we appointed M. Bradley Wings to succeed Mr. Feinberg as President and Chief Executive Officer of Hilltop Securities effective February 20, 2019. The Feinberg Retention Agreement provides that, as of February 20, 2019, Mr. Feinberg resigned as President and Chief Executive Officer of Hilltop Securities and from all other positions with Hilltop and its subsidiaries, other than as Chairman of the Board of Directors of Hilltop Securities, as a member of the Board of Directors of Hilltop and a member of Executive Committee of the Board of Directors of Hilltop. Pursuant to the Feinberg Retention Agreement, Mr. Feinberg will continue to serve as the Chairman of the Board of Directors of Hilltop Securities until June 30, 2019, at which time he will become Chairman Emeritus of Hilltop Securities and resign from his membership on the Executive Committee of the Board of Directors of Hilltop. The Feinberg Retention Agreement provides for aggregate payments of \$1.4 million to Mr. Feinberg upon his termination, resignation or death, of which \$0.9 million was paid during the first quarter of 2019. Mr. Feinberg may resign or be terminated at any time. In connection with the appointment of Mr. Wings, Hilltop and Mr. Wings entered into an employment agreement providing for a sign-on cash bonus of \$1.5 million, among other benefits, on the effective date of his employment. During the first quarter of 2019, the broker-dealer segment's financial results reflect aggregate pre-tax charges within employees' compensation and benefits noninterest expenses of \$2.2 million related to these items.

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During the three months ended March 31, 2019, the total impact of the above noted changes in management was \$8.0 million before income taxes. These changes and the related impact on our results of operations are collectively referred to as the “Leadership Changes.”

Technology Enhancements and Corporate Initiatives

In furtherance of our goal of building a premier, diversified financial services company, we regularly evaluate strategic opportunities to invest in our business and technology platforms. Such investments are intended to support long-term technological competitiveness and improved operational efficiencies throughout our organization. During 2018, we began the significant investment in new technological solutions, substantial core system upgrades and other technology enhancements, and we are working on preliminary plans for additional investments in such solutions, upgrades and enhancements. Such significant investments specifically include single, enterprise-wide general ledger and procurement solutions, a mortgage loan origination system and a core system replacement within our broker-dealer segment (collectively referred to as “Core System Improvements”). In combination with these technology enhancements, we have begun the consolidation of common back office functions. We believe that costs incurred related to these Core System Improvements will continue to represent an increasingly significant portion of our noninterest expenses in the near term, but we are making such investments with the expectation that they will result in cost savings over the long term. Costs related to our Core System Improvements, disaggregated by segment between internal-use software costs that were capitalized as premises and equipment and costs that were recorded to noninterest expense, were as follows (in thousands).

Three Months Ended March 31, 2019	Mortgage					Hilltop
	Banking	Broker-Dealer	Origination	Insurance	Corporate	Consolidated
Premises and equipment	\$ —	\$ 1,151	\$ 2,001	\$ —	\$ 218	\$ 3,370
Noninterest expense	—	1,043	1,022	—	402	2,467
Total	\$ —	\$ 2,194	\$ 3,023	\$ —	\$ 620	\$ 5,837

Three Months Ended March 31, 2018	Mortgage					Hilltop
	Banking	Broker-Dealer	Origination	Insurance	Corporate	Consolidated
Premises and equipment	\$ —	\$ 129	\$ —	\$ —	\$ —	\$ 129
Noninterest expense	—	1,215	549	—	344	2,108
Total	\$ —	\$ 1,344	\$ 549	\$ —	\$ 344	\$ 2,237

Factors Affecting Comparability of Results of Operations

Prior Year Acquisition

On August 1, 2018, we acquired privately-held, Houston-based The Bank of River Oaks (“BORO”) in an all-cash transaction (the “BORO Acquisition”). Pursuant to the terms of the definitive agreement, we paid cash in the aggregate amount of \$85 million to the shareholders and option holders of BORO. The fair value of the assets acquired was \$434.8 million, including \$326.6 million in loans, while the fair value of liabilities assumed was \$389.4 million, consisting primarily of \$376.4 million in deposits. The operations of BORO were included in our operating results beginning August 1, 2018. The estimated fair value of the core deposit intangible asset acquired as of August 1, 2018 was \$10.0 million and resulting goodwill was \$39.6 million. In connection with the acquisition, we merged BORO into the Bank, and all customer accounts were converted to the PlainsCapital Bank platform.

Termination of FDIC Loss-Share Agreements

In the fourth quarter of 2018, the Bank terminated its loss-share agreements with the FDIC which were entered into in connection with the FNB Transaction, resulting in a \$6.26 million payment from the FDIC to the Bank. Prior to the termination, the Bank recorded “true-up” accruals with respect to the FNB Transaction loss-share agreements with the FDIC of \$0.1 million during the three months ended March 31, 2018. The true-up accrual was based on a formula within the loss-share agreements, pursuant to which we agreed to reimburse the FDIC if actual losses incurred and billed to the FDIC through loss sharing were below a stated threshold. During the three months ended March 31, 2018, the Bank also recorded \$3.9 million of amortization of excess book value of its receivables under the loss-share agreements (the “FDIC Indemnification Asset”) due to lower projected collections from the FDIC than were initially estimated at the acquisition date.

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Segment Information

We have three primary business units, PCC (banking and mortgage origination), Securities Holdings (broker-dealer) and NLC (insurance). Under accounting principles generally accepted in the United States (“GAAP”), our business units are comprised of four reportable business segments organized primarily by the core products offered to the segments’ respective customers: banking, broker-dealer, mortgage origination and insurance. Consistent with our historical segment operating results, we anticipate that future revenues will be driven primarily from the banking segment, with the remainder being generated by our broker-dealer, mortgage origination and insurance segments. Operating results for the mortgage origination segment have historically been more volatile than operating results for the banking, broker-dealer and insurance segments.

The banking segment includes the operations of the Bank, and since August 1, 2018, the operations acquired in the BORO Acquisition. The banking segment primarily provides business and consumer banking services from offices located throughout Texas and generates revenue from its portfolio of earning assets. The Bank’s results of operations are primarily dependent on net interest income. The Bank also derives revenue from other sources, including service charges on customer deposit accounts and trust fees.

The broker-dealer segment includes the operations of Securities Holdings, which operates through its wholly owned subsidiaries Hilltop Securities and HTS Independent Network. The broker-dealer segment generates a majority of its revenues from fees and commissions earned from investment advisory and securities brokerage services. Hilltop Securities is a broker-dealer registered with the SEC and the Financial Industry Regulatory Authority (“FINRA”) and a member of the New York Stock Exchange (“NYSE”), HTS Independent Network is an introducing broker-dealer that is also registered with the SEC and FINRA. Hilltop Securities, HTS Independent Network and Hilltop Securities Asset Management, LLC, a wholly-owned subsidiary of First Southwest Holdings, LLC, are registered investment advisers under the Investment Advisers Act of 1940.

The mortgage origination segment includes the operations of PrimeLending, which offers a variety of loan products and generates revenue predominantly from fees charged on the origination and servicing of loans and from selling these loans in the secondary market.

The insurance segment includes the operations of NLC, which operates through its wholly owned subsidiaries, NLIC and ASIC, in Texas and other areas of the southern United States. Insurance segment income is primarily generated from revenue earned on net insurance premiums less loss and loss adjustment expenses (“LAE”) and policy acquisition and other underwriting expenses.

Corporate includes certain activities not allocated to specific business segments. These activities include holding company financing and investing activities, merchant banking investment opportunities, and management and administrative services to support the overall operations of the Company.

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The eliminations of intercompany transactions are included in “All Other and Eliminations.” Additional information concerning our reportable segments is presented in Note 23, Segment and Related Information, in the notes to our consolidated financial statements. The following table presents certain information about the operating results of our reportable segments (in thousands). This table serves as a basis for the discussion and analysis in the segment operating results sections that follow.

	Three Months Ended March 31,		Variance 2019 vs 2018		
	2019	2018	Amount	Percent	
Net interest income (expense):					
Banking	\$ 92,690	\$ 86,638	\$ 6,052	7	%
Broker-Dealer	12,850	12,550	300	2	%
Mortgage Origination	(467)	941	(1,408)	(150)	%
Insurance	642	787	(145)	(18)	%
Corporate	(1,330)	(2,091)	761	36	%
All Other and Eliminations	4,546	4,595	(49)	(1)	%
Hilltop Consolidated	\$ 108,931	\$ 103,420	\$ 5,511	5	%
Provision (recovery) for loan losses:					
Banking	\$ 1,025	\$ (1,531)	\$ 2,556	167	%
Broker-Dealer	(74)	(276)	202	73	%
Mortgage Origination	—	—	—	—	%
Insurance	—	—	—	—	%
Corporate	—	—	—	—	%
All Other and Eliminations	—	—	—	—	%
Hilltop Consolidated	\$ 951	\$ (1,807)	\$ 2,758	153	%
Noninterest income:					
Banking	\$ 10,621	\$ 10,180	\$ 441	4	%
Broker-Dealer	91,307	68,547	22,760	33	%
Mortgage Origination	118,033	127,102	(9,069)	(7)	%
Insurance	36,492	35,018	1,474	4	%
Corporate	538	(712)	1,250	176	%
All Other and Eliminations	(4,523)	(4,992)	469	9	%
Hilltop Consolidated	\$ 252,468	\$ 235,143	\$ 17,325	7	%
Noninterest expense:					
Banking	\$ 60,726	\$ 59,370	\$ 1,356	2	%
Broker-Dealer	87,807	77,776	10,031	13	%
Mortgage Origination	114,677	130,704	(16,027)	(12)	%
Insurance	30,338	31,013	(675)	(2)	%
Corporate	15,562	9,403	6,159	66	%
All Other and Eliminations	(25)	(64)	39	61	%
Hilltop Consolidated	\$ 309,085	\$ 308,202	\$ 883	0	%

Income (loss) before income taxes:

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Banking	\$ 41,560	\$ 38,979	\$ 2,581	7	%
Broker-Dealer	16,424	3,597	12,827	357	%
Mortgage Origination	2,889	(2,661)	5,550	209	%
Insurance	6,796	4,792	2,004	42	%
Corporate	(16,354)	(12,206)	(4,148)	(34)	%
All Other and Eliminations	48	(333)	381	114	%
Hilltop Consolidated	\$ 51,363	\$ 32,168	\$ 19,195	60	%

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How We Generate Revenue

We generate revenue from net interest income and from noninterest income. Net interest income represents the difference between the income earned on our assets, including our loans and investment securities, and our cost of funds, including the interest paid on the deposits and borrowings that are used to support our assets. Net interest income is a significant contributor to our operating results and is primarily earned by our banking segment. Fluctuations in interest rates, as well as the amounts and types of interest-earning assets and interest-bearing liabilities we hold, affect net interest income. Net interest income increased during the three months ended March 31, 2019, compared with the three months ended March 31, 2018, primarily due to an increase within our banking segment and, to a lesser extent within our broker-dealer segment and corporate, partially offset by a decrease within our mortgage origination segment.

The other component of our revenue is noninterest income, which is primarily comprised of the following:

- (i) Income from broker-dealer operations. Through Securities Holdings, we provide investment banking and other related financial services. We generated \$56.1 million and \$57.1 million in securities commissions and fees and investment and securities advisory fees and commissions, and \$31.6 million and \$7.0 million in gains from derivative and trading portfolio activities (included within other noninterest income), during the three months ended March 31, 2019 and 2018, respectively.
- (ii) Income from mortgage operations. Through PrimeLending, we generate noninterest income by originating and selling mortgage loans. During the three months ended March 31, 2019 and 2018, we generated \$118.0 million and \$126.4 million, respectively, in net gains from the sale of loans, other mortgage production income (including income associated with retained mortgage servicing rights), and mortgage loan origination fees.
- (iii) Income from insurance operations. Through NLC, we provide fire and limited homeowners insurance for low value dwellings and manufactured homes. We generated \$33.2 million and \$34.3 million in net insurance premiums earned during the three months ended March 31, 2019 and 2018, respectively.

The increase in noninterest income noted in the table above was primarily due to increases of \$24.6 million in gains from derivative and trading portfolio activities and \$1.8 million in investment and securities advisory fees and commissions, partially offset by decreases of \$9.6 million in net gains from sale of loans and other mortgage production income and \$2.7 million in securities commissions and fees.

We also incur noninterest expenses in the operation of our businesses. Our businesses engage in labor intensive activities and, consequently, employees' compensation and benefits represent the majority of our noninterest expenses.

Consolidated Operating Results

Net income applicable to common stockholders during the three months ended March 31, 2019 was \$38.8 million, or \$0.41 per diluted share, compared with net income applicable to common stockholders of \$24.4 million, or \$0.25 per diluted share, during the three months ended March 31, 2018. The first quarter of 2019 included costs associated with significant Leadership Changes and other efficiency initiative-related charges which, in the aggregate, totaled \$8.7 million before income taxes.

Certain items included in net income for the three months ended March 31, 2019 and 2018 resulted from purchase accounting associated with the merger of PlainsCapital Corporation with and into a wholly owned subsidiary of Hilltop on November 30, 2012 (the “PlainsCapital Merger”), the Federal Deposit Insurance Corporation (“FDIC”) -assisted transaction (the “FNB Transaction”) whereby the Bank acquired certain assets and assumed certain liabilities of FNB, the acquisition of SWS Group, Inc. in a stock and cash transaction (the “SWS Merger”) and the BORO Acquisition (collectively, the “Bank Transactions”). Income before taxes during the three months ended March 31, 2019 and 2018, included the following purchase accounting items related to the Bank Transactions (in thousands).

Three Months Ended March 31, 2019	PlainsCapital Merger	FNB Transaction	SWS Merger	BORO Acquisition	Total
Net accretion on earning assets and liabilities	\$ 544	\$ 5,533	\$ 561	\$ 1,977	\$ 8,615
Amortization of identifiable intangibles	(1,001)	(76)	(174)	(714)	(1,965)
Three Months Ended March 31, 2018	PlainsCapital Merger	FNB Transaction	SWS Merger	BORO Acquisition	Total
Net accretion on earning assets and liabilities	\$ 574	\$ 8,377	\$ 708	\$ —	\$ 9,659
Amortization of identifiable intangibles	(1,448)	(114)	(195)	—	(1,757)

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We consider the ratios shown in the table below to be key indicators of our performance.

	Three Months Ended March 31,			
	2019		2018	
Return on average stockholder's equity	8.04	%	5.19	%
Return on average assets	1.21	%	0.77	%
Net interest margin (1) (3) (4)	3.69	%	3.52	%
Net interest margin (taxable equivalent) (2) (3) (4)	3.70	%	3.53	%

- (1) Net interest margin is defined as net interest income divided by average interest-earning assets.
- (2) Net interest margin (taxable equivalent), a non-GAAP measure, is defined as taxable equivalent net interest income divided by average interest-earning assets. Annualized taxable equivalent adjustments are based on the applicable corporate federal income tax rate of 21%. The interest income earned on certain earnings assets is completely or partially exempt from federal income tax. See footnote 2 to the following tables for the taxable equivalent adjustments to interest income.
- (3) The securities financing operations within our broker-dealer segment had the effect of lowering both the net interest margin and taxable equivalent net interest margin by 43 basis points and 42 basis points during the three months ended March 31, 2019 and 2018, respectively.
- (4) During the three months ended March 31, 2019 and 2018, purchase accounting contributed 32 basis points and 36 basis points, respectively, to both net interest margin and taxable equivalent net interest margin.

We present net interest margin in the previous table, and net interest margin and net interest income below, on a taxable equivalent basis. The interest income earned on certain earning assets is completely or partially exempt from federal income tax. As such, these tax-exempt instruments typically yield lower returns than taxable investments. To provide more meaningful comparisons of net interest margins for all earning assets, we use net interest income on a taxable- equivalent basis in calculating net interest margin by increasing the interest income earned on tax-exempt assets to make it fully equivalent to interest income earned on taxable investments.

During the three months ended March 31, 2019 and 2018, purchase accounting contributed 32 and 36 basis points, respectively, to our consolidated taxable equivalent net interest margin of 3.70% and 3.53%, respectively, and primarily related to the following purchase accounting items associated with the Bank Transactions (in thousands).

Three Months Ended March 31, 2019	PlainsCapital Merger	FNB Transaction	SWS Merger	BORO Acquisition	Total
Accretion of discount on loans	\$ 753	\$ 5,533	\$ 536	\$ 1,913	\$ 8,735
Accretion (amortization) of discount (premium) on acquired securities	(209)	—	7	64	(138)

Three Months Ended March 31, 2018	PlainsCapital Merger	FNB Transaction	SWS Merger	BORO Acquisition	Total
Accretion of discount on loans	\$ 938	\$ 8,377	\$ 552	\$ —	\$ 9,867
Amortization of premium on acquired securities	(410)	—	—	—	(410)

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The table below provides additional details regarding our consolidated net interest income (dollars in thousands).

	Three Months Ended March 31, 2019				2018			
	Average Outstanding Balance	Interest Earned or Paid	Annualized Yield or Rate		Average Outstanding Balance	Interest Earned or Paid	Annualized Yield or Rate	
Assets								
Interest-earning assets								
Loans held for sale	\$ 1,015,010	\$ 12,487	4.92	%	\$ 1,294,245	\$ 14,613	4.52	%
Loans held for investment, gross								
(1)	6,843,343	98,383	5.76	%	6,308,756	85,331	5.42	%
Investment securities - taxable	1,792,501	15,584	3.48	%	1,613,608	10,928	2.71	%
Investment securities - non-taxable (2)	221,602	1,658	2.99	%	258,732	2,030	3.14	%
Federal funds sold and securities purchased under agreements to resell	66,346	388	2.37	%	189,623	481	1.03	%
Interest-bearing deposits in other financial institutions	505,582	3,151	2.53	%	632,727	2,478	1.59	%
Securities borrowed	1,446,412	16,859	4.66	%	1,537,306	16,300	4.24	%
Other	61,263	1,671	11.01	%	70,854	1,452	8.27	%
Interest-earning assets, gross (2)	11,952,059	150,181	5.03	%	11,905,851	133,613	4.50	%
Allowance for loan losses	(59,549)				(65,202)			
Interest-earning assets, net	11,892,510				11,840,649			
Noninterest-earning assets	1,419,075				1,228,058			
Total assets	\$ 13,311,585				\$ 13,068,707			