





BUSINESS BANKING \ BETTER BANKING

At CommunityBank of Texas, relationships are the bedrock of our business. They are a reflection of our deep commitment to building strong, honest partnerships in all we do, and our mandate to measure our performance by the success we create for our partners.

Service to others, both financially and philanthropically, is a core pillar of our brand, and we pledge that every time is the right time to put our clients' and our communities' needs first.

We're proud to be here, to live in and serve the cities and communities of Southeast Texas. Thank you for trusting our dedicated team at CommunityBank of Texas to be your better business banking partner.







Dear Shareholders,

For community banks, our strength is often the resolve of our customers and our employees to find the right answers as we work together to solve issues on an individualized basis. Neither we nor our customers caused the current economic conditions. We will be working with our customers to get through this time of anxiety. Your bank has many tools available to help weather this storm and we will use all means in our tool belt to get our customers and ourselves to a better time.

As I write to you today, we are in the early stages of the COVID-19 crisis, oil prices have dropped to the lowest level in 18 years, the Federal Reserve has lowered interest rates to zero and the stock market cannot seem to find its footing. Each of these challenges alone might seem daunting, but we have them all together, pulling at each other at every minute. We are experiencing stresses to the economy and stresses to the lives of every American and country in the world.

Given these challenges, one might tend to be overwhelmed. But the great employees of CBTX, Inc., are not. This unique set of circumstances is not the first stressful time that our team has experienced over the years. The same holds true for our customers. We do not know how long COVID-19 will be with us. Perhaps it never completely goes away. But we have faith in our medical professionals to find prevention and treatment strategies that will ultimately curb and control this virus enough for us to go on with our lives. As we know, disruption leads to innovation, which eventually translates to improvement and ultimately, opportunity.

I would be remiss if I did not acknowledge the great job our team did in 2019. Because of our incredible employees and their work with our customers, we delivered record profitability for 2019. We finished the year with a strong net interest margin, strong capital and strong credit quality. As a result, we have a very solid capital base from which to work through problems that may result from the current economic stresses.

We have a very experienced team that has been through hurricanes, floods, economic downturns, high interest rates, low interest rates – the many interruptions that life may throw our way. Although each disturbance is different, the experience is the same.

We know that the next several months will be difficult for our families, our communities, our customers, our employees and our shareholders. We will rely on the strength of our capital, our resilient customer base and our experienced, hardworking team to get us all through this storm and on to reach our desired goals. We feel that CBTX, Inc., is uniquely poised to take advantage of opportunities as they may present themselves.

I urge you to take care of yourselves and each other. That is always our goal at CBTX, Inc. My expectations are for continued great things for CBTX, Inc., over the long term.

Thank you for your faith in CBTX, Inc.

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ROBERT R. FRANKLIN, JR. \ Chairman, President & CEO



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

FORM 10-K

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

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

For the fiscal year ended December 31, 2019

or

For the transition period from to	Commission File Number: 00	1-38280
	CBTX, Inc.	
	(Exact name of registrant as specified	1 in its charter)
Texas (State or other jurisdiction incorporation or organization)		i
	(713) 210-7600	
	(Registrant's telephone number, inclu	ding area code)
Securities registered pursuant to Section 12(b) or	f the Act:	
Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common stock, par value \$0.01 per share	CBTX	The Nasdaq Global Select Market
Indicate by check mark if the registrant is a well-	-known seasoned issuer, as defined in	Rule 405 of the Securities Act. Yes □ No ⊠
Indicate by check mark if the registrant is not red	quired to file reports pursuant to Secti	on 13 or Section 15(d) of the Act. Yes □ No ⊠
	ch shorter period that the registrant wa	filed by Section 13 or 15(d) of the Securities Exchange Act of as required to file such reports) and (2) has been subject to such
		ractive Data File required to be submitted pursuant to Rule 405 ach shorter period that the registrant was required to submit such
		ed filer, a non-accelerated filer, a smaller reporting company or rated filer," "smaller reporting company," and emerging growth
Large accelerated filer □	Accelerate	
Non-accelerated filer □		porting company □ growth company ⊠
If an emerging growth company, indicate by che new or revised financial accounting standards pr		ot to use the extended transition period for complying with any e Exchange Act. ⊠
Indicate by check mark whether the registrant is	a shell company (as defined in Rule 1	2b-2 of the Exchange Act). Yes □ No 🗵

Document Incorporated by Reference:

As of June 30, 2019, the aggregate market value of the registrant's common stock held by non-affiliates was approximately \$498.7 million.

As of February 21, 2020, there were 25,195,123 shares of the registrant's common stock, par value \$0.01 per share outstanding, including

Portions of the registrant's Definitive Proxy Statement relating to the 2020 Annual Meeting of Shareholders are incorporated by reference into Part III of this Annual Report on Form 10-K to the extent stated herein. Such Definitive Proxy Statement will be filed with the Securities and Exchange Commission within 120 days after the end of the registrant's fiscal year ended December 31, 2019.

210,400 shares of unvested restricted stock deemed to have beneficial ownership.

CBTX, INC.

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PART I.

Item 1. Business

The disclosures set forth in this item are qualified by Item 1A. "Risk Factors" and the section captioned "Cautionary Note Regarding Forward-Looking Statements" in Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations" of this Annual Report on Form 10-K and other cautionary statements set forth elsewhere in this Annual Report on Form 10-K.

CBTX, Inc., is a bank holding company incorporated in Texas in 2007. All references to "we," "our," "us," "ourselves," and "the Company" refer to CBTX, Inc. and its consolidated subsidiaries and all references to "CommunityBank of Texas" or "the Bank" refer to CommunityBank of Texas, National Association, its wholly-owned bank subsidiary, unless otherwise indicated or the context otherwise requires. All references to "Houston" refer to the Houston-The Woodlands-Sugar Land Metropolitan Statistical Area, or MSA and surrounding counties references to "Beaumont" refer to the Beaumont-Port Arthur MSA and surrounding counties and references to "Dallas" refer to the Dallas-Fort Worth-Arlington MSA and surrounding counties.

The Bank's headquarters are located at 5999 Delaware Street, Beaumont, Texas 77706 and the telephone number is (409) 861-7200. A majority of the Company's executives are located in our Houston office at 9 Greenway Plaza, Suite 110, Houston, Texas 77046 and the telephone number is (713) 210-7600. The Company completed an initial public offering of its common stock on November 10, 2017. The Company's common stock is listed on the Nasdaq Global Select Market, or Nasdaq, under the symbol "CBTX."

The Bank operates 19 branches located in the Houston market, 15 branches located in the Beaumont market and one branch in the Dallas market. The Company has experienced significant organic growth since commencing banking operations, as well as growth through mergers, acquisitions and *de novo* branches. The Company is focused on controlled profitable growth. Total assets increased from \$2.6 billion at December 31, 2014 to \$3.5 billion as of December 31, 2019 and return on average assets improved from 0.9% for the year ended December 31, 2014 to 1.50% for the year ended December 31, 2019.

The Company's merger, acquisition and expansion history includes the following:

	Date		Branches	
(Dollars in millions)	Acquired/Added	Assets Acquired	Acquired/Added	Location
Bank Acquired (1)				
County Bancshares, Inc./County Bank, N.A	August 2007	\$ 130	-	Beaumont
Crosby Bancshares, Inc. (Crosby State Bank)	December 2008	439	8	Houston
Founders Bank, SSB	July 2011	124	1	Houston
VB Texas, Inc. (Vista Bank Texas)	July 2013	665	7	Houston
MC Bancshares, Inc. (Memorial City Bank)	February 2015	268	2	Houston
Branch Added				
Pasadena Branch	July 2012	-	1	Houston
Westchase Branch	May 2014	-	1	Houston
The Woodlands Branch	May 2015	-	1	Houston
South Belt Branch	January 2019	-	1	Houston
Dallas Preston Center Branch	January 2019	-	1	Dallas

⁽¹⁾ Assets of acquired banks are as of the most recent quarter prior to their respective close dates.

The Company began operations in Beaumont and surrounding counties and expanded into the Houston market. The loan portfolio at December 31, 2019 was 74.1% in the Houston market and 24.6% in the Beaumont market. In November 2018, the Bank opened a loan production office in Dallas, which became a full branch in January 2019. The Company believes that there are significant ongoing growth opportunities in its markets.

The Bank is primarily a business bank and its focus is on providing commercial banking solutions to small and mid-sized businesses and professionals including attorneys, accountants and other professional service providers with operations in our markets. The Bank offers a broad range of banking products, including commercial and industrial loans, commercial real estate loans, construction and development loans, 1-4 family residential mortgage loans, multi-family residential loans consumer loans, agricultural loans, treasury services, traditional retail deposits and a full suite of online banking services. The Bank has a relationship-based approach, and at December 31, 2019, 82.1% of the Bank's loan customers had a deposit relationship with the Bank.

The banking and financial services industry is highly competitive, and the Company competes with a wide range of financial institutions within its markets, including local, regional and national commercial banks and credit unions. The Company also competes with mortgage companies, brokerage firms, consumer finance companies, mutual funds, securities firms, insurance companies, third-party payment processors, financial technology, or fintech companies and other financial intermediaries for certain of our products and services. Some of the Company's competitors are not subject to the same regulatory restrictions and the level of regulatory supervision applicable to the Company.

Interest rates on loans and deposits, as well as prices on fee-based services, are typically significant competitive factors within the banking and financial services industry. Many of the Company's competitors are much larger financial institutions that have greater financial resources and compete aggressively for market share. These competitors attempt to gain market share through their financial product mix, pricing strategies and banking center locations. Other important competitive factors in our industry and markets include office locations and hours, quality of customer service, community reputation, continuity of personnel and services, capacity and willingness to extend credit and ability to offer sophisticated banking products and services.

The Bank seeks to remain competitive with respect to fees charged, interest rates and pricing and the Bank believes that its broad and sophisticated suite of financial solutions, high-quality customer service culture, positive reputation and long-standing community relationships enables it to compete successfully within its markets and enhances its ability to attract and retain customers.

Employees

The Company's success depends on its ability to attract and retain highly qualified senior and middle management and other skilled employees. Competition for qualified employees can be intense and it may be difficult to locate personnel with the necessary combination of skills, attributes and business relationship.

Additionally, the Company is committed to employee development, including a mentorship program, which provides retail staff with one on one training with experienced employees. The Company also has an officer development program with formal in-house training programs for junior bankers including guidance from senior banking team members.

As of December 31, 2019, the Company employed 500 full-time equivalent employees.

Available Information

The Company's website address is www.communitybankoftx.com. The Company makes available free of charge on or through its website its annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, as soon as reasonably practicable after such materials are electronically filed with or furnished to the Securities and Exchange Commission, or SEC. Information contained on the Company's website is not incorporated by reference into this Annual Report on Form 10-K and is not part of this or any other report that the Company files with or furnishes to the SEC. The SEC maintains an internet site that contains reports, proxy statements and other information that the Company files with or furnishes to the SEC and these reports may be accessed at http://www.SEC.gov.

Supervision and Regulation

The United States, or U.S., banking industry is highly regulated under federal and state law. Consequently, our growth and earnings performance will be affected not only by management decisions and general and local economic

conditions, but also by the statutes administered by, and the regulations and policies of, various governmental regulatory authorities. These authorities include the Board of Governors of the Federal Reserve System, or Federal Reserve, Office of the Comptroller of the Currency, or OCC, Federal Deposit Insurance Corporation, or FDIC, Consumer Financial Protection Bureau, or CFPB, Internal Revenue Service, or IRS, and state taxing authorities. The effect of these statutes, regulations and policies, and any changes to such statutes, regulations and policies, can be significant and cannot be predicted.

The primary goals of the bank regulatory scheme are to maintain a safe and sound banking system, facilitate the conduct of sound monetary policy and promote fairness and transparency for financial products and services. The system of supervision and regulation applicable to us and our subsidiaries establishes a comprehensive framework for their respective operations and is intended primarily for the protection of the FDIC's Deposit Insurance Fund, the Bank's depositors and the public, rather than our shareholders or creditors. The description below summarizes certain elements of the applicable bank regulatory framework. This description is not intended to describe all laws and regulations applicable to us and our subsidiaries, and the description is qualified in its entirety by reference to the full text of the statutes, regulations, policies, interpretive letters and other written guidance that are described herein.

Financial Services Industry Reform. On July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act, or Dodd-Frank Act, was enacted. The Dodd-Frank Act has had a broad impact on the financial services industry, including significant regulatory and compliance changes such as, among many other things, (i) enhanced resolution authority of troubled and failing banks and their holding companies; (ii) increased regulatory examination fees; (iii) creation of the CFPB, an independent organization dedicated to promulgating and enforcing consumer protection laws applicable to all entities offering consumer financial products or services; and (iv) numerous other provisions designed to improve supervision and oversight of, and strengthen safety and soundness for, the financial services sector. Additionally, the Dodd-Frank Act established a new framework for systemic risk oversight within the financial system to be distributed among new and existing federal regulatory agencies, including the Financial Stability Oversight Council, the Federal Reserve, the OCC and the FDIC.

On May 24, 2018, the Economic Growth, Regulatory Relief, and Consumer Protection Act, or the Regulatory Relief Act, was enacted. The Regulatory Relief Act repealed or modified several provisions of the Dodd-Frank Act and included a number of burden reduction measures for community banks, including, among other things, directing the federal banking regulators to develop a community bank leverage ratio for banking organizations that have less than \$10.0 billion in total assets and have certain risk profiles, exempting certain banking organizations with less than \$10.0 billion or less in total assets from the Volcker Rule (discussed below), narrowing and simplifying the definition of high volatility commercial real estate, and requiring the federal banking regulators to raise the asset threshold under the Small Bank Holding Company and Savings and Loan Holding Company Policy Statement from \$1.0 billion to \$3.0 billion.

The Regulatory Relief Act also expands the eligibility for certain small banks to undergo 18-month examination cycles, rather than annual cycles, raising the consolidated asset threshold from \$1.0 billion to \$3.0 billion for eligible banks. In addition, the Regulatory Relief Act added certain protections for consumers, including veterans and active duty military personnel and student borrowers, expanded credit freezes and created an identity theft protection database. The Regulatory Relief Act requires the enactment of a number of implementing regulations, the details of which may have a material effect on the ultimate impact of the law.

Regulatory Capital Rules. The Company and the Bank are each required to comply with applicable capital adequacy standards established by the Federal Reserve and the OCC. The current risk-based capital standards applicable to the Company and the Bank are based on the December 2010 final capital framework for strengthening international capital standards, known as Basel III, of the Basel Committee on Banking Supervision, or Basel Committee. In July 2013, the federal bank regulators approved final rules, the Basel III Capital Rules, implementing the Basel III framework as well as certain provisions of the Dodd-Frank Act. The Basel III Capital Rules became effective for the Company and the Bank on January 1, 2015 (subject to a phase-in period for certain provisions). The Basel III Capital Rules require banks and bank holding companies, including the Company and the Bank, to maintain four minimum capital standards: (1) a Tier 1 capital-to-adjusted total assets ratio, or leverage capital ratio, of at least 4.0%; (2) a Tier 1 capital to risk-weighted assets ratio, or Tier 1 risk-based capital ratio, of at least 6.0%; (3) a total risk-based capital (Tier 1 plus Tier 2) to risk-weighted assets ratio, or total risk-based capital ratio, of at least 8.0%; and (4) a Common Equity Tier 1, or CET1, capital ratio of at least 4.5%.

The Basel III Capital Rules also require bank holding companies and banks to maintain a "capital conservation buffer" on top of the minimum risk-based capital ratios. The buffer is intended to help ensure that banking organizations conserve capital when it is most needed, allowing them to better weather periods of economic stress. The buffer, which became fully phased in on January 1, 2019, requires banking organizations to hold CET1 capital in excess of the minimum risk-based capital ratios by at least 2.5% to avoid limits on capital distributions and certain discretionary bonus payments to executive officers and similar employees.

The Basel III Capital Rules attempted to improve the quality of capital by implementing changes to the definition of capital. Among the most important changes were stricter eligibility criteria for regulatory capital instruments that disallow the inclusion of certain instruments, such as trust preferred securities (other than grandfathered trust preferred securities), in Tier 1 capital, new constraints on the inclusion of minority interests, mortgage-servicing assets, deferred tax assets and certain investments in the capital of unconsolidated financial institutions, and the requirement that most regulatory capital deductions be made from CET1 capital. The Basel III Capital Rules also changed the methods of calculating certain risk-weighted assets, which in turn affected the calculation of risk-based ratios. Under the Basel III Capital Rules, higher or more sensitive risk weights are assigned to various categories of assets, including certain credit facilities that finance the acquisition, development or construction of real property, certain exposures or credits that are 90 days past due or on nonaccrual status, foreign exposures and certain corporate exposures. In addition, these rules include greater recognition of collateral and guarantees, and revised capital treatment for derivatives and repo-style transactions.

The Basel III Capital Rules permit the Federal Reserve and the OCC to set higher capital requirements for individual institutions whose circumstances warrant it. For example, institutions experiencing internal growth or making acquisitions are expected to maintain strong capital positions substantially above the minimum supervisory levels, without significant reliance on intangible assets. At this time, the bank regulatory agencies are more inclined to impose higher capital requirements to meet "well capitalized" standards and future regulatory change could impose higher capital standards as a routine matter. The Company's regulatory capital ratios and those of the Bank are in excess of the levels established for "well capitalized" institutions under the rules.

The federal banking regulators have modified certain aspects of the Basel III Capital Rules since the rules were initially published, and additional modifications may be made in the future. In December 2017, the Basel Committee published standards that it described as the finalization of the Basel III post-crisis regulatory reforms (commonly referred to as Basel IV). Among other things, these standards revise the Basel Committee's standardized approach for credit risk (including by recalibrating risk weights and introducing new capital requirements for certain "unconditionally cancellable commitments," such as unused credit card lines of credit) and provides a new standardized approach for operational risk capital. Under the Basel framework, these standards will generally be effective on January 1, 2022, with an aggregate output floor phasing in through January 1, 2027. Under the current U.S. capital rules, operational risk capital requirements and a capital floor apply only to advanced approaches institutions, and not to the Company or the Bank. The impact of Basel IV on us will depend on the manner in which it is implemented by the federal banking regulators.

Pursuant to the Regulatory Relief Act, the Federal Reserve, the OCC and the FDIC published final rules implementing the community bank leverage ratio. Under the final rules, which went into effect on January 1, 2020, depository institutions and depository institution holding companies that have less than \$10.0 billion in total consolidated assets and meet other qualifying criteria, including a leverage capital ratio of greater than 9.0%, off-balance-sheet exposures of 25.0% or less of total consolidated assets and trading assets plus trading liabilities of 5.0% or less of total consolidated assets, are deemed "qualifying community banking organizations" and are eligible to opt into the community bank leverage ratio framework. A qualifying community banking organization that elects to use the community bank leverage ratio framework and that maintains a leverage capital ratio of greater than 9.0% is considered to have satisfied the generally applicable risk-based and leverage capital requirements under the Basel III Capital Rules and, if applicable, is considered to have met the "well capitalized" ratio requirements for purposes of its primary federal regulator's prompt corrective action rules, discussed below. The final rules include a two-quarter grace period during which a qualifying community banking organization that temporarily fails to meet any of the qualifying criteria, including the greater-than-9.0% leverage capital ratio requirement, is generally still deemed "well capitalized" so long as the banking organization maintains a leverage capital ratio greater than 8.0%. A banking organization that fails to maintain a leverage capital ratio greater than 8.0% is not permitted to use the grace period and must comply with the generally applicable requirements under the Basel III Capital Rules and file the appropriate regulatory reports. The Company and the Bank have not made an election to use the community bank leverage ratio framework but may make such an election in the future.

Imposition of Liability for Undercapitalized Subsidiaries. Bank regulators are required to take prompt corrective action to resolve problems associated with insured depository institutions whose capital declines below certain levels as further described below. In the event an institution becomes undercapitalized, it must submit a capital restoration plan. The capital restoration plan will not be accepted by the regulators unless each company having control of the undercapitalized institution guarantees the subsidiary's compliance with the capital restoration plan up to a certain specified amount. Any such guarantee from a depository institution's holding company is entitled to a priority of payment in bankruptcy.

The aggregate liability of the holding company of an undercapitalized bank is limited to the lesser of 5.0% of the institution's assets at the time it became undercapitalized and the amount necessary to cause the institution to become adequately capitalized. The bank regulators have greater power in situations where an institution becomes significantly or critically undercapitalized or fails to submit a capital restoration plan. For example, a bank holding company controlling such an institution can be required to obtain prior Federal Reserve approval of proposed dividends or might be required to consent to a consolidation or to divest the troubled institution or other affiliates.

Volcker Rule. As mandated by the Dodd-Frank Act, in December 2013, the OCC, Federal Reserve, FDIC, SEC and Commodity Futures Trading Commission issued a final rule implementing certain prohibitions and restrictions on the ability of a banking entity and non-bank financial company supervised by the Federal Reserve to engage in proprietary trading and have certain ownership interests in, or relationships with, a "covered fund" (commonly referred to as the "Volcker Rule"). The Regulatory Relief Act discussed above included a provision exempting banking organizations with \$10.0 billion or less in total consolidation assets, and total trading assets and trading liabilities that are 5.0% or less of total consolidated assets, from the Volcker Rule. Thus, the Company and the Bank are not currently subject to the Volcker Rule.

CBTX, Inc.

As a bank holding company, we are subject to regulation under the Bank Holding Company Act of 1956, as amended, or BHC Act, and to supervision, examination and enforcement by the Federal Reserve. The BHC Act and other federal laws subject bank holding companies to particular restrictions on the types of activities in which they may engage, and to a range of supervisory requirements and activities, including regulatory enforcement actions for violations of laws and regulations. The Federal Reserve's jurisdiction also extends to any company that we directly or indirectly control, such as any nonbank subsidiaries and other companies in which we own a controlling investment.

Acquisitions by Bank Holding Companies. The BHC Act requires every bank holding company to obtain the prior approval of the Federal Reserve before it acquires all or substantially all of the assets of any bank, or ownership or control of any voting shares of any bank or bank holding company if after such acquisition it would own or control, directly or indirectly, more than 5.0% of the voting shares of such bank or bank holding company. In approving bank holding company acquisitions by bank holding companies, the Federal Reserve is required to consider, among other things, the effect of the acquisition on competition, the financial condition, managerial resources and future prospects of the bank holding company and the banks concerned, the convenience and needs of the communities to be serve, including the record of performance under the Community Reinvestment Act of 1977, or CRA, the effectiveness of the applicant in combating money laundering activities and the extent to which the proposed acquisition would result in greater or more concentrated risks to the stability of the U.S. banking or financial system. Our ability to make future acquisitions will depend on our ability to obtain approval for such acquisitions from the Federal Reserve. The Federal Reserve could deny our application based on the above criteria or other considerations. For example, we could be required to sell banking centers as a condition to receiving regulatory approval, which condition may not be acceptable to us or, if acceptable to us, may reduce the benefit of a proposed acquisition.

Under the Riegle-Neal Interstate Banking and Branching Efficiency Act, or the Riegle-Neal Act, a bank holding company may acquire banks in states other than its home state, subject to any state requirement that the bank has been organized and operating for a minimum period of time, not to exceed five years, and to certain deposit market-share limitations. Bank holding companies must be well capitalized and well managed, not merely adequately capitalized and adequately managed, in order to acquire a bank located outside of the bank holding company's home state.

Control Acquisitions. Under the BHC Act, a company may not acquire "control" of a bank holding company or a bank without the prior approval of the Federal Reserve. The statute defines control as ownership or control of 25.0% or more of any class of voting securities, control of the election of a majority of the board of directors, or any other circumstances in which the Federal Reserve determines that a company directly or indirectly exercises a controlling

influence over the management or policies of the bank holding company or bank. The Federal Reserve regulations include a presumption that control does not exist only when a company owns or controls less than 5.0% of the outstanding shares of any class of voting securities. Companies that propose to acquire between 5.0% and 25.0% of any class of voting securities usually consult with the Federal Reserve in advance and often must make written commitments not to exercise control. As a matter of policy, the Federal Reserve has in a number of cases required a company to take certain actions to avoid control if it proposes to acquire 25.0% or more but less than 33.0% of the total equity of a bank or bank holding company through the acquisition of both voting and non-voting shares, even if the voting shares are less than 25.0% of a class. The Federal Reserve generally deems the acquisition of 33.0% or more of the total equity of a bank or bank holding company to represent control.

The BHC Act does not apply to acquisitions by individuals or certain trusts, but if an individual, trust, or company proposes to acquire control of a bank or bank holding company, the Change in Bank Control Act, or CIBC Act, requires prior notice to the bank's primary federal regulator or to the Federal Reserve in the case of a bank holding company. The CIBC Act uses the same definition of control as the BHC Act, but agency regulations under the CIBC Act presume in many cases that a change in control occurs when an individual, trust, or company acquires 10.0% or more of any class of voting securities. The notice is not required for a company required to file an application under the BHC Act for the same transaction.

The requirements of the BHC Act and the CIBC Act could limit our access to capital and could limit parties who could acquire shares of our common stock.

Regulatory Restrictions on Dividends; Source of Strength. We are regarded as a legal entity separate and distinct from CommunityBank of Texas. The principal source of our revenues is dividends received from the Bank. Federal law currently imposes limitations upon certain capital distributions by national banks, such as certain cash dividends, payments to repurchase or otherwise acquire its shares, payments to shareholders of another institution in a cash-out merger and other distributions charged against capital. The Federal Reserve and OCC regulate all capital distributions by the Bank directly or indirectly to the Company, including dividend payments. The Federal Reserve regulates capital dividends paid by the Company. The Federal Reserve has issued a policy statement that provides that a bank holding company should not pay dividends unless (1) its net income over the last four quarters (net of dividends paid) has been sufficient to fully fund the dividends, (2) the prospective rate of earnings retention appears to be consistent with the capital needs, asset quality and overall financial condition of the bank holding company and its subsidiaries and (3) the bank holding company will continue to meet minimum required capital adequacy ratios. Accordingly, we should not pay cash dividends that exceed our net income in any year or that can only be funded in ways that weaken our financial strength, including by borrowing money to pay dividends.

Under Federal Reserve policy, bank holding companies have historically been required to act as a source of financial and managerial strength to each of their banking subsidiaries, and the Dodd-Frank Act codified this policy as a statutory requirement. Under this requirement, we are expected to commit resources to support the Bank, including at times when we may not be in a financial position to provide such resources. Any capital loans by a bank holding company to any of its subsidiary banks are subordinate in right of payment to deposits and to certain other indebtedness of such subsidiary banks. As discussed above, a bank holding company, in certain circumstances, could be required to guarantee the capital restoration plan of an undercapitalized banking subsidiary. If the capital of the Bank were to become impaired, the Federal Reserve could assess us for the deficiency. If we failed to pay the assessment within three months, the Federal Reserve could order the sale of our stock in the Bank to cover the deficiency.

In the event of a bank holding company's bankruptcy under Chapter 11 of the U.S. Bankruptcy Code, the trustee will be deemed to have assumed and will be required to cure immediately any deficit under any commitment by the debtor holding company to any of the federal banking agencies to maintain the capital of an insured depository institution, and any claim for breach of such obligation will generally have priority over most other unsecured claims.

Scope of Permissible Activities. Under the BHC Act, we may engage or acquire a company engaged solely in certain types of activities. Permissible activities include banking, managing or controlling banks or furnishing services to or performing services for the Bank, and certain activities found by the Federal Reserve to be so closely related to banking or managing and controlling banks as to be a proper incident thereto. These activities include, among others, operating a mortgage, finance, credit card or factoring company; performing certain data processing operations; providing investment and financial advice; acting as an insurance agent for certain types of credit-related insurance; leasing personal property on a full-payout, nonoperating basis; and providing certain stock brokerage and investment advisory services. The BHC

Act also permits certain other specific activities. To engage in such activities, we would in many cases be required to obtain the prior approval of the Federal Reserve. In its review of applications, the Federal Reserve considers, among other things, whether the acquisition or the additional activities can reasonably be expected to produce benefits to the public, such as greater convenience, increased competition, or gains in efficiency, that outweigh such possible adverse effects as undue concentration of resources, decreased or unfair competition, conflicts of interest or unsound banking practices.

The Gramm-Leach-Bliley Act, also known as the Financial Services Modernization Act of 1999, effective March 11, 2000, or the GLB Act, amended the BHC Act to expand the scope of activities available to a bank holding company. The amendments allow a qualifying bank holding company to elect "financial holding company" status. A financial holding company may affiliate with securities firms and insurance companies and engage in other activities that are "financial in nature." Such activities include, among other things, securities underwriting, dealing and market making; sponsoring mutual funds and investment companies; insurance underwriting and agency; merchant banking activities; and activities that the Federal Reserve has determined to be closely related to banking. No regulatory approval is required for a financial holding company to acquire a company, other than a bank or savings association, engaged in activities that are financial in nature or incidental to activities that are financial in nature, as determined by the Federal Reserve. We qualify for financial holding company status, but we have not made such an election. We would make such an election in the future if we plan to engage in any lines of business that are impermissible for bank holding companies but permissible for financial holding companies.

Safety and Soundness. Bank holding companies are not permitted to engage in unsafe or unsound practices. The Federal Reserve's Regulation Y, for example, generally requires a bank holding company to provide the Federal Reserve with prior notice of any redemption or repurchase of its own equity securities, if the consideration to be paid, together with the consideration paid for any repurchases or redemptions in the preceding year, is equal to 10.0% or more of the bank holding company's consolidated net worth. The Federal Reserve may oppose the transaction if it believes that the transaction would constitute an unsafe or unsound practice or would violate any law or regulation. In certain circumstances, the Federal Reserve could take the position that paying a dividend would constitute an unsafe or unsound practice.

The Federal Reserve has broad authority to prohibit activities of bank holding companies and their nonbanking subsidiaries which represent unsafe and unsound practices, result in breaches of fiduciary duty or which constitute violations of laws or regulations, and to assess civil money penalties or impose enforcement action for such activities. The penalties can be as high as \$1.0 million for each day the activity continues.

Anti-tying Restrictions. Bank holding companies and their affiliates are prohibited from tying the provision of certain services, such as extensions of credit, to other nonbanking services offered by a bank holding company or its affiliates.

CommunityBank of Texas, N.A.

The Bank is subject to various requirements and restrictions under the laws of the U.S. and to regulation, supervision and examination by the OCC. The Bank is also an insured depository institution and, therefore, subject to regulation by the FDIC, although the OCC is the Bank's primary federal regulator. The OCC and the FDIC have the power to enforce compliance with applicable banking statutes and regulations. Such requirements and restrictions include requirements to maintain reserves against deposits, restrictions on the nature and amount of loans that may be made and the interest that may be charged thereon and restrictions relating to investments and other activities of the Bank.

Capital Adequacy Requirements. Under the Basel III Capital Rules, discussed above, the OCC monitors the capital adequacy of the Bank by using a combination of risk-based guidelines and leverage ratios. The OCC considers the Bank's capital levels when acting on various types of applications and when conducting supervisory activities related to the safety and soundness of the Bank and the banking system. Higher capital levels may be required if warranted by the circumstances or risk profiles of individual institutions, or if required by the banking regulators due to the economic conditions impacting our markets. For example, OCC regulations provide that higher capital may be required to take adequate account of, among other things, interest rate risk and the risks posed by concentrations of credit, nontraditional activities or securities trading activities.

Corrective Measures for Capital Deficiencies. The federal banking regulators are required by the Federal Deposit Insurance Act, or FDI Act, to take "prompt corrective action" with respect to capital-deficient institutions that are FDIC-insured. Agency regulations define, for each capital category, the levels at which institutions are "well capitalized,"

"adequately capitalized," "undercapitalized," "significantly undercapitalized" and "critically undercapitalized." Under the current capital rules, which became effective on January 1, 2015, a well capitalized bank has a total risk-based capital ratio of 10.0% or higher, a Tier 1 risk-based capital ratio of 8.0% or higher, a leverage ratio of 5.0% or higher, a CET1 capital ratio of 6.5% or higher and is not subject to any written agreement, order or directive requiring it to maintain a specific capital level for any capital measure. An adequately capitalized bank has a total risk-based capital ratio of 8.0% or higher, a Tier 1 risk-based capital ratio of 6.0% or higher, a leverage ratio of 4.0% or higher, a CET1 capital ratio of 4.5% or higher and does not meet the criteria for a well capitalized bank. A bank is undercapitalized if it fails to meet any one of the ratios required to be adequately capitalized.

In addition to requiring undercapitalized institutions to submit a capital restoration plan, agency regulations contain broad restrictions on certain activities of undercapitalized institutions including asset growth, acquisitions, branch establishment and expansion into new lines of business. With certain exceptions, an insured depository institution is prohibited from making capital distributions, including dividends, and is prohibited from paying management fees to control persons if the institution would be undercapitalized after any such distribution or payment.

As a national bank's capital decreases, the OCC is statutorily required to take increasingly severe actions against the bank. If a national bank is significantly undercapitalized, the OCC must, among other actions, require the bank to engage in capital raising activities, restrict interest rates paid by the bank, restrict the bank's activities or asset growth, require the bank to dismiss certain directors and senior executive officers, restrict the bank's transactions with its affiliates, or require the bank to divest itself of or liquidate certain subsidiaries. The OCC has very limited discretion in dealing with a critically undercapitalized national bank and is virtually required to appoint a receiver or conservator.

Banks with risk-based capital and leverage ratios below the required minimums may also be subject to certain administrative actions, including the termination of deposit insurance upon notice and hearing, or a temporary suspension of insurance without a hearing in the event the institution has no tangible capital.

Standards for Safety and Soundness. Federal law requires each federal banking agency to prescribe certain standards for all insured depository institutions. These standards relate to, among other things, internal controls, information systems and audit systems, loan documentation, credit underwriting, interest rate risk exposure, asset growth, compensation and other operational and managerial standards as the agency deems appropriate. Interagency guidelines set forth the safety and soundness standards that the federal banking agencies use to identify and address problems at insured depository institutions before capital becomes impaired. If the appropriate federal banking agency determines that an institution fails to meet any standard prescribed by the guidelines, the agency may require the institution to submit to the agency an acceptable plan to achieve compliance with the standard. Failure to implement such a plan can result in further enforcement action, including the issuance of a cease and desist order or the imposition of civil money penalties.

Branching. National banks are required by the National Bank Act to adhere to branching laws applicable to state banks in the states in which they are located. Under the Dodd-Frank Act, *de novo* interstate branching by national banks is permitted if, under the laws of the state where the branch is to be located, a state bank chartered in that state would have been permitted to establish a branch. Under current Texas law, state banks are permitted to establish branch offices throughout Texas with prior regulatory approval. In addition, with prior regulatory approval, state banks are permitted to acquire branches of existing banks located in Texas. State banks located in Texas may also branch across state lines by merging with banks or by purchasing a branch of another bank in other states if allowed by the applicable states' laws.

Restrictions on Transactions with Affiliates and Insiders. Transactions between the Bank and its nonbanking subsidiaries and/or affiliates, including the Company, are subject to Section 23A and 23B of the Federal Reserve Act and Regulation W promulgated under such Sections. In general, Section 23A of the Federal Reserve Act imposes limits on the amount of such transactions and requires certain levels of collateral for loans to affiliated parties. It also limits the amount of advances to third-parties which are collateralized by the securities or obligations of the Company or its subsidiaries. Covered transactions with any single affiliate may not exceed 10.0% of the capital stock and surplus of the Bank, and covered transactions with all affiliates may not exceed, in the aggregate, 20.0% of the Bank's capital and surplus. For a bank, capital stock and surplus refer to the bank's Tier 1 and Tier 2 capital, as calculated under the risk-based capital guidelines, plus the balance of the allowance for credit losses excluded from Tier 2 capital. The Bank's transactions with all of its affiliates in the aggregate are limited to 20.0% of the foregoing capital. "Covered transactions" are defined by statute to include a loan or extension of credit to an affiliate, as well as a purchase of securities issued by an affiliate, a purchase of assets (unless otherwise exempted by the Federal Reserve) from the affiliate, the acceptance of securities issued by the affiliate as collateral for a loan and the issuance of a guarantee, acceptance or letter of credit on behalf of an

affiliate. In addition, in connection with covered transactions that are extensions of credit, the Bank may be required to hold collateral to provide added security to the Bank, and the types of permissible collateral may be limited. The Dodd-Frank Act generally enhances the restrictions on transactions with affiliates, including an expansion of what types of transactions are covered transactions to include credit exposures related to derivatives, repurchase agreement and securities lending arrangements and an increase in the amount of time for which collateral requirements regarding covered transactions must be satisfied. Affiliate transactions are also subject to Section 23B of the Federal Reserve Act which generally requires that certain transactions between the Bank and its affiliates be on terms substantially the same, or at least as favorable to the Bank, as those prevailing at the time for comparable transactions with or involving other nonaffiliated persons.

The restrictions on loans to directors, executive officers, principal shareholders and their related interests (collectively referred to herein as "insiders") contained in Section 22(h) of the Federal Reserve Act and in Regulation O promulgated by the Federal Reserve apply to all insured institutions and their subsidiaries and bank holding companies. These restrictions include limits on loans to one borrower and conditions that must be met before such a loan can be made. There is also an aggregate limitation on all loans to insiders and their related interests. Generally, the aggregate of these loans cannot exceed the institution's total unimpaired capital and surplus, although a bank's regulators may determine that a more stringent limit is appropriate. Loans to senior executive officers of a bank are even further restricted. Insiders are subject to monetary penalties for knowingly accepting loans in violation of applicable restrictions.

Restrictions on Distribution of Bank Dividends and Assets. Dividends paid by the Bank have provided a substantial part of our operating funds and for the foreseeable future it is anticipated that dividends paid by the Bank to us will continue to be our principal source of operating funds. Earnings and capital adequacy requirements serve to limit the amount of dividends that may be paid by the Bank. In general terms, federal law provides that the Bank's Board of Directors may, from time to time and as it deems expedient, declare a dividend out of its net profits. Generally, the total of all dividends declared in a year shall not, unless approved by the OCC, exceed the net profits of that year combined with its net profits of the past two years.

In addition, under the Federal Deposit Insurance Corporation Improvement Act of 1991, or FDICIA, the Bank may not pay any dividend if it is undercapitalized or the payment of the dividend would cause it to become undercapitalized. The OCC may further restrict the payment of dividends by requiring that the Bank maintain a higher level of capital than otherwise required for it to be adequately capitalized for regulatory purposes. Moreover, if, in the opinion of the OCC, the Bank is engaged in an unsound practice (which could include the payment of dividends), it may require, generally after notice and hearing, that the Bank cease such practice. The OCC has indicated that paying dividends that deplete a depository institution's capital base to an inadequate level would be an unsafe banking practice. The OCC has also issued policy statements providing that insured depository institutions generally should pay dividends only out of current operating earnings.

Depositor Preference. In the event of the "liquidation or other resolution" of an insured depository institution, the claims of depositors of the institution, including the claims of the FDIC as subrogee of insured depositors, and certain claims for administrative expenses of the FDIC as a receiver, will have priority over other general unsecured claims against the institution. If an insured depository institution fails, insured and uninsured depositors, along with the FDIC, will have priority in payment ahead of unsecured, non-deposit creditors, including the parent bank holding company, with respect to any extensions of credit they have made to such insured depository institution.

Incentive Compensation Guidance. The federal banking agencies have issued comprehensive guidance on incentive compensation policies intended to help ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of those organizations by encouraging excessive risk-taking. The incentive compensation guidance sets expectations for banking organizations concerning their incentive compensation arrangements and related risk management, control and governance processes. The incentive compensation guidance, which covers all employees that can materially affect the risk profile of an organization, either individually or as part of a group, is based upon three primary principles: (1) balanced risk-taking incentives, (2) compatibility with effective controls and risk management and (3) strong corporate governance. Any deficiencies in compensation practices that are identified may be incorporated into the organization's supervisory ratings, which can affect its ability to make acquisitions or take other actions. In addition, under the incentive compensation guidance, a banking organization's federal supervisor may initiate enforcement action if the organization's incentive compensation arrangements pose a risk to the safety and soundness of the organization. Further, a provision of the Basel III capital standards described above would limit discretionary bonus payments to bank executives if the institution's regulatory capital ratios fail to exceed certain thresholds. A number of

federal regulatory agencies proposed rules that would require enhanced disclosure of incentive-based compensation arrangements initially in April 2011 and again in April and May 2016. The scope and content of the U.S. banking regulators' policies on executive compensation are continuing to develop and are likely to continue evolving in the near future.

Audits. For insured institutions with total assets of \$500 million or more, financial statements prepared in accordance with accounting principles generally accepted in the U.S., or GAAP, as well as management's certifications signed by our and the Bank's chief executive officer and chief accounting or financial officer concerning management's responsibility for the financial statements, must be submitted to the FDIC. If the insured institution has consolidated total assets of more than \$1.0 billion, it must additionally submit an attestation by the auditors regarding the institution's internal controls. Insured institutions with total assets of \$500 million or more must also have an audit committee consisting exclusively of outside directors (the majority of whom must be independent of management), and insured institutions with total assets of \$1.0 billion or more must have an audit committee that is entirely independent. The committees of institutions with total assets of more than \$3.0 billion must include members with experience in banking or financial management, must have access to outside counsel and must not include representatives of large customers. The Bank's audit committee consists entirely of independent directors and includes members with experience in banking or related financial management.

Deposit Insurance Assessments. The FDIC insures the deposits of federally insured banks up to prescribed statutory limits for each depositor through the Deposit Insurance Fund and safeguards the safety and soundness of the banking and thrift industries. The maximum amount of deposit insurance for banks and savings institutions is \$250,000 per depositor, per ownership category. The amount of FDIC assessments paid by each insured depository institution is based on its relative risk of default as measured by regulatory capital ratios and other supervisory factors and is calculated based on an institution's average consolidated total assets minus average tangible equity.

We are generally unable to control the amount of premiums that we are required to pay for FDIC insurance. At least semi-annually, the FDIC will update its loss and income projections for the Deposit Insurance Fund and, if needed, will increase or decrease assessment rates, following notice-and-comment rulemaking, if required. If there are additional bank or financial institution failures or if the FDIC otherwise determines to increase assessment rates, the Bank may be required to pay higher FDIC insurance premiums. Any future increases in FDIC insurance premiums may have a material and adverse effect on our earnings.

Financial Subsidiaries. Under the GLB Act, banks may establish financial subsidiaries and engage, subject to limitations on investment, in activities that are financial in nature, other than insurance underwriting as principal, insurance company portfolio investment, real estate development, real estate investment, annuity issuance and merchant banking activities. To do so, a bank must be well capitalized, well managed and have a CRA rating from its primary federal regulator of satisfactory or better. Banks with financial subsidiaries, as well as subsidiary banks of financial holding companies, must remain well capitalized and well managed to continue to engage in activities that are financial in nature without regulatory actions or restrictions. Such actions or restrictions could include divestiture of the "financial in nature" subsidiary or subsidiaries.

Brokered Deposit Restrictions. Insured depository institutions that are categorized as adequately capitalized institutions under the FDI Act and corresponding federal regulations cannot accept, renew or roll over brokered deposits without receiving a waiver from the FDIC and are subject to restrictions on the interest rates that can be paid on any deposits. Insured depository institutions that are categorized as undercapitalized institutions under the FDI Act and corresponding federal regulations may not accept, renew or roll over brokered deposits. The Bank is not currently subject to such restrictions.

Concentrated Commercial Real Estate Lending Regulations. The federal banking regulatory agencies have promulgated guidance governing financial institutions with concentrations in commercial real estate lending. The guidance provides that a bank may be exposed to heightened commercial real estate lending concentration risk and subject to further supervisory analysis if (1) total reported loans for construction, land development and other land represent 100.0% or more of total capital or (2) total reported loans secured by multi-family residential properties and nonfarm nonresidential properties and loans for construction, land development and other land represent 300.0% or more of total capital and the bank's commercial real estate loan portfolio has increased by 50.0% or more during the prior 36 months. If a concentration is present, management is expected to employ heightened risk management practices that address, among other things, board and management oversight and strategic planning, portfolio management, development of underwriting standards,

risk assessment and monitoring through market analysis and stress testing and maintenance of increased capital levels as needed to support the level of commercial real estate lending.

Community Reinvestment Act. The CRA and the regulations issued thereunder are intended to encourage banks to help meet the credit needs of their entire assessment area, including low and moderate income neighborhoods, consistent with the safe and sound operations of such banks. These regulations also provide for regulatory assessment of a bank's record in meeting the needs of its assessment area when considering applications to establish branches, merger applications and applications to acquire the assets and assume the liabilities of another bank. The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 requires federal banking agencies to make public a rating of a bank's performance under the CRA. In the case of a bank holding company, the CRA performance record of the banks involved in the transaction are reviewed in connection with the filing of an application to acquire ownership or control of shares or assets of a bank or to merge with any other bank holding company. An unsatisfactory CRA record could substantially delay approval or result in denial of an application. The Bank received a "satisfactory" rating in its most recent CRA examination.

Consumer Laws and Regulations. The Bank is subject to numerous federal laws and regulations intended to protect consumers in transactions with the Bank, including but not limited to the Electronic Fund Transfer Act, the Equal Credit Opportunity Act, the Fair Credit Reporting Act, the Fair Debt Collection Practices Act, the Real Estate Procedures Act of 1974, the S.A.F.E. Mortgage Licensing Act of 2008, the Truth in Lending Act, the Truth in Savings Act and laws prohibiting unfair, deceptive or abusive acts and practices in connection with consumer financial products and services. Many states and local jurisdictions have consumer protection laws analogous, and in addition, to those enacted under federal law. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must deal with customers when taking deposits, making loans and conducting other types of transactions. Failure to comply with these laws and regulations could give rise to regulatory sanctions, customer rescission and registration rights, action by state and local attorneys general and civil or criminal liability.

The authority to supervise and examine depository institutions with \$10.0 billion or less in assets for compliance with federal consumer laws remains largely with those institutions' primary regulators (the OCC, in the case of the Bank). However, the CFPB may participate in examinations of these smaller institutions on a "sampling basis" and may refer potential enforcement actions against such institutions to their primary regulators. Accordingly, the CFPB may participate in examinations of the Bank, which currently has assets of less than \$10.0 billion, and could supervise and examine our other direct or indirect subsidiaries that offer consumer financial products or services.

Mortgage Lending Rules. CFPB regulations that require lenders to determine whether a consumer has the ability to repay a mortgage loan became effective on January 10, 2014. These regulations established certain minimum requirements for creditors when making ability-to-repay determinations and provide certain safe harbors from liability for mortgages that are "qualified mortgages" and are not "higher-priced." Generally, these CFPB regulations apply to all consumer, closed-end loans secured by a dwelling, including home-purchase loans, refinancing and home equity loans (whether first or subordinate lien). Qualified mortgages must generally satisfy detailed requirements related to product features, underwriting standards, and requirements where the total points and fees on a mortgage loan cannot exceed specified amounts or percentages of the total loan amount. Qualified mortgages must: (1) have a term not exceeding 30 years; (2) provide for regular periodic payments that do not result in negative amortization, deferral of principal repayment, or a balloon payment; (3) and be supported with documentation of the borrower and his or her credit worthiness.

The Regulatory Relief Act included a provision that provides for certain residential mortgages held in portfolio by banks with less than \$10.0 billion in consolidated assets to automatically be deemed "qualified mortgages." This relieves such institutions from many of the requirements to satisfy the criteria listed above for "qualified mortgages." Mortgages meeting the "qualified mortgage" safe harbor may not have negative amortization, must follow prepayment penalty limitations included in the Truth in Lending Act, and may not have fees greater than three percent of the total value of the loan.

Anti-Money Laundering and Office of Foreign Assets Control. A major focus of governmental policy on banks and other financial institutions in recent years has been combating money laundering and terrorist financing. The Bank Secrecy Act, or BSA, the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, or the USA PATRIOT Act, and other federal laws impose significant obligations on certain financial institutions, including the Bank, to detect and deter money laundering and terrorist financing. The principal obligations of an insured depository institution include, among other things, the need to: (i) establish an antimoney laundering program that includes training and audit components; (ii) designate a BSA officer; (iii) establish a

"know your customer" program involving due diligence to confirm the identity of persons seeking to open accounts and to deny accounts to those persons unable to demonstrate their identities; (iv) identify and verify the identity of beneficial owners of legal entity customers, subject to certain exclusions and exemptions; (v) take additional precautions with respect to customers that pose heightened risk; (vi) monitor, investigate and report suspicious transactions or activity; (vii) file currency transaction reports for deposits and withdrawals of large amounts of cash; (viii) verify and certify money laundering risk with respect to private banking and foreign correspondent banking relationships; (ix) maintain records for certain minimum periods of time; and (x) respond to requests for information by law enforcement. The Financial Crimes Enforcement Network, or FinCEN, and the federal banking regulators have imposed significant civil money penalties against banks found to be violating these obligations.

The Office of Foreign Assets Control, or OFAC, administers laws and Executive Orders that prohibit U.S. entities from engaging in transactions with certain prohibited parties. OFAC publishes lists of persons and organizations suspected of aiding, harboring or engaging in terrorist acts, known as Specially Designated Nationals and Blocked Persons. Generally, if a bank identifies a transaction, account or wire transfer relating to a person or entity on an OFAC list, it must freeze the account or block the transaction, file a suspicious activity report and notify the appropriate authorities.

Bank regulators routinely examine institutions for compliance with these obligations and they must consider an institution's compliance in connection with the regulatory review of applications, including applications for bank mergers and acquisitions. In addition, other government agencies have the authority to conduct investigations of an institution's compliance with these obligations. Failure of a financial institution to maintain and implement adequate programs to combat money laundering and terrorist financing and comply with OFAC sanctions, or to comply with relevant laws and regulations, could have serious legal, reputational and financial consequences for the institution.

Privacy. The federal banking regulators have adopted rules that limit the ability of banks and other financial institutions to disclose non-public information about consumers to non-affiliated third-parties. These limitations require disclosure of privacy policies to consumers and, in some circumstances, allow consumers to prevent disclosure of certain personal information to a non-affiliated third-party. These regulations affect how consumer information is transmitted through financial services companies and conveyed to outside vendors. In addition, consumers may also prevent disclosure of certain information among affiliated companies that is assembled or used to determine eligibility for a product or service, such as that shown on consumer credit reports and asset and income information from applications. Consumers also have the option to direct banks and other financial institutions not to share information about transactions and experiences with affiliated companies for the purpose of marketing products or services. In addition to applicable federal privacy regulations, the Bank is subject to certain state privacy laws.

Federal Home Loan Bank System. The Federal Home Loan Bank System, of which the Bank is a member, is composed of 11 regional Federal Home Loan Banks, or FHLBs, more than 7,300 member financial institutions, and a fiscal agent. The FHLBs provide long- and short-term advances (i.e., loans) to member institutions within their assigned regions in accordance with policies and procedures established by the boards of directors of each regional FHLB. Such advances are primarily collateralized by residential mortgage loans, as well as government and agency securities, and are priced at a small spread over comparable U.S. Department of the Treasury obligations.

As a member of the Dallas FHLB, the Bank is entitled to borrow from the Dallas FHLB, provided it posts acceptable collateral. The Bank is also required to own a certain amount of capital stock in the Dallas FHLB. The Bank is in compliance with the stock ownership rules with respect to such advances, commitments and letters of credit and collateral requirements with respect to home mortgage loans and similar obligations. All loans, advances and other extensions of credit made by the Dallas FHLB to the Bank are secured by a portion of the respective mortgage loan portfolio, certain other investments and the capital stock of the Dallas FHLB held by the Bank.

Enforcement Powers. The federal banking agencies, including our primary federal regulator, the OCC, have broad enforcement powers, including the power to terminate deposit insurance, impose substantial fines and other civil and criminal penalties and appoint a conservator or receiver. Failure to comply with applicable laws, regulations and supervisory agreements, breaches of fiduciary duty or the maintenance of unsafe and unsound conditions or practices could subject the Company or the Bank and their subsidiaries, as well as their respective officers, directors and other institution-affiliated parties, to administrative sanctions and potentially substantial civil money penalties. For example, the regulatory authorities may appoint the FDIC as conservator or receiver for a banking institution (or the FDIC may appoint itself, under certain circumstances) if any one or more of a number of circumstances exist, including, without limitation, the fact that the banking institution is undercapitalized and has no reasonable prospect of becoming adequately capitalized,

fails to become adequately capitalized when required to do so, fails to submit a timely and acceptable capital restoration plan or materially fails to implement an accepted capital restoration plan.

Effect of Governmental Monetary Policies

The commercial banking business is affected not only by general economic conditions but also by U.S. fiscal policy and the monetary policies of the Federal Reserve. Some of the instruments of monetary policy available to the Federal Reserve include changes in the discount rate on member bank borrowings, the fluctuating availability of borrowings at the "discount window," open market operations, the imposition of and changes in reserve requirements against member banks' deposits and certain borrowings by banks and their affiliates and assets of foreign branches. These policies influence, to a significant extent, the overall growth of bank loans, investments, deposits and the interest rates charged on loans or paid on deposits. We cannot predict the nature of future fiscal and monetary policies or the effect of these policies on our operations and activities, financial condition, results of operations, growth plans or future prospects.

Impact of Current Laws and Regulations

The cumulative effect of these laws and regulations, while providing certain benefits, adds significantly to the cost of our operations and thus may have a negative impact on our profitability. There has also been a notable expansion in recent years of financial service providers that are not subject to the examination, oversight and other rules and regulations to which we are subject. Those providers, because they are not so highly regulated, may have a competitive advantage over us and may continue to draw large amounts of funds away from traditional banking institutions, with a continuing adverse effect on the banking industry in general.

Implications of Being an Emerging Growth Company

As a company with less than \$1.07 billion in total annual gross revenues during our last fiscal year and satisfying other applicable standards, we qualify as an "emerging growth company" under the Jumpstart Our Business Startups Act of 2012, or the JOBS Act. An emerging growth company may take advantage of reduced reporting and other requirements that are otherwise generally applicable to public companies. As an emerging growth company:

- we may present less than five years of selected historical financial data;
- we are exempt from the requirement to obtain an attestation and report from our auditors on management's assessment of our internal control over financial reporting under the Sarbanes-Oxley Act of 2002;
- we are permitted to have an extended transition period for adopting any new or revised accounting standards that may be issued by the Financial Accounting Standards Board, or FASB, or by the SEC;
- we are permitted to provide less extensive disclosure about our executive compensation arrangements; and
- we are not required to give our shareholders nonbinding advisory votes on executive compensation or golden parachute arrangements.

We have elected to take advantage of the scaled disclosures and other relief described above in this Annual Report on Form 10-K, and we may take advantage of these exemptions until December 31, 2022 or such earlier time that we are no longer an "emerging growth company." In general, we would cease to be an "emerging growth company" if we have \$1.07 billion or more in annual revenues, we have more than \$700 million in market value of our common stock held by non-affiliates on any June 30 more than one year after our initial public offering, or we issue more than \$1.0 billion of non-convertible debt over a three-year period. As a result, we could cease to be an "emerging growth company" as soon as the end of the 2020 fiscal year. For so long as we may choose to take advantage of some or all of these reduced burdens, the level of information that we provide shareholders may be different than you might get from other public companies in which you hold stock. In addition, when these exemptions cease to apply, we expect to incur additional expenses and devote increased management effort toward ensuring compliance with them, which we may not be able to predict or estimate.

Future Legislation and Regulatory Reform

In recent years, regulators have increased their focus on the regulation of financial institutions. From time to time, various legislative and regulatory initiatives are introduced in Congress and state legislatures. New regulations and statutes are regularly proposed that contain wide-ranging proposals for altering the structures, regulations and competitive

relationships of financial institutions operating in the U.S. We cannot predict whether or in what form any proposed regulation or statute will be adopted or the extent to which our business may be affected by any new regulation or statute. Future legislation, regulation and policies and the effects of such legislation, regulation and policies, may have a significant influence on our operations and activities, financial condition, results of operations, growth plans or future prospects and the overall growth and distribution of loans, investments and deposits. Such legislation, regulation and policies have had a significant effect on the operations and activities, financial condition, results of operations, growth plans and future prospects of commercial banks in the past and are expected to continue to do so.

Item 1A. Risk Factors

Our business involves significant risks, some of which are described below. You should carefully consider the risks and uncertainties described below, together with all the other information in this Annual Report on Form 10-K including "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and the related notes. If any of the following risks occur, our business, reputation, financial condition, results of operations, revenue and future prospects could be seriously harmed. As a result, the trading price of our common stock could decline, and you could lose all or part of your investment. Some statements in this Annual Report on Form 10-K, including statements in the following risk factors section, constitute forward-looking statements. Please refer to "Cautionary Note Regarding Forward-Looking Statements" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7 of this Annual Report on Form 10-K.

Risks Related to Our Business

We may not be able to adequately measure and limit our credit risk, which could lead to unexpected losses.

The business of lending is inherently risky, including risks that the principal of or interest on any loan will not be repaid timely or at all or that the value of any collateral supporting the loan will be insufficient to cover our outstanding exposure. These risks may be affected by the strength of the borrower's business sector and local, regional and national market and economic conditions. Our risk management practices, such as monitoring the concentration of our loans within specific industries and our credit approval practices, may not adequately reduce credit risk and our credit administration personnel, policies and procedures may not adequately adapt to changes in economic or any other conditions affecting customers and the quality of our loan portfolio. Failure to effectively measure and limit the credit risk associated with our loan portfolio could lead to unexpected losses and have a material adverse impact on our business, financial condition and results of operations.

We are subject to interest rate risk and fluctuations in interest rates may adversely impact our earnings.

Changes in interest rates could have an adverse impact on our net interest income and on our business, financial condition and results of operations. Many factors outside our control impact interest rates, including governmental monetary policies and macroeconomic conditions. A majority of our banking assets and liabilities are monetary in nature and subject to risk from changes in interest rates. Like most financial institutions, our earnings are significantly dependent on our net interest income and are subject to "gaps" in the interest rate sensitivities of our assets and liabilities that may negatively impact our earnings. Interest rate increases often result in larger payment requirements for our borrowers, which increase the potential for default and delayed payment, and reduces demand for collateral securing the loan. Further, loans in nonaccrual status require continued funding costs, but result in decreased interest income. Interest rate increases may also reduce the demand for loans and increase competition for deposits. Declining interest rates can increase loan prepayments and long-term fixed rate credits, which could adversely impact our earnings and net interest margin if rates increase. If short-term interest rates remain at low levels for a prolonged period and longer-term interest rates fall, we could experience net interest margin compression as our interest-earning assets would continue to reprice downward while our interest-bearing liability rates could fail to decline in tandem. Changes in interest rates can also impact the value of loans, securities and other assets.

Our business is concentrated in and largely dependent upon the continued growth and welfare of our markets and on the banking industry in general.

Our business is concentrated in the Houston and Beaumont, Texas markets and we recently entered the Dallas, Texas market. Our success depends, to a significant extent, upon the economic activity and conditions in our markets. Economic conditions within our markets are influenced by the energy sector generally and the price of oil and gas in

particular. Adverse economic conditions that impact our markets could reduce our growth rate, the ability of our customers to repay their loans, the value of collateral underlying our loans, our ability to attract deposits and generally impact our business, financial condition, results of operations and future prospects. Due to our geographic concentration, we may be less able than other larger regional or national financial institutions to diversify our credit risks.

National market conditions and economic trends, such as volatility in the real estate market in some parts of the country, uncertain regulatory and changing interest rate conditions could adversely impact our business, financial condition and results of operations. A national economic downturn or deterioration of conditions in our market could adversely impact our borrowers and cause losses beyond those that are provided for in our allowance for credit losses due to increases in loan delinquencies, nonperforming assets and foreclosures and decreases in demand for our products and services, which could adversely impact our liquidity position and decrease the value of the collateral.

Our allowance for loan losses may prove to be insufficient to absorb potential losses in our loan portfolio.

We maintain an allowance for loan losses that represents management's judgment of probable losses and risks inherent in our loan portfolio. The determination of the appropriate level of the allowance for loan losses is inherently highly subjective and requires us to make significant estimates of and assumptions regarding current credit risks and future trends, all of which may undergo material changes. Inaccurate management assumptions, deterioration of economic conditions affecting borrowers, new information regarding existing loans, identification or deterioration of additional problem loans, acquisition of problem loans and other factors, both within and outside of our control, may require us to increase our allowance for loan losses.

In addition, our regulators, as an integral part of their periodic examinations, review our methodology for calculating and the adequacy of our allowance for loan losses and may direct us to make additions to the allowance based on their judgments about information available to them at the time of their examination. Further, if actual charge-offs in future periods exceed the amounts allocated to the allowance for loan losses, we may need additional provisions for loan losses to restore the adequacy of our allowance for loan losses.

Finally, the measure of our allowance for loan losses is dependent on the adoption and interpretation of accounting standards. The adoption of Accounting Standards Update ("ASU") 2016-13, Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments on January 1, 2020 will impact our methodology for estimating the allowance for loan losses. See "Item 8—Financial Statements and Supplementary Data—Note 1."

The amount of nonperforming and classified assets may increase significantly, resulting in additional losses and costs and expenses.

Our nonperforming assets include nonaccrual loans and assets acquired through foreclosure. Loans are placed on nonaccrual status when, in management's opinion, the borrower may be unable to meet payment obligations when they become due. The resolution of nonperforming assets requires significant commitments of time from management, which may materially and adversely impact their ability to perform their other responsibilities. While we seek to reduce problem assets through loan workouts, restructurings and otherwise, decreases in the value of the underlying collateral, or in these borrowers' performance or financial condition and any increase in the amount of nonperforming or classified assets could have a material impact on our business, financial condition and results of operations, including through increased capital requirements from regulators.

The small to medium-sized businesses that we lend to may have fewer resources to endure adverse business developments, which may impair our borrowers' ability to repay loans.

We focus our business development and marketing strategy primarily on small to medium-sized businesses. Small to medium-sized businesses frequently have smaller market shares than their competition, may be more vulnerable to economic downturns, often need substantial additional capital and may experience substantial volatility in operating results, any of which may impair a borrower's ability to repay a loan. In addition, the success of a small and medium-sized business often depends on the management skills, talents and efforts of a small group of people and the death, disability or resignation of one or more of these people could have an adverse impact on the business and its ability to repay its loan. If our borrowers are unable to repay their loans, our business, financial condition and results of operations could be adversely affected.

We could be adversely impacted by sustained low oil prices, volatility in oil prices and downturns in the energy industry.

The economy in Texas is dependent on the energy industry. Sustained low oil prices or the failure of oil prices to rise in the future and the resulting downturns or lack of growth in the energy industry and energy-related business, could have a negative impact on the Texas economy and adversely impact our results of operations and financial condition. Prolonged or heightened pricing pressure on oil and gas could lead to increased credit stress in our energy portfolio, increased losses associated with that portfolio and weaker demand for energy lending. More significantly for us, sustained low oil prices or general uncertainty resulting from energy price volatility could have other adverse impacts such as job losses in industries tied to energy, lower spending habits, lower borrowing needs and a number of other potential impacts that are difficult to isolate or quantify.

We are subject to risk arising from conditions impacting the real estate market and related appraisals and other valuation techniques to evaluate and monitor these loans.

As of December 31, 2019, \$2.0 billion, or 75.0%, of our gross loans were loans with real estate as a primary or secondary component of collateral. Real estate values in many Texas markets have experienced periods of fluctuation and can fluctuate significantly in a short period. Adverse developments affecting real estate values and the liquidity of real estate in our markets or in Texas generally, could increase the credit risk associated with our loan portfolio, result in losses that adversely affect credit quality and cause us to increase our allowance for loan losses. Negative changes in the economy affecting real estate values and liquidity in our market areas could significantly impair the value of property pledged as collateral on loans and affect our ability to sell the collateral upon foreclosure without a loss or additional losses. In addition, adverse weather events, including hurricanes and flooding, could damage the property pledged as collateral, which could also result in additional losses upon foreclosure. Collateral may have to be sold for less than the outstanding balance of the loan, which could result in losses on such loans. Any declines in real estate values that are used as collateral for loans, decreased liquidity and increased losses on foreclosure could have a material adverse impact on our business, financial condition and results of operations.

In considering whether to make a loan secured by real property, we generally require an appraisal of the property. However, an appraisal is only an estimate of the value of the property at the time of appraisal and real estate values may change significantly in relatively short periods of time. These estimates may not accurately describe the value of the real property collateral and we may not be able to realize the full amount of any remaining indebtedness when we foreclose on and sell the relevant property.

We are subject to risk from foreclosure of real estate assets.

If we foreclose on a loan with real estate assets as collateral, we would own the underlying real estate, subjecting us to the costs and potential risks associated with the ownership. The amount that we may realize after a default is dependent upon factors outside of our control, including, but not limited to general or local economic conditions, environmental cleanup liability, assessments, real estate tax rates, operating expenses of the mortgaged properties, ability to obtain and maintain adequate occupancy of the properties, zoning laws, governmental and regulatory rules and natural disasters.

Additionally, consumer protection initiatives or changes in state or federal law may substantially increase the time and expense associated with the foreclosure process or prevent us from foreclosing at all. While historically Texas has had foreclosure laws that are favorable to lenders, a number of states in recent years have either considered or adopted foreclosure reform laws that make it substantially more difficult and expensive for lenders to foreclose on properties in default and we cannot be certain that Texas will not adopt similar legislation in the future. Additionally, federal regulators have prosecuted a number of mortgage servicing companies for alleged consumer law violations.

Commercial real estate and real estate construction and development loan portfolio have credit risks that may be greater than the risks related to other types of loans.

As of December 31, 2019, \$1.2 billion, or 44.5%, of our gross loans were nonresidential real estate loans (including owner-occupied commercial real estate loans) and \$527.8 million, or 19.9%, of our total loans were construction and development loans. These loans typically involve repayment dependent upon income generated, or expected to be generated, by the property securing the loan in amounts sufficient to cover operating expenses and debt service. The availability of such income for repayment may be adversely affected by changes in the economy or local market conditions.

Owner-occupied commercial real estate is generally less dependent upon income generated directly from the property but still carries risks from the successful operation of the underlying business or adverse economic conditions. These loans expose a lender to greater credit risk than loans secured by other types of collateral because the collateral securing these loans is typically more difficult to liquidate due to the fluctuation of real estate values. Additionally, non-owner-occupied commercial real estate loans generally involve relatively large balances to single borrowers or related groups of borrowers. Unexpected deterioration in the credit quality of our non-owner-occupied commercial real estate loan portfolio could require us to increase our allowance for loan losses.

Construction and development loans also involve risks because loan funds are secured by a project under construction and the project is of uncertain value prior to its completion. It can be difficult to accurately evaluate the total funds required to complete a project and construction and development lending often involves the disbursement of substantial funds with repayment dependent, in part, on the success of the ultimate project rather than the ability of a borrower or guarantor to repay the loan. If we are forced to foreclose on a project prior to completion, we may be unable to recover the entire unpaid portion of the loan. In addition, we may be required to fund additional amounts to complete a project, incur taxes, maintenance and compliance costs for a foreclosed property and may have to hold the property for an indeterminate period.

We could be adversely impacted by loans collateralized by general business assets.

As of December 31, 2019, commercial and industrial loans were \$527.6 million, or 19.9%, of our gross loans. Commercial and industrial loans are generally collateralized by general business assets, including, among other things, accounts receivable, inventory and equipment and most are backed by a personal guaranty of the borrower or principal. Commercial and industrial loans are typically larger in amount than loans to individuals and, therefore, have the potential for larger losses on a single loan basis and repayment is subject to the ongoing business operations risks of the borrower. The collateral securing such loans generally includes moveable property such as equipment and inventory, which may decline in value more rapidly than we anticipate, thus exposing us to increased credit risk.

Delinquencies, defaults and foreclosures in residential mortgages create a higher risk of repurchases and indemnity requests.

We originate residential mortgage loans for sale to correspondent banks who may resell such mortgages to government-sponsored enterprises, such as Fannie Mae, Freddie Mac and other investors. As a part of this process, we make various representations and warranties to the purchasers that are tied to the underwriting standards under which the investors agreed to purchase the loan. If a representation or warranty proves to be untrue, we could be required to repurchase one or more of the mortgage loans or indemnify the investor. Repurchase and indemnity obligations tend to increase during weak economic times, as investors seek to pass on the risks associated with mortgage loan delinquencies to the originator of the mortgage. Although we did not repurchase any residential mortgage loans sold to correspondent banks in 2018 or 2019, if we are forced to repurchase mortgage loans in the future that we have previously sold to investors, or indemnify those investors, our business, financial condition and results of operations could be adversely impacted.

Our largest loan and deposit relationships currently make up significant percentages of our total loan portfolio and of our deposits, respectively.

As of December 31, 2019, our 15 largest loan relationships, including related entities, totaled \$334.4 million, or 12.6%, of the total loan portfolio. The concentration risk associated with having a small number of large loan relationships is that, if one or more of these relationships were to become delinquent or suffer default, we could be at serious risk of material losses. The allowance for loan losses may not be adequate to cover losses associated with any of these relationships and any loss or increase in the allowance would negatively impact our earnings and capital. Even if the loans are collateralized, a large increase in classified assets could harm our reputation with our regulators and inhibit our ability to execute our business plan.

As of December 31, 2019, our 15 largest depositors, including related entities, totaled \$394.2 million, or 13.8%, of our total deposits. Several of our large depositors have business, family, or other relationships with each other, which creates a risk that any one customer's withdrawal of their deposits could lead to a loss of other deposits from customers within the relationship. Withdrawals of deposits by any one of our largest depositors or by one of our related customer groups could force us to rely more heavily on borrowings and other sources of funding for our business and withdrawal demands, which may be more expensive and less stable.

We have made loans to and accepted deposits from related parties.

From time to time, we have made loans to and accepted deposits from certain of our directors and officers and the directors and officers of the Bank in compliance with applicable regulations and our written policies. Our business relationships with related parties are highly regulated. In particular, our ability to do business with related parties is limited with respect to, among other things, extensions of credit described in the Federal Reserve's Regulation O and covered transactions described in sections 23A and 23B of the Federal Reserve Act and the Federal Reserve's Regulation W. If we were to fail to comply with any of these regulations, we could be subject to enforcement and other legal actions by the Federal Reserve.

We could be adversely impacted by the unexpected loss of the services of our executive management team and other key employees.

Our success depends in large part on the performance of our executive management team and other key personnel, as well as on our ability to attract, motivate and retain highly qualified senior and middle management and other skilled employees. Competition for qualified employees is intense and the process of locating qualified key personnel may be lengthy and expensive. We may not be successful in retaining our key employees or finding adequate replacements for lost personnel.

Our growth strategy, which includes acquisitions and de novo branching, includes a number of risks.

We intend to pursue acquisition opportunities that we believe complement our activities and have the ability to enhance our profitability and provide attractive risk-adjusted returns. Our acquisition activities could be material to our business and involve a number of risks, including, but not limited to, the following:

- competition from other banking organizations and other acquirers;
- market pricing for desirable acquisitions resulting in lower than traditional returns;
- the time and expense associated with identifying, evaluating, and negotiating acquisitions, including diversion of management time from the operation of our existing business;
- using inaccurate estimates and judgments with respect to the health or value of acquisition targets;
- failure to achieve expected revenues, earnings, savings or synergies from an acquisition;
- unknown or contingent target liabilities, including compliance and regulatory issues;
- the time and expense required of integration of target customers and data;
- loss of key employees and customers;
- reputational issues if the target's management does not align with our culture and values;
- risks of impairment to goodwill; and
- regulatory delays.

Our business strategy includes evaluating strategic opportunities to grow through de novo branching which carries with it certain potential risks, including significant startup costs and anticipated initial operating losses; an inability to gain regulatory approval; an inability to secure the services of qualified senior management to operate the de novo banking locations and successfully integrate and promote our corporate culture among various others. Failure to adequately manage the risks associated with our anticipated growth through de novo branching could have a material adverse impact on our business, financial condition and results of operations.

The accuracy of our financial statements and related disclosures could be affected if the judgments, assumptions or estimates used in our critical accounting policies are inaccurate.

The preparation of financial statements and related disclosures in conformity with GAAP requires us to make judgments, assumptions and estimates that affect the amounts reported in our consolidated financial statements and accompanying notes. The accounting policies we consider to be "critical" are those significant accounting policies and methods that require judgments, assumptions and estimates and materially affect our consolidated financial statements and related disclosures. See the section captioned "Management's Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies" in this Annual Report on Form 10-K. If future events or regulatory views differ significantly from our judgments, assumptions and estimates, a restatement of prior period financial statements may

be required. Any such restatement may damage our reputation and could adversely impact the price of our common stock, financial condition and results of operations.

There could be material changes to our financial statements and disclosures as a result of changes in accounting standards or regulatory interpretations of existing standards.

From time to time the FASB or the SEC change the financial accounting and reporting standards that govern the preparation of our financial statements. Such changes may result in us being subject to new accounting and reporting standards or change existing accounting and reporting standards. In addition, the bodies that interpret the accounting standards (such as banking regulators or outside auditors) may change their interpretations or positions on how new or existing standards should be applied. These changes may be beyond our control, can be hard to predict and can materially impact how we record and report our financial condition and results of operations. In some cases, we could be required to apply a new standard, a revision to an existing standard or change the application of a standard in such a way that financial statements for periods previously reported are revised.

If we fail to maintain effective internal control over financial reporting, we may not be able to report our financial results accurately and timely.

Our management is responsible for establishing and maintaining adequate internal control over financial reporting and for evaluating and reporting on that system of internal control. In the past, significant deficiencies have been identified in our internal controls over financial reporting. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those responsible for oversight of the Company's financial reporting. Our actions to maintain effective controls and remedy any weakness or deficiency may not be sufficient to result in an effective internal control environment and any future failure to maintain effective internal control over financial reporting could impair the reliability of our financial statements, which in turn could harm our business, impair investor confidence in the accuracy and completeness of our financial reports, impair our access to the capital markets, cause the price of our common stock to decline and subject us to increased regulatory scrutiny and/or penalties, and higher risk of shareholder litigation.

We are dependent on the use of data and modeling in our decision-making.

The use of statistical and quantitative models and other quantitative analyses is endemic to bank decision-making and the employment of such analyses is becoming increasingly widespread in our operations. Liquidity stress testing, interest rate sensitivity analysis and the identification of possible violations of anti-money laundering regulations are all examples of areas in which we are dependent on models and the data that underlies them. The use of statistical and quantitative models is also becoming more prevalent in regulatory compliance. While we are not currently subject to annual Dodd-Frank Act stress testing and Comprehensive Capital Analysis and Review submissions, we anticipate that model-derived testing may become more extensively implemented by regulators in the future.

We anticipate data-based modeling will penetrate further into bank decision-making, particularly risk management efforts, as the capacities developed to meet rigorous stress testing requirements can be employed more widely and in differing applications. While we believe these quantitative techniques and approaches improve our decision-making, they also create the possibility that faulty data or flawed quantitative approaches could negatively impact our decision-making ability or if we become subject to regulatory stress testing in the future, adverse regulatory scrutiny. Further, because of the complexity inherent in these approaches, misunderstanding or misuse of their outputs could similarly result in suboptimal decision-making.

A lack of liquidity could impair our ability to fund operations.

Liquidity risk is the potential that we will be unable to meet our obligations as they become due because of an inability to liquidate assets or obtain adequate funding. We require sufficient liquidity to meet customer loan requests, customer deposit maturities and withdrawals, payments on our debt obligations as they come due and other cash commitments under both normal operating conditions and unpredictable circumstances, including events causing industry or general financial market stress. We rely on our ability to generate deposits and effectively manage the repayment and maturity schedules of our loans and securities to ensure that we have adequate liquidity to fund our operations. An inability to raise funds through deposits, borrowings, loan repayments, sales of our securities, sales of loans and other sources could have a negative impact on our liquidity.

Our most important source of funds is deposits, which have historically been stable sources of funds. However, deposits are subject to potentially dramatic fluctuations in availability or price due to factors that may be outside of our control, including increasing competitive pressure from other financial services firms for consumer or corporate customer deposits, changes in interest rates and returns on other investment classes. As a result, there could be significant outflows of deposits within short periods of time or significant changes in pricing necessary to maintain current customer deposits or attract additional deposits, increasing our funding costs and reducing our net interest income and net income.

Our access to funding sources, such as through our line of credit, capital markets offerings, borrowing from the Federal Reserve Bank of Dallas and the Federal Home Loan Bank, or from other third-parties, in amounts adequate to finance or capitalize our activities, or on terms that are acceptable to us, could be impaired by factors that affect us directly or the financial services industry or economy in general, such as disruptions in the financial markets or negative views and expectations about the prospects for the financial services industry.

We have unfunded credit commitments, which could adversely impact our liquidity.

We have unfunded commitments to extend credit, which are formal agreements to lend funds to customers as long as there are no violations of any conditions established in the contracts. Unfunded credit commitments are not reflected on our consolidated balance sheet and are generally not drawn upon. Borrowing needs of our customers may exceed our expectations, especially during a challenging economic environment where clients are more dependent on our credit commitments. Increased borrowings under these commitments could adversely impact our liquidity.

We face strong competition from financial services companies and other companies that offer banking services.

We operate in the highly competitive financial services industry and face significant competition for customers from financial institutions located both within and beyond our principal markets. We compete with commercial banks, savings banks, credit unions, nonbank financial services companies and other financial institutions operating within or near the areas we serve. Additionally, certain large banks headquartered outside of our markets and large community banking institutions target the same customers we do. In addition, as customer preferences and expectations continue to evolve, technology has lowered barriers to entry and made it possible for banks to expand their geographic reach by providing services over the internet and mobile devices and for nonbanks to offer products and services traditionally provided by banks, such as automatic transfer and automatic payment systems. The banking industry has experienced rapid changes in technology and, as a result, our future success may depend in part on our ability to address our customers' needs by using technology. Customer loyalty can be influenced by a competitor's new products, especially offerings that could provide cost savings or a higher return to the customer. Increased lending activity of competing banks can also lead to increased competitive pressures on loan rates and terms for high-quality credits. We may not be able to compete successfully with other financial institutions in our markets and we may have to pay higher interest rates to attract deposits, accept lower yields to attract loans and pay higher wages for new employees, resulting in lower net interest margins and reduced profitability.

Many of our nonbank competitors are not subject to the same extensive regulations that govern our activities and may have greater flexibility in competing for business. The financial services industry could become even more competitive because of legislative, regulatory and technological changes and continued consolidation. In addition, some of our current commercial banking customers may seek alternative banking sources as they develop needs for credit facilities larger than we may be able to accommodate.

Negative public opinion regarding our company or failure to maintain our reputation in the communities we serve could adversely impact our business.

As a community bank, our reputation within the communities we serve is critical to our success. We believe we have set ourselves apart from our competitors by building strong personal and professional relationships with our customers and by being active members of the communities we serve. As such, we strive to enhance our reputation by recruiting, hiring and retaining employees who share our core values of being an integral part of the communities we serve and delivering superior service to our customers. If our reputation is negatively affected by the actions of our employees or otherwise, we may be less successful in attracting new talent and customers or may lose existing customers. Further, negative public opinion can expose us to litigation and regulatory action and could delay and impede our efforts to implement our expansion strategy.

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We could recognize losses on securities held in our portfolio, particularly if interest rates increase or economic and market conditions deteriorate.

We invest in securities with the primary objectives of providing a source of liquidity, providing an appropriate return on funds invested, managing interest rate risk, meeting pledging requirements and meeting regulatory capital requirements. Factors beyond our control can significantly and adversely influence the fair value of securities in our portfolio. For example, fixed rate securities are generally subject to decreases in market value when interest rates rise. Additional factors include, but are not limited to, rating agency downgrades of the securities, defaults by the issuer or individual borrowers with respect to the underlying securities and instability in the credit markets. Any of the foregoing factors could cause other-than-temporary impairment or in future periods and result in realized losses. The process for determining whether impairment is other-than-temporary usually requires difficult, subjective judgments about the future financial performance of the issuer and any collateral underlying the security to assess the probability of receiving all contractual principal and interest payments on the security. Although we have not recognized other-than-temporary impairment related to our investment portfolio as of December 31, 2019, changing economic and market conditions affecting interest rates, the financial condition of issuers of the securities and the performance of the underlying collateral, among other factors, may cause us to recognize realized and/or unrealized losses in future periods.

We depend on our information technology and telecommunications systems, including third-party service providers.

Our business depends on the successful and uninterrupted functioning of our information technology and telecommunications systems including with third-party servicers and financial intermediaries. We outsource many of our major systems. Specifically, we rely on third-parties for certain services, including, but not limited to, core systems processing, website hosting, internet services, monitoring our network and other processing services. Our business depends on the successful and uninterrupted functioning of our information technology and telecommunications systems and third-party servicers. We could experience service denials if demand for such services exceeds capacity or such third-party systems fail or experience interruptions. The failure of these systems, an information security or cybersecurity breach involving any of our third-party service providers, or the termination or change in terms of a third-party software license or service agreement on which any of these systems is based, could interrupt our operations. Replacing vendors or addressing other issues with our third-party service providers could entail significant delay, expense and disruption of service could adversely impact or business, financial condition and results of operations. Even if we can replace third-party service providers, it may be at a higher cost to us.

In addition, the Bank's primary federal regulator, the OCC, has issued guidance outlining the expectations for third-party service provider oversight and monitoring by financial institutions. The federal banking agencies, including the OCC, have issued enforcement actions against financial institutions for failure in oversight of third-party providers and violations of federal banking law by such providers when performing services for financial institutions. Any failure on our part to adequately oversee the actions of our third-party service providers could result in regulatory actions against the Bank.

We could be adversely impacted by fraudulent activity, breaches of our information security and cybersecurity attacks.

As a financial institution, we are susceptible to fraudulent activity, information security breaches and cybersecurity-related incidents that may be committed against us, our clients, or third-parties with whom we interact and that may result in financial losses or increased costs to us or our clients, disclosure or misuse of confidential information belonging to us or personal or confidential information belonging to our clients, misappropriation of assets, litigation, or damage to our reputation. Our industry has seen increases in electronic fraudulent activity, hacking, security breaches, sophisticated social engineering and cyber-attacks, including within the commercial banking sector, as cyber-criminals have been targeting commercial bank and brokerage accounts on an increasing basis.

Our business is highly dependent on the security and efficacy of our infrastructure, computer and data management systems, as well as those of third-parties with whom we interact or on whom we rely. Our business relies on the secure processing, transmission, storage and retrieval of confidential, proprietary and other information in our computer and data management systems and networks, and in the computer and data management systems and networks of third-parties. In addition, to access our network, products and services, our customers and other third-parties may use personal mobile devices or computing devices that are outside of our network environment and are subject to their own cybersecurity risks. All of these factors increase our risks related to cyber-threats and electronic disruptions.

In addition to well-known risks related to fraudulent activity, which take many forms, such as check "kiting" or fraud, wire fraud, and other dishonest acts, information security breaches and cybersecurity-related incidents have become a material risk in the financial services industry. These threats may include fraudulent or unauthorized access to data processing or data storage systems used by us or by our clients, electronic identity theft, "phishing", account takeover, denial or degradation of service attacks, and malware or other cyber-attacks. These electronic viruses or malicious code are typically designed to, among other things:

- obtain unauthorized access to confidential information belonging to us or our clients and customers;
- manipulate or destroy data;
- disrupt, sabotage or degrade service on a financial institution's systems; or
- steal money.

In recent periods, several governmental agencies and large corporations, including financial service organizations and retail companies, have suffered major data breaches, in some cases exposing not only their confidential and proprietary corporate information, but also sensitive financial and other personal information of their clients or clients and their employees or other third-parties, and subjecting those agencies and corporations to potential fraudulent activity and their clients and other third-parties to identity theft and fraudulent activity in their credit card and banking accounts. Therefore, security breaches and cyber-attacks can cause significant increases in operating costs, including the costs of compensating clients and customers for any resulting losses they may incur, and the costs and capital expenditures required to correct the deficiencies in and strengthen the security of data processing and storage systems.

Unfortunately, it is not always possible to anticipate, detect or recognize these threats to our systems, or to implement effective preventative measures against all breaches, whether those breaches are malicious or accidental. Cybersecurity risks for banking organizations have significantly increased in recent years and have been difficult to detect before they occur because of the following, among other reasons:

- the proliferation of new technologies, and the use of the internet and telecommunications technologies to conduct financial transactions;
- these threats arise from numerous sources, not all of which are in our control, including among others, human
 error, fraud or malice on the part of employees or third-parties, accidental technological failure, electrical or
 telecommunication outages, failures of computer servers or other damage to our property or assets, natural
 disasters or severe weather conditions, health emergencies or pandemics, or outbreaks of hostilities or
 terrorist acts:
- the techniques used in cyber-attacks change frequently and may not be recognized until launched or until
 well after the breach has occurred;

- the increased sophistication and activities of organized crime groups, hackers, terrorist organizations, hostile foreign governments, disgruntled employees or vendors, activists and other external parties, including those involved in corporate espionage;
- the vulnerability of systems to third-parties seeking to gain access to such systems either directly or using equipment or security passwords belonging to employees, customers, third-party service providers or other users of our systems; and
- our frequent transmission of sensitive information to, and storage of such information by, third-parties, including our vendors and regulators, and possible weaknesses that go undetected in our data systems notwithstanding the testing we conduct of those systems.

While we invest in systems and processes that are designed to detect and prevent security breaches and cyber-attacks and we conduct periodic tests of our security systems and processes, we may not succeed in anticipating or adequately protecting against or preventing all security breaches and cyber-attacks from occurring. Even the most advanced internal control environment may be vulnerable to compromise. Targeted social engineering attacks are becoming more sophisticated and are extremely difficult to prevent. Additionally, the existence of cyber-attacks or security breaches at third-parties with access to our data, such as vendors, may not be disclosed to us in a timely manner. As cyber-threats continue to evolve, we may be required to expend significant additional resources to continue to modify or enhance our protective measures or to investigate and remediate any information security vulnerabilities or incidents.

As is the case with non-electronic fraudulent activity, cyber-attacks or other information or security breaches, whether directed at us or third-parties, may result in a material loss or have material consequences. Furthermore, the public perception that a cyber-attack on our systems has been successful, whether or not this perception is correct, may damage our reputation with customers and third-parties with whom we do business. A successful penetration or circumvention of system security could cause negative consequences, including loss of customers and business opportunities, disruption to our operations and business, misappropriation or destruction of our confidential information and/or that of our customers, or damage to our customers' and/or third-parties' computers or systems, and could expose us to additional regulatory scrutiny and result in a violation of applicable privacy laws and other laws, litigation exposure, regulatory fines, penalties or intervention, loss of confidence in our security measures, reputational damage, reimbursement or other compensatory costs, additional compliance costs, and could adversely impact our results of operations, liquidity and financial condition.

During 2018, we experienced a security incident involving the possible unauthorized access of certain personal information in the possession of the Bank. We take the privacy of personal information seriously and we took steps to address the incident promptly after it was discovered, including initiating an internal investigation into the incident and working with an independent forensic investigation firm to assist us in the investigation of and response to the incident. We also reported the incident to law enforcement authorities. Based on the report of the independent forensic investigation firm, we believe that a phishing incident occurred where certain emails and attachments from two employee email accounts may have been accessed by an unauthorized person. We believe that these email accounts contained certain personal information for approximately 7,800 individuals. Although our investigation has not found any evidence that the incident involved any unauthorized access to or use of any of the Bank's internal computer systems or network, and we believe that the access was limited to information that was contained in the email accounts of the two employees, we may become subject to claims in the future for purportedly fraudulent transactions or other matters arising out of the breach of information stored in the affected email accounts. Additionally, the incident may have a negative impact on our reputation if we become subject to claims in the future, and reputational harm arising out of such claims or litigation may cause our customers to lose confidence in our ability to safeguard their information.

We have a continuing need for technological change.

The financial services industry has undergone rapid technological changes with frequent introductions of new technology-driven products and services. In addition to better serving customers, the effective use of technology increases efficiency and enables financial institutions to reduce costs. Our future success will depend, at least in part, upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands for convenience as well as to create additional efficiencies in our operations as we continue to grow and expand our products and service offerings. We may experience operational challenges as we implement these new technology enhancements or products, which could impair our ability to realize the anticipated benefits from such new technology or require us to incur significant costs to remedy any such challenges in a timely manner.

We are subject to laws regarding the privacy, information security and protection of personal information.

Our business requires the collection and retention of large volumes of customer data, including personally identifiable information in various information systems that we maintain and in those maintained by third-parties with whom we contract to provide data services. We also maintain important internal company data such as personally identifiable information about our employees and information relating to our operations. We are subject to complex and evolving laws and regulations governing the privacy and protection of personal information of individuals (including customers, employees, suppliers and other third-parties). For example, our business is subject to the Gramm-Leach-Bliley Act which, among other things: (i) imposes certain limitations on our ability to share nonpublic personal information about our customers with nonaffiliated third-parties; (ii) requires that we provide certain disclosures to customers about our information collection, sharing and security practices and afford customers the right to "opt out" of any information sharing by us with nonaffiliated third-parties (with certain exceptions); and (iii) requires that we develop, implement and maintain a written comprehensive information security program containing appropriate safeguards based on our size and complexity, the nature and scope of our activities and the sensitivity of customer information we process, as well as plans for responding to data security breaches. There are various state and federal data security breach notification requirements with varying levels of individual, consumer, regulatory or law enforcement notification in certain circumstances in the event of a security breach. Ensuring that our collection, use, transfer and storage of personal information complies with all applicable laws and regulations can increase our costs.

Furthermore, we may not be able to ensure that all our clients, suppliers, counterparties and other third-parties have appropriate controls in place to protect the confidentiality of the information that they exchange with us, particularly where such information is transmitted by electronic means. If personal, confidential or proprietary information of customers or others were to be mishandled or misused (in situations where, for example, such information was erroneously provided to parties who are not permitted to have the information, or where such information was intercepted or otherwise compromised by third-parties), we could be exposed to litigation or regulatory sanctions under personal information laws and regulations. Concerns regarding the effectiveness of our measures to safeguard personal information, or even the perception that such measures are inadequate, could cause us to lose customers or potential customers for our products and services and thereby reduce our revenues. Accordingly, any failure or perceived failure to comply with applicable privacy or data protection laws and regulations may subject us to inquiries, examinations and investigations that could result in requirements to modify or cease certain operations or practices or in significant liabilities, fines or penalties and could damage our reputation and otherwise adversely impact our operations and financial condition.

We could be adversely impact by employee errors and customer or employee fraud.

Because we are a financial institution, employee errors and employee or customer misconduct could cause financial losses or regulatory sanctions and seriously harm our reputation. Misconduct by our employees could include hiding unauthorized activities from us, improper or unauthorized activities on behalf of our customers or improper use of confidential information, each of which can be particularly damaging for financial institutions. It is not always possible to prevent employee errors and misconduct and the precautions we take to prevent and detect this activity may not be effective in all cases. Employee errors could also subject us to financial claims for negligence.

We maintain a system of internal controls to mitigate operational risks, including data processing system failures and errors and customer or employee fraud, as well as insurance coverage designed to protect us from material losses associated with these risks, including losses resulting from any associated business interruption. If our internal controls fail to prevent or detect an occurrence, or if any resulting loss is not insured or exceeds applicable insurance limits, it could adversely impact our business, financial condition and results of operations.

We depend on the accuracy and completeness of information provided to us by our borrowers and counterparties.

In deciding whether to approve loans or to enter into other transactions with borrowers and counterparties, we rely on information furnished to us by, or on behalf of, borrowers and counterparties, including financial statements, credit reports and other financial information. We also rely on representations of borrowers and counterparties as to the accuracy and completeness of that information and, with respect to financial statements, on reports of independent auditors. If any of this information is intentionally or negligently misrepresented and such misrepresentation is not detected prior to loan funding, the value of the loan may be significantly lower than expected and we may be subject to regulatory action. Whether a misrepresentation is made by the loan applicant, another third-party, or one of our employees, we generally bear the risk of loss associated with the misrepresentation. Our controls and processes may not have detected, or may not

detect all, misrepresented information in our loan originations or from our business clients. Any such misrepresented information could adversely impact our business, financial condition and results of operations.

We may be subject to environmental liabilities in connection with the real properties we own and the foreclosure on real estate assets securing our loan portfolio.

We may purchase real estate in connection with our acquisition and expansion efforts, or we may foreclose on and take title to real estate or otherwise be deemed to be in control of property that serves as collateral on loans we make. We could be subject to environmental liabilities with respect to those properties. We may be held liable to a governmental entity or to third-parties for property damage, personal injury, investigation and clean-up costs incurred by these parties in connection with environmental contamination, or we may be required to investigate or clean up hazardous or toxic substances or chemical releases at a property. The costs associated with investigation or remediation activities could be substantial. In addition, if we are the owner or former owner of a contaminated site, we may be subject to common law claims by third-parties based on damages and costs resulting from environmental contamination emanating from the property. The cost of removal or abatement may substantially exceed the value of the affected properties or the loans secured by those properties, we may not have adequate remedies against the prior owners or other responsible parties and we may not be able to resell the affected properties either before or after completion of any such removal or abatement procedures.

We could be adversely impacted by natural disasters, pandemics and other catastrophes.

We operate banking locations throughout Houston and Beaumont areas, which are susceptible to hurricanes, tropical storms, other adverse weather conditions, pandemics and other catastrophes. In addition, man-made events such as acts of terror and governmental responses to acts of terror, malfunctions of the electronic grid and other infrastructure breakdowns, could adversely affect economic conditions in our markets. These adverse weather and catastrophic events can disrupt our operations, cause widespread and extensive property damage, force the relocation of residents and significantly disrupt economic activity in the region, significantly depress the local economies in which we operate and adversely affect our customers. If the economies in our markets experience an overall decline because of a catastrophic event, demand for loans and our other products and services could decline. In addition, the rates of delinquencies, foreclosures, bankruptcies and losses on our loan portfolios may increase substantially after events such as hurricanes, as uninsured property losses, interruptions of our customers' operations or sustained job interruption or loss may materially impair the ability of borrowers to repay their loans. Moreover, the value of real estate or other collateral that secures our loans could be materially and adversely affected by a catastrophic event.

We are subject to claims and litigation pertaining to intellectual property in addition to other litigation in the ordinary course of business.

Banking and other financial services companies, such as our company, rely on technology companies to provide information technology products and services necessary to support their day-to-day operations. Technology companies frequently enter litigation based on allegations of patent infringement or other violations of intellectual property rights. We also use trademarks and logos for marketing purposes, and third-parties may allege that our marketing, processes or systems may infringe their intellectual property rights. Competitors of our vendors, or other individuals or companies, may from time to time claim to hold intellectual property sold to us by our vendors. Such claims may increase in the future as the financial services sector becomes more reliant on information technology vendors. The plaintiffs in these actions frequently seek injunctions and substantial damages.

These licenses may also significantly increase our operating expense. If legal matters related to intellectual property claims were resolved against us or settled, we could be required to make payments in amounts that could have a material adverse effect on our business, financial condition and results of operations.

Regardless of the scope or validity of such patents or other intellectual property rights, or the merits of any claims by potential or actual litigants, we may have to engage in protracted litigation that can be expensive, time-consuming, disruptive to our operations and distracting to management. If we are found to infringe one or more patents or other intellectual property rights, we may be required to pay substantial damages or royalties to a third-party.

In addition to litigation relating to intellectual property, we are regularly involved in litigation matters in the ordinary course of business. While we believe that these litigation matters should not have a material adverse impact on

our business, financial condition, results of operations or future prospects, we may be unable to successfully defend or resolve any current or future litigation matters.

The value of our goodwill and other intangibles may become impaired.

We review goodwill and other intangibles for impairment at least annually, or more frequently if a triggering event occurs which indicates that the carrying value of these assets might be impaired. While we have not recorded any impairment charges related to goodwill and other intangibles, there can be no assurance that our future evaluations of our existing goodwill and intangibles or such assets we may acquire in the future will not result in findings of impairment and related write-downs.

Risks Related to the Regulation of Our Industry

We operate in a highly regulated environment.

Banking is highly regulated under federal and state law. As such, we are subject to extensive regulation, supervision and legal requirements that govern almost all aspects of our operations. These laws and regulations are not intended to protect our shareholders. Rather, these laws and regulations are intended to protect customers, depositors, the Deposit Insurance Fund and the overall financial stability of the U.S. These laws and regulations, among other matters, prescribe minimum capital requirements, impose limitations on the business activities in which we can engage, limit the dividend or distributions that the Bank can pay to us, restrict the ability of institutions to guarantee our debt and impose certain specific accounting requirements on us that may be more restrictive and may result in greater or earlier charges to earnings or reductions in our capital than GAAP would require. Compliance with laws and regulations can be difficult and costly and changes to laws and regulations often impose additional operating costs. Our failure to comply with these laws and regulations, even if the failure follows good faith effort or reflects a difference in interpretation, could subject us to restrictions on our business activities, enforcement actions and fines and other penalties, any of which could adversely affect our results of operations, regulatory capital levels and the price of our securities. Further, any new laws, rules and regulations could make compliance more difficult or expensive or otherwise adversely impact our business, financial condition and results of operations.

The implementation of the Dodd-Frank Act could adversely affect our business, financial condition and results of operations.

On July 21, 2010, the Dodd-Frank Act was signed into law and there remains uncertainty around the impact of the law and the implementation and regulations pursuant to the law. The Trump administration issued an executive order calling for a full review of the Dodd-Frank Act and the regulations promulgated under it. The changes resulting from the Dodd-Frank Act may impact the profitability of our business activities, require changes to certain of our business practices, require the development of new compliance infrastructure, impose upon us more stringent capital, liquidity and leverage requirements or otherwise adversely affect our business. These changes may also require us to invest significant management attention and resources to evaluate and make any changes necessary to comply with new statutory and regulatory requirements. Failure to comply with the new requirements or with any future changes in laws or regulations could adversely impact our business, financial condition and results of operations.

We could be adversely impacted if we fail to comply with any supervisory actions.

As part of the bank regulatory process, the OCC and the Federal Reserve periodically conduct examinations of our business, including compliance with laws and regulations. If one of these federal banking agencies were to determine that the financial condition, capital resources, asset quality, earnings prospects, management, liquidity, asset sensitivity, risk management or other aspects of any of our operations have become unsatisfactory, or that our Company, the Bank or their respective management were in violation of any law or regulation, it may take a number of different remedial actions as it deems appropriate. These actions include the power to enjoin "unsafe or unsound" practices, to require affirmative actions to correct any conditions resulting from any violation or practice, to issue an administrative order that can be judicially enforced, to direct an increase in our capital levels, to restrict our growth, to assess civil monetary penalties against us, the Bank or their respective officers or directors, to remove officers and directors and, if it is concluded that such conditions cannot be corrected or there is an imminent risk of loss to depositors, to terminate the Bank's deposit insurance. Becoming subject to such regulatory actions could adversely impact our reputation, business, financial condition and results of operations.

We are subject to stringent capital requirements.

The federal banking agencies published new capital rules, referred to herein as the Basel III capital rules, which apply to all bank holding companies with \$3.0 billion or more in consolidated assets and all banks regardless of size. Under the Basel III capital rules, we are required to maintain certain minimum capital levels. Our inability to comply with these capital requirements could, among other things, result in lower returns on equity, require the raising of additional capital, limit our ability to repurchase shares or pay dividends and discretionary bonuses or result in regulatory actions, any of which could adversely impact our business, financial condition and results of operations.

Many of our new activities and expansion plans require regulatory approvals and failure to obtain them may restrict our growth.

We intend to complement and expand our business by pursuing strategic acquisitions of financial institutions and other complementary businesses and expansion of the Bank's banking location network, or *de novo* branching. Generally, we must receive federal regulatory approval before we can acquire a depository institution or related business insured by the FDIC, or before we open a *de novo* branch. In determining whether to approve a proposed acquisition, federal banking regulators will consider, among other factors, the impact of the acquisition on competition, our financial condition, our future prospects and the impact of the proposal on U.S. financial stability. The regulators also review current and projected capital ratios and levels, the competence, experience and integrity of management and its record of compliance with laws and regulations, the convenience and needs of the communities to be served (including the acquiring institution's record of compliance under the CRA and the effectiveness of the acquiring institution in combating money laundering activities). Such regulatory approvals may not be granted on terms that are acceptable to us, or at all. We may also be required to sell banking locations as a condition to receiving regulatory approval, which condition may not be acceptable to us or, if acceptable to us, may reduce the benefit of any acquisition.

We face a risk of noncompliance and enforcement action related to anti-money laundering statutes and regulations.

The BSA, the USA PATRIOT Act, and other laws and regulations require financial institutions, among other duties, to institute and maintain an effective anti-money laundering program and file suspicious activity and currency transaction reports as appropriate. FinCEN, established by the U.S. Department of the Treasury to administer the BSA, is authorized to impose significant civil money penalties for violations of those requirements and frequently coordinates enforcement efforts with the individual federal banking regulators, as well as the U.S. Department of Justice, the Drug Enforcement Administration and the IRS. There is also increased scrutiny of compliance with the sanctions programs and rules administered and enforced by OFAC.

To comply with regulations, guidelines and examination procedures in this area, we have dedicated significant resources to our anti-money laundering program. If our policies, procedures, systems and practices are deemed deficient, we could be subject to liability, including fines, regulatory actions such as restrictions on our ability to pay dividends and the inability to obtain regulatory approvals to proceed with certain aspects of our business plans, including acquisitions and *de novo* branching, and criminal sanctions.

The Bank is the subject of an investigation by FinCEN regarding the Bank's compliance with the BSA and anti-money laundering laws and regulations.

The Bank is the subject of an investigation by FinCEN and the Bank is cooperating with this investigation. The Bank has incurred material fees and expenses regarding with this matter and may continue to incur material fees and expenses regarding this matter at least through the completion of FinCEN's investigation. Additionally, the Bank could be subject to additional liability or restrictions on its operations in the event the investigation results in some type of finding of a deficiency in its program that results in an enforcement action or civil money penalty which could have a material adverse impact on us and our operations.

We are subject to numerous laws designed to protect consumers and failure to comply with these laws could lead to a wide variety of sanctions.

The CRA, the Equal Credit Opportunity Act, the Fair Housing Act and other fair lending laws and regulations impose nondiscriminatory lending requirements on financial institutions. The CFPB, the U.S. Department of Justice and other federal agencies are responsible for enforcing these laws and regulations. The CFPB was created under the

Dodd-Frank Act to centralize responsibility for consumer financial protection with broad rulemaking authority to administer and carry out the purposes and objectives of federal consumer financial laws with respect to all financial institutions that offer financial products and services to consumers. The CFPB is also authorized to prescribe rules applicable to any covered person or service provider, identifying and prohibiting acts or practices that are "unfair, deceptive, or abusive" in connection with any transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial product or service. The ongoing broad rulemaking powers of the CFPB have potential to have a significant impact on the operations of financial institutions offering consumer financial products or services. The CFPB has indicated that it may propose new rules on overdrafts and other consumer financial products or services, which could have a material adverse impact on our business, financial condition and results of operations if any such rules limit our ability to provide such financial products or services.

A successful regulatory challenge to an institution's performance under the CRA, fair lending laws or regulations, or consumer lending laws and regulations could result in a wide variety of sanctions, including damages and civil money penalties, injunctive relief, restrictions on mergers and acquisitions activity, restrictions on expansion and restrictions on entering new business lines. Private parties can also challenge an institution's performance under fair lending laws in private class action litigation. Such actions could have a material adverse impact on our business, financial condition and results of operations.

Failure to comply with economic and trade sanctions or with applicable anti-corruption laws could have a material adverse impact our business, financial condition and results of operations.

OFAC administers and enforces economic and trade sanctions against targeted foreign countries and regimes, under authority of various laws, including designated foreign countries, nationals and others. We are responsible for, among other things, blocking accounts of and transactions with such persons and countries, prohibiting unlicensed trade and financial transactions with them and reporting blocked transactions after their occurrence. Through our Company and the Bank and our agents and employees, we are subject to the Foreign Corrupt Practices Act, or the FCPA, which prohibits offering, promising, giving, or authorizing others to give anything of value, either directly or indirectly, to a non-U.S. government official in order to influence official action or otherwise gain an unfair business advantage. We are also subject to applicable anti-corruption laws in the jurisdictions in which we may operate. We have implemented policies, procedures and internal controls that are designed to comply with economic and trade sanctions or with applicable anti-corruption laws, including the FCPA. Failure to comply with economic and trade sanctions or with applicable anti-corruption laws, including the FCPA, could have serious legal and reputational consequences for us.

Federal, state and local consumer lending laws may restrict our ability to originate certain mortgage loans or increase our risk of liability with respect to such loans.

Federal, state and local laws have been adopted that are intended to eliminate certain lending practices considered "predatory." These laws prohibit practices such as steering borrowers away from more affordable products, selling unnecessary insurance to borrowers, repeatedly refinancing loans and making loans without a reasonable expectation that the borrowers will be able to repay the loans irrespective of the value of the underlying property. It is our policy not to make predatory loans, but these laws create the potential for liability with respect to our lending and loan investment activities. They increase our cost of doing business and, ultimately, may prevent us from making certain loans and cause us to reduce the average percentage rate or the points and fees on loans that we do make.

Federal, state and local regulations and/or the licensing of loan servicing, collections and our sales of loans to third-parties may increase the cost of compliance and the risks of noncompliance and subject us to litigation.

We service some of our own loans and loan servicing is subject to extensive regulation by federal, state and local governmental authorities, as well as various laws and judicial and administrative decisions imposing requirements and restrictions on those activities. The volume of new or modified laws and regulations has increased in recent years and, in addition, some individual municipalities have begun to enact laws that restrict loan servicing activities, including delaying or temporarily preventing foreclosures or forcing the modification of certain mortgages. If regulators impose new or more restrictive requirements, we may incur additional significant costs to comply with such requirements, which may further adversely affect us. In addition, if we were subject to regulatory investigation or regulatory action regarding our loan modification and foreclosure practices, our financial condition and results of operations could be adversely impacted.

In addition, we have sold loans to third-parties. In these sales, we or certain of our subsidiaries or legacy companies make or have made various representations and warranties. Breaches of these representations and warranties may result in a requirement that we repurchase the loans, or otherwise make whole or provide other remedies to counterparties. These aspects of our business or our failure to comply with applicable laws and regulations could possibly lead to civil and criminal liability; loss of licensure; damage to our reputation in the industry; fines and penalties and litigation, including class action lawsuits; and administrative enforcement actions.

Potential limitations on incentive compensation contained in proposed federal agency rulemaking may adversely impact our ability to attract and retain our highest performing employees.

In April 2011 and May 2016, the Federal Reserve, other federal banking agencies and the SEC jointly published proposed rules designed to implement provisions of the Dodd-Frank Act prohibiting incentive compensation arrangements that would encourage inappropriate risk taking at covered financial institutions, which includes a bank or bank holding company with \$1 billion or more in assets, such as the Bank. It cannot be determined at this time whether or when a final rule will be adopted and whether compliance with such a final rule will substantially affect the way we structure compensation for our executives and other employees. Depending on the nature and application of the final rules, we may not be able to successfully compete with certain financial institutions and other companies that are not subject to some or all the rules to retain and attract executives and other high performing employees. If this were to occur, relationships that we have established with our clients may be impaired and our business, financial condition and results of operations could be adversely impacted.

Increases in FDIC insurance premiums could adversely impact our earnings and results of operations.

We are generally unable to control the amount of premiums that we are required to pay for FDIC insurance. In 2010, the FDIC increased the Deposit Insurance Fund's target reserve ratio to 2.0% of insured deposits following the Dodd-Frank Act's elimination of the 1.5% cap on the insurance fund's reserve ratio and the FDIC is required to put in place a restoration plan should the Deposit Insurance Fund fall below its 1.35% minimum reserve ratio. If the Deposit Insurance Fund falls below its minimum reserve ratio or fails to meet its funding requirements, special assessments or increases in deposit insurance premiums may be required. Further, if there are additional financial institution failures that affect the Deposit Insurance Fund, we may be required to pay higher FDIC premiums.

The Federal Reserve may require us to commit capital resources to support the Bank.

The Federal Reserve requires a bank holding company to act as a source of financial and managerial strength to its subsidiary banks and to commit resources to support its subsidiary banks. Under the "source of strength" doctrine that was codified by the Dodd-Frank Act, the Federal Reserve may require a bank holding company to make capital injections into a troubled subsidiary bank at times when the bank holding company may not be inclined to do so and may charge the bank holding company with engaging in unsafe and unsound practices for failure to commit resources to such a subsidiary bank. Accordingly, we could be required to provide financial assistance to the Bank if it experiences financial distress.

A capital injection may be required at a time when our resources are limited, and we may be required to borrow the funds or raise capital to make the required capital injection. Any loan by a bank holding company to its subsidiary bank is subordinate in right with payment to deposits and certain other indebtedness of such subsidiary bank. In the event of a bank holding company's bankruptcy, the bankruptcy trustee will assume any commitment by the holding company to a federal bank regulatory agency to maintain the capital of a subsidiary bank. Moreover, bankruptcy law provides that claims based on any such commitment will be entitled to a priority of payment over the claims of the holding company's general unsecured creditors, including the holders of any note obligations. Thus, any borrowing by a bank holding company to make a capital injection to a subsidiary bank often becomes more difficult and expensive relative to other corporate borrowings.

We could be adversely impacted by the soundness of other financial institutions.

Financial services institutions are interrelated because of trading, clearing, counterparty or other relationships. We have exposure to many different industries and counterparties and routinely execute transactions with counterparties in the financial services industry, including commercial banks, brokers and dealers, investment banks and other institutional clients. Many of these transactions expose us to credit risk in the event of a default by a counterparty or client.

In addition, our credit risk may be exacerbated when our collateral cannot be foreclosed upon or is liquidated at prices not sufficient to recover the full amount of the credit or derivative exposure due.

We could be adversely impacted by monetary policies and regulations of the Federal Reserve.

In addition to being affected by general economic conditions, our earnings and growth are affected by the policies of the Federal Reserve. An important function of the Federal Reserve is to regulate the U.S. money supply and credit conditions. Among the instruments used by the Federal Reserve to implement these objectives are open market purchases and sales of securities by the Federal Reserve, adjustments of both the discount rate and the federal funds rate and changes in reserve requirements against bank deposits. These instruments are used in varying combinations to influence overall economic growth and the distribution of credit, bank loans, investments and deposits. Their use also affects interest rates charged on loans or paid on deposits. The monetary policies and regulations of the Federal Reserve have had a significant impact on the operating results of commercial banks in the past and are expected to continue to do so in the future. Although we cannot determine the effects of such policies on us, such policies could adversely impact our business, financial condition and results of operations.

We are subject to commercial real estate lending guidance issued by the federal banking regulators that impacts our operations and capital requirements.

The OCC and the other federal bank regulatory agencies have promulgated joint guidance on sound risk management practices for financial institutions regarding concentrations in commercial real estate lending. Under the guidance, a financial institution that, like us, is actively involved in commercial real estate lending should perform a risk assessment to identify concentrations. A financial institution may have a concentration in commercial real estate lending if, among other factors, (1) total reported loans for construction, land acquisition and development and other land represent 100% or more of total capital, or (2) total reported loans secured by multi-family and nonfarm nonresidential properties, loans for construction, land acquisition and development and other land and loans otherwise sensitive to the general commercial real estate market, including loans to commercial real estate related entities, represent 300% or more of total capital.

The focus of the guidance is on exposure to commercial real estate loans that are dependent on the cash flow from the real estate held as collateral and that are likely to be at greater risk to conditions in the commercial real estate market (as opposed to real estate collateral held as a secondary source of repayment or as an abundance of caution). The purpose of the guidance is to guide banks in developing risk management practices and capital levels commensurate with the level and nature of real estate concentrations. The guidance states that management should employ heightened risk management practices including board and management oversight and strategic planning, development of underwriting standards, risk assessment and monitoring through market analysis and stress testing. While we believe we have implemented policies and procedures with respect to our commercial real estate loan portfolio consistent with this guidance, bank regulators could require us to implement additional policies and procedures consistent with their interpretation of the guidance that may result in additional costs to us or that may result in a curtailment of our commercial real estate lending and/or the requirement that we maintain higher levels of regulatory capital, either of which would adversely impact our loan originations and profitability.

Risks Related to Ownership of our Common Stock

The market price of our common stock may be subject to substantial fluctuations.

The market price of our common stock may be highly volatile, which may make it difficult for you to resell your shares at the volume, prices and times desired. There are many factors that may affect the market price and trading volume of our common stock, including, without limitation:

- actual or anticipated fluctuations in our operating results, financial condition or asset quality;
- changes in economic or business conditions;
- the effects of and changes in, trade, monetary and fiscal policies, including the interest rate policies of the Federal Reserve:
- publication of research reports about us, our competitors, or the financial services industry generally, or changes in, or failure to meet, securities analysts' estimates of our financial and operating performance, or lack of research reports by industry analysts or ceasing of coverage;

- operating and stock price performance of companies that investors deemed comparable to us;
- additional or anticipated sales of our common stock or other securities by us or our existing shareholders;
- additions or departures of key personnel;
- perceptions in the marketplace regarding our competitors or us, including the perception that investment in Texas is unattractive or less attractive during periods of low oil prices;
- significant acquisitions or business combinations, strategic partnerships, joint ventures or capital commitments by or involving our competitors or us;
- other economic, competitive, governmental, regulatory and technological factors affecting our operations, pricing, products and services; and
- other news, announcements or disclosures (whether by us or others) related to us, our competitors, our primary markets or the financial services industry.

The stock market and especially the market for financial institution stocks have experienced substantial fluctuations in recent years, which in many cases have been unrelated to the operating performance and prospects of companies. In addition, significant fluctuations in the trading volume in our common stock may cause significant price variations to occur. Increased market volatility may materially and adversely affect the market price of our common stock and could make it difficult to sell your shares at the volume, prices and times desired.

Future sales and issuances of our capital stock or rights to purchase capital stock could result in additional dilution of the percentage ownership of our shareholders.

We may issue additional securities in the future and from time to time, including as consideration in future acquisitions or under compensation or incentive plan. Future sales and issuances of our common stock or rights to purchase our common stock could result in substantial dilution to our existing shareholders. New investors in such subsequent transactions could gain rights, preferences and privileges senior to those of holders of our common stock. We may grant registration rights covering shares of our common stock or other securities in connection with acquisitions and investments.

The obligations associated with being a public company require significant resources and management attention.

As a public company, our legal, accounting, administrative and other costs and expenses are substantial. We are subject to the reporting requirements of the Exchange Act and the rules and regulations implemented by the SEC, the Sarbanes-Oxley Act of 2002, the Dodd-Frank Act, the Public Company Accounting Oversight Board, or PCAOB and the Nasdaq, each of which imposes additional reporting and other obligations on public companies. As a public company, compliance with these reporting requirements and other SEC and Nasdaq rules has made certain operating activities more time-consuming. Further, our reporting burden will increase when we no longer qualify for the scaled disclosure allowed us as an "emerging growth company" under the JOBS Act. We could cease to be an "emerging growth company" as soon as the end of the 2020 fiscal year. When these exemptions cease to apply, we will likely incur additional expenses and devote increased management effort toward compliance.

Our management and Board of Directors have significant control over our business.

Our directors and named executive officers beneficially owned approximately 29.3% of our outstanding common stock as a group at December 31, 2019. Consequently, our management and Board of Directors may be able to significantly affect our affairs and policies, including the outcome of the election of directors and the potential outcome of other matters submitted to a vote of our shareholders, such as mergers, the sale of substantially all our assets and other extraordinary corporate matters. This influence may also have the effect of delaying or preventing changes of control or changes in management or limiting the ability of our other shareholders to approve transactions that they may deem to be in the best interests of our Company. The interests of these insiders could conflict with the interests of our other shareholders.

The holders of our debt obligations have priority over our common stock with respect to payment in the event of liquidation, dissolution or winding up and with respect to the payment of interest.

In the event of any liquidation, dissolution or winding up of the Company, our common stock would rank below all claims of debt holders against us. Our debt obligations are senior to our shares of common stock. As a result, we must make payments on our debt obligations before any dividends can be paid on our common stock. In the event of bankruptcy, dissolution or liquidation, the holders of our debt obligations must be satisfied before any distributions can be made to the holders of our common stock. To the extent that we issue additional debt obligations they will be of equal rank with, or senior to, our existing debt obligations and senior to our shares of common stock.

We may issue shares of preferred stock in the future.

Our certificate of formation authorizes us to issue up to 10,000,000 shares of one or more series of preferred stock. Our Board of Directors will have the authority to determine the preferences, limitations and relative rights of shares of preferred stock and to fix the number of shares constituting any series and the designation of such series, without any further vote or action by our shareholders. Our preferred stock could be issued with voting, liquidation, dividend and other rights superior to the rights of our common stock. The potential issuance of preferred stock may delay or prevent a change in control of us, discourage bids for our common stock at a premium over the market price and materially adversely impact the market price and the voting and other rights of the holders of our common stock.

We are dependent upon the Bank for cash flow and the Bank's ability to make cash distributions is restricted.

Our primary tangible asset is the stock of the Bank. As such, we depend upon the Bank for cash distributions that we use to pay our operating expenses, satisfy our obligations and to pay dividends on our common stock. Federal statutes, regulations and policies restrict the Bank's ability to make cash distributions to us. These statutes and regulations require, among other things, that the Bank maintain certain levels of capital in order to pay a dividend. Further, the OCC can restrict the Bank's payment of dividends by supervisory action. If the Bank is unable to pay dividends to us, we will not be able to satisfy our obligations or pay dividends on our common stock.

Our dividend policy may change without notice and our future ability to pay dividends is subject to restrictions.

Although we have historically paid dividends to our shareholders, we have no obligation to continue doing so and may change our dividend policy at any time without notice to holders of our common stock. Holders of our common stock are only entitled to receive such cash dividends as our Board of Directors may declare out of funds legally available for such payments. Furthermore, consistent with our strategic plans, growth initiatives, capital availability, projected liquidity needs and other factors, we have made and will continue to make, capital management decisions and policies that could adversely impact the amount of dividends paid to holders of our common stock.

We are also subject to regulation by the Federal Reserve requiring that we inform and consult with the Federal Reserve prior to declaring and paying a dividend that exceeds earnings for the period for which the dividend is being paid or that could result in an adverse change to our capital structure, including interest on our other debt obligations. If required payments on our other debt obligations are not made or are deferred, or dividends on any preferred stock we may issue are not paid, we will be prohibited from paying dividends on our common stock.

In addition, our ability to declare or pay dividends is also subject to the terms of our loan agreement, which prohibits us from declaring or paying dividends upon the occurrence and during the continuation of an event of default. See "Item 8—Financial Statements and Supplementary Data—Note 11."

Our corporate organizational documents and provisions of federal and state law to which we are subject contain certain provisions that could have an anti-takeover effect.

Our certificate of formation and our bylaws (each as amended and restated) may have an anti-takeover effect and may delay, discourage or prevent an attempted acquisition or change of control or a replacement of our incumbent Board of Directors or management. Our governing documents include provisions that:

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• empower our Board of Directors, without shareholder approval, to issue our preferred stock, the terms of which, including voting power, are to be set by our Board of Directors;

- establish a classified Board of Directors, with directors of each class serving a three-year term upon completion of a phase-in period;
- provide that directors may only be removed from office for cause and only upon a majority shareholder vote;
- eliminate cumulative voting in elections of directors;
- permit our Board of Directors to alter, amend or repeal our amended and restated bylaws or to adopt new bylaws;
- require the request of holders of at least 50.0% of the outstanding shares of our capital stock entitled to vote at a meeting to call a special shareholders' meeting;
- prohibit shareholder action by less than unanimous written consent, thereby requiring virtually all actions to be taken at a meeting of the shareholders;
- require shareholders that wish to bring business before annual or special meetings of shareholders, or to nominate candidates for election as directors at our annual meeting of shareholders, to provide timely notice of their intent in writing; and
- enable our Board of Directors to increase, between annual meetings, the number of persons serving as directors and to fill the vacancies created as a result of the increase by a majority vote of the directors present at a meeting of directors.

In addition, certain provisions of Texas law, including a provision which restricts certain business combinations between a Texas corporation and certain affiliated shareholders, may delay, discourage or prevent an attempted acquisition or change in control. Furthermore, banking laws impose notice, approval and ongoing regulatory requirements on any shareholder or other party that seeks to acquire direct or indirect "control" of an FDIC-insured depository institution or its holding company. These laws include the BHC Act and the CIBC Act. These laws could delay or prevent an acquisition.

Furthermore, our bylaws provide that the state or federal courts located in Jefferson County, Texas, the county in which Beaumont is located, will be the exclusive forum for: (a) any actual or purported derivative action or proceeding brought on our behalf; (b) any action asserting a claim of breach of fiduciary duty by any of our directors or officers; (c) any action asserting a claim against us or our directors or officers arising pursuant to the Texas Business Organizations Code, our certificate of formation, or our bylaws; or (d) any action asserting a claim against us or our officers or directors that is governed by the internal affairs doctrine. As a shareholder of our Company, you will be deemed to have notice of and have consented to the provisions of our bylaws related to choice of forum. The choice of forum provision in our bylaws may limit our shareholders' ability to obtain a favorable judicial forum for disputes with us. Alternatively, if a court were to find the choice of forum provision contained in our bylaws to be inapplicable or unenforceable in an action, we may incur additional costs associated with resolving such action in other jurisdictions.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

The Bank operates 35 banking locations, all of which are in Texas. The headquarters of the Bank is located at 5999 Delaware Street, Beaumont, Texas 77706 and the telephone number is (409) 861-7200. A majority of the Company's executives are located in Houston at 9 Greenway Plaza, Suite 110, Houston, Texas 77046 and the telephone number is (713) 210-7600. The Bank operates branches in the following Texas locations:

	Number of Branches	Owned	Leased
Houston Market			
Baytown	1	1	
Boling	1	1	_
Crosby	2	2	_
Houston	9	3	6
Humble	1	1	
Pasadena	1	1	
Sugar Land	1	_	1
Tomball	1	1	_
Wharton	1	_	1
The Woodlands	1		1
	19	10	9
Beaumont Market			
Beaumont	4	2	2
Buna	1	1	
Jasper	1	1	_
Kirbyville	1	1	
Lumberton	1	1	
Nederland	1	1	_
Newton	1	1	_
Orange	1	1	_
Port Arthur	1	1	_
Silsbee	1	1	_
Vidor	1	1	_
Woodville	1	1	
	15	13	2
Dallas Market			
Preston Center	1		1
Total	35	23	12

For the leased locations, the Company either leases the location entirely, owns the building and has a ground lease, or owns the drive-in and leases the branch. The Company believes that lease terms for the 12 branches that it leases are generally consistent with prevailing market terms. The expiration dates of the leases range from 2023 to 2045, without consideration of any renewal periods available.

Item 3. Legal Proceedings

We are not currently subject to any material legal proceedings. We are from time to time subject to claims and litigation arising in the ordinary course of business.

At this time, in the opinion of management, the likelihood is remote that the impact of such proceedings, either individually or in the aggregate, would have a material adverse effect on our consolidated results of operations, financial

condition or cash flows. However, one or more unfavorable outcomes in any claim or litigation against us could have a material adverse effect for the period in which they are resolved. In addition, regardless of their merits or their ultimate outcomes, such matters are costly, divert management's attention and may materially and adversely affect our reputation, even if resolved in our favor.

Item 4. Mine Safety Disclosures

Not Applicable.

PART II.

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Market Information for Common Stock

Shares of our common stock are traded on the Nasdaq under the symbol "CBTX".

Holders of Record

As of February 19, 2020, there were approximately 464 holders of record of our common stock. Additionally, a greater number of holders of our common stock are "street name" or beneficial holders, whose shares are held by banks, brokers and other financial institutions.

Securities Authorized for Issuance Under Equity Compensation Plans

Plan Category	Number of Shares to be Issued Upon Exercise of Outstanding Awards	Weighted-Average Exercise Price of Outstanding Awards	Number of Shares Available for Future Grants
Equity compensation plans approved by shareholders ⁽¹⁾ Equity compensation plans not approved by	157,000	\$18.94	1,278,113
shareholders (2)	_		_
Total	157,000	\$18.94	1,278,113

⁽¹⁾ The number of shares available for future issuance includes 314,913 shares available under the Company's 2017 Omnibus Incentive Plan (which allows for the issuance of options, as well as various other stock-based awards) and 963,200 shares available under the Company's 2014 Stock Option Plan.

Unregistered Sales of Equity Securities

None.

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

In July 2019, the Company's Board of Directors authorized a share repurchase program under which the Company may repurchase up to \$40.0 million of the Company's common stock through September 30, 2020. Repurchases under the program may be made from time to time at the Company's discretion in open market transactions, through block trades, in privately negotiated transactions, and pursuant to any trading plan that may be adopted by the Company's management in accordance with Rule 10b5-1 of the Exchange Act of 1934 or otherwise. The timing and actual number of shares repurchased will depend on a variety of factors including price, corporate and regulatory requirements, market conditions, and other corporate liquidity requirements and priorities. The repurchase program does not obligate the Company to acquire a specific dollar amount or number of shares and may be modified, suspended or discontinued at any time. The maximum number of shares that may yet be purchased in the table below relates to this repurchase program. No shares were repurchased under this program during the fourth quarter of 2019.

⁽²⁾ The number of shares to be issued upon exercise of outstanding options, warrants and rights excludes 56,078 options with a weighted-average exercise price of \$11.29 to be issued under a stock option plan the Company assumed in a 2006 acquisition.

The Company's stock compensation plans allow employees to elect to have shares withheld to satisfy their tax liabilities related to options exercised or restricted stock vested or to pay the exercise price of the options. When this settlement method is elected by the employee, the Company repurchases the shares withheld upon vesting of the award stock.

Period	Number of Shares Purchased		Number of Shares Purchased as Part of Publicly Announced Plan	Maximum Number of Shares That May Yet be Purchased Under a Plan at the End of the Period (1)
October 1, 2019 - October 31, 2019	-	-	-	1,396,063
November 1, 2019 - November 30, 2019	6,001	\$ 29.35	-	1,354,919
December 1, 2019 - December 31, 2019	1,475	\$ 29.43	-	1,285,257

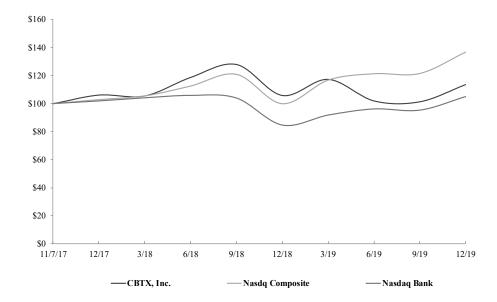
⁽¹⁾ Computed based on the closing share price of the Company's common stock as of the end of the periods shown.

Stock Performance Graph

The following performance graph compares total stockholders' return on our common stock for the period beginning at the close of trading on November 7, 2017 and for each quarter until the end of 2019, with the cumulative total return of the Nasdaq Composite Index and the Nasdaq Bank Index for the same periods. Cumulative total return is computed by dividing the difference between our share price at the end and the beginning of the measurement period by the share price at the beginning of the measurement period. The performance graph assumes \$100 is invested on November 7, 2017, in the Company's common stock, including reinvestment of dividends and October 31, 2017 in the Nasdaq Composite Index and the Nasdaq Bank Index. Historical stock price performance is not necessarily indicative of future stock price performance. This performance graph and related information shall not be deemed "soliciting material" or to be "filed" with the SEC for purposes of Section 18 of the Exchange Act of 1934, or incorporated by reference into any future SEC filing, except as shall be expressly set forth by specific reference in such filing.

Dollars	11/7/17	12/17	3/18	6/18	9/18	12/18	3/19	6/19	9/19	12/19
CBTX, Inc	100.0	106.11	105.50	118.61	127.73	105.84	117.26	101.98	101.40	113.55
Nasdaq Composite	100.0	102.83	105.49	112.47	120.81	99.91	116.71	121.22	119.66	136.58
Nasdaq Bank	100.0	101.91	104.15	105.90	104.01	84.56	91.72	96.17	104.05	105.03

Cumulative Total Return



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Item 6. Selected Financial Data

The following consolidated selected financial data as of and for the five-year period ended December 31, 2019, is derived from our audited financial statements and should be read in conjunction with "Item 7 – Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements and the related notes included elsewhere in this Annual Report on Form 10-K.

As of and for the Years Ended December 31,									
(Dollars in thousands, except per share data)	2019	2018	2017	2016	2015				
Balance Sheet Data:		· <u> </u>							
Cash and equivalents	\$ 372,064	\$ 382,070	\$ 326,199	\$ 382,103	\$ 434,901				
Loans, excluding loans held for sale	2,639,085	2,446,823	2,311,544	2,154,885	2,092,010				
Allowance for loan losses	(25,280)	(23,693)	(24,778)	(25,006)	(25,315)				
Loans, net	2,613,805	2,423,130	2,286,766	2,129,879	2,066,695				
Goodwill and other intangible assets, net	85,888	86,725	87,720	88,741	89,829				
Total assets	3,478,544	3,279,096	3,081,083	2,951,522	2,882,625				
Noninterest-bearing deposits	1,184,861	1,183,058	1,109,789	1,025,425	1,053,957				
Interest-bearing deposits	1,667,527	1,583,224	1,493,183	1,515,335	1,429,409				
Total deposits	2,852,388	2,766,282	2,602,972	2,540,760	2,483,366				
Shareholders' equity	535,721	487,625	446,214	357,637	344,313				
Income Statement Data:									
Interest income	\$ 153,395	\$ 135,759	\$ 116,659	\$ 109,951	\$ 105,525				
Interest expense	17,407	11,098	8,885	8,405	7,654				
Net interest income	135,988	124,661	107,774	101,546	97,871				
Provision (recapture) for loan losses	2,385	(1,756)	(338)	4,575	6,950				
Net interest income after provision (recapture)									
for loan losses	133,603	126,417	108,112	96,971	90,921				
Noninterest income	18,628	14,252	14,204	15,749	14,967				
Noninterest expense	90,143	82,016	78,292	73,502	70,961				
Income before income taxes	62,088	58,653	44,024	39,218	34,927				
Income tax expense	11,571	11,364	16,453	12,010	10,791				
Net income	\$ 50,517	\$ 47,289	\$ 27,571	\$ 27,208	\$ 24,136				
Share and Per Share Data:		· <u> </u>							
Earnings per share - basic	\$ 2.03	\$ 1.90	\$ 1.23	\$ 1.23	\$ 1.07				
Earnings per share - diluted	2.02	1.89	1.22	1.22	1.06				
Dividends per share	0.40	0.20	0.20	0.20	0.20				
Book value per share	21.45	19.58	17.97	16.21	15.44				
Tangible book value per share (1)	18.01	16.10	14.44	12.19	11.41				
Weighted-average common shares									
outstanding- basic	24,926	24,859	22,457	22,049	22,462				
Weighted-average common shares	2-0	0.7.04.0	22.772	22.22.	22.575				
outstanding- diluted	25,053	25,018	22,573	22,235	22,675				
Common shares outstanding at period end	24,980	24,907	24,833	22,062	22,303				

(table continued on next page)

	As of and for the Years Ended December 31,								
(Dollars in thousands, except per share data)	2019	2018	2017	2016	2015				
Performance Ratios:									
Return on average assets	1.50%	1.50%	0.93%	0.94%	0.85%				
Return on average shareholders' equity	9.81%	10.18%	7.18%	7.79%	7.16%				
Net interest margin - tax equivalent basis	4.42%	4.35%	4.06%	3.96%	3.85%				
Efficiency ratio (2)	58.30%	59.04%	64.19%	62.66%	62.89%				
Selected Ratios:									
Loans to deposits	92.52%	88.45%	88.80%	84.81%	84.24%				
Noninterest-bearing deposits to total deposits	41.54%	42.77%	42.64%	40.36%	42.44%				
Cost of total deposits	0.58%	0.40%	0.30%	0.29%	0.26%				
Credit Quality Ratios:									
Nonperforming assets to total assets	0.03%	0.11%	0.27%	0.27%	0.52%				
Nonperforming loans to total loans	0.04%	0.14%	0.33%	0.29%	0.66%				
Allowance for loan losses to nonperforming									
loans	2,587.51%	678.88%	324.06%	400.80%	183.28%				
Allowance for loan losses to total loans	0.96%	0.97%	1.07%	1.16%	1.21%				
Net charge-off (recovery) to average loans	0.03%	(0.03%)		0.23%	0.32%				
Liquidity and Capital Ratios:									
Total shareholders' equity to total assets	15.40%	14.87%	14.48%	12.12%	11.94%				
Tangible equity to tangible assets (1)	13.26%	12.56%	11.98%	9.39%	9.11%				
Common equity tier 1 capital ratio	15.52%	14.71%	14.19%	11.52%	10.89%				
Tier 1 risk-based capital ratio	15.52%	14.76%	14.44%	11.78%	11.16%				
Total risk-based capital ratio	16.41%	15.63%	15.42%	12.85%	12.24%				
Tier 1 leverage ratio	13.11%	12.74%	12.30%	9.78%	9.34%				

⁽¹⁾ Non-GAAP financial measure. See "Non-GAAP Financial Measures" below.

Non-GAAP Financial Measures

The Company's accounting and reporting policies conform to GAAP and the prevailing practices in the banking industry. However, the Company also evaluates its performance based on certain additional non-GAAP financial measures. The Company classifies a financial measure as being a non-GAAP financial measure if that financial measure excludes or includes amounts or is subject to adjustments that have the effect of excluding or including amounts, that are not included or excluded in the most directly comparable measure calculated and presented in accordance with GAAP as in effect from time to time in the U.S. in the statements of income, balance sheets or statements of cash flows. Non-GAAP financial measures do not include operating, other statistical measures or ratios calculated using exclusively financial measures calculated in accordance with GAAP. Non-GAAP financial measures should not be considered in isolation or as a substitute for the most directly comparable or other financial measures calculated in accordance with GAAP. Moreover, the way the Company calculates non-GAAP financial measures may differ from that of other companies reporting measures with similar names.

The Company calculates tangible equity as total shareholders' equity, less goodwill and other intangible assets, net of accumulated amortization, and tangible book value per share as tangible equity divided by shares of common stock outstanding at the end of the relevant period. The most directly comparable GAAP financial measure for tangible book value per share is book value per share.

The Company calculates tangible assets as total assets less goodwill and other intangible assets, net of accumulated amortization. The most directly comparable GAAP financial measure for tangible equity to tangible assets is total shareholders' equity to total assets.

The Company believes that tangible book value per share and tangible equity to tangible assets are measures that are important to many investors in the marketplace who are interested in book value per share and total shareholders' equity to total assets, exclusive of change in intangible assets.

The following table reconciles, as of the dates set forth below, total shareholders' equity to tangible equity, total assets to tangible assets and presents book value per share, tangible book value per share, total shareholders' equity to total assets and tangible equity to tangible assets:

			D	ecember 31,			
(Dollars in thousands, except per share data)	2019	2018		2017	2016		2015
Tangible Equity							
Total shareholders' equity	\$ 535,721	\$ 487,625	\$	446,214	\$ 357,637	\$	344,313
Adjustments:							
Goodwill	80,950	80,950		80,950	80,950		80,950
Other intangibles	 4,938	 5,775		6,770	 7,791		8,879
Tangible equity	\$ 449,833	\$ 400,900	\$	358,494	\$ 268,896	\$	254,484
Tangible Assets	 	 			 	-	
Total assets	\$ 3,478,544	\$ 3,279,096	\$	3,081,083	\$ 2,951,522	\$	2,882,625
Adjustments:							
Goodwill	80,950	80,950		80,950	80,950		80,950
Other intangibles	4,938	5,775		6,770	7,791		8,879
Tangible assets	\$ 3,392,656	\$ 3,192,371	\$	2,993,363	\$ 2,862,781	\$	2,792,796
Common shares outstanding	24,980	24,907		24,833	22,062		22,303
Book value per share	\$ 21.45	\$ 19.58	\$	17.97	\$ 16.21	\$	15.44
Tangible book value per share	\$ 18.01	\$ 16.10	\$	14.44	\$ 12.19	\$	11.41
Total shoraholdara' aquity to total assats	15.40%	14.87%		14.48%	12.12%		11.94%
Total shareholders' equity to total assets							
Tangible equity to tangible assets	13.26%	12.56%		11.98%	9.39%		9.11%

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⁽²⁾ Efficiency ratio is calculated by dividing noninterest expense by the sum of net interest income and noninterest income.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Cautionary Note Regarding Forward-Looking Statements

This Annual Report on Form 10-K contains forward-looking statements. These forward-looking statements reflect the Company's current views with respect to, among other things, future events and our financial performance. These statements are often, but not always, made through the use of words or phrases such as "may," "should," "could," "predict," "potential," "believe," "will likely result," "expect," "continue," "will," "anticipate," "seek," "estimate," "intend," "plan," "projection," "would" and "outlook," or the negative version of those words or other comparable words or phrases of a future or forward-looking nature. These forward-looking statements are not historical facts, and are based on current expectations, estimates and projections about the Company's industry, management's beliefs and certain assumptions made by management, many of which, by their nature, are inherently uncertain and beyond the Company's control. Accordingly, the Company cautions you that any such forward-looking statements are not guarantees of future performance and are subject to risks, assumptions and uncertainties that are difficult to predict. Although the Company believes that the expectations reflected in these forward-looking statements are reasonable as of the date made, actual results may prove to be materially different from the results expressed or implied by the forward-looking statements.

There are or will be important factors that could cause the Company's actual results to differ materially from those indicated in these forward-looking statements, including, but not limited to, the risks described in "Part I – Item 1A. – Risk Factors" and the following:

- natural disasters and adverse weather (including the effects of recent hurricanes, tropical storms and tropical
 depressions on the Company's market area), acts of terrorism, pandemics, an outbreak of hostilities or other
 international or domestic calamities and other matters beyond the Company's control;
- the geographic concentration of the Company's markets in Beaumont and Houston, Texas;
- the Company's ability to prudently manage growth and execute its strategy;
- risks associated with the Company's acquisition and de novo branching strategy, including entry into new markets:
- changes in management personnel;
- the amount of nonperforming and classified assets that the Company holds and the time and effort necessary to resolve nonperforming assets;
- deterioration of asset quality;
- interest rate risk associated with the Company's business;
- business and economic conditions generally and in the financial services industry, nationally and within the Company's primary markets;
- volatility and direction of oil prices and the strength of the energy industry, generally and within Texas;
- the composition of the loan portfolio, including the identity of the Company's borrowers and the concentration of loans in specialized industries;
- changes in the value of collateral securing the Company's loans;
- the Company's ability to maintain important deposit customer relationships and its reputation;
- the Company's ability to maintain effective internal control over financial reporting;
- increased competition in the financial services industry, particularly from regional and national institutions;
- volatility and direction of market interest rates;
- liquidity risks associated with the Company's business;
- systems failures or interruptions involving our information technology and telecommunications systems or third-party servicers;
- interruptions or breaches in the Company's information system security;
- the failure of certain third-party vendors to perform;
- environmental liability associated with the Company's lending activities;
- the institution and outcome of litigation and other legal proceedings against the Company or to which it may become subject;
- repeal of Federal prohibitions on payment of interest on demand deposits;

- the costs and effects of regulatory or other governmental inquiries, the results of regulatory examinations, investigations (including an ongoing FinCEN investigation), or reviews or the ability to obtain required regulatory approvals;
- changes in the laws, rules, regulations, interpretations or policies relating to financial institution, accounting, tax, trade, monetary and fiscal matters;
- further government intervention in the U.S. financial system; and
- other risks, uncertainties, and factors that are discussed from time to time in reports and documents filed with the SEC.

The foregoing factors should not be construed as exhaustive and should be read together with the other cautionary statements included in this Annual Report on Form 10-K. If one or more events related to these or other risks or uncertainties materialize, or if the Company's underlying assumptions prove to be incorrect, actual results may differ materially from what is anticipated. Accordingly, you should not place undue reliance on any such forward-looking statements. Any forward-looking statement speaks only as of the date made and the Company does not undertake any obligation to publicly update or review any forward-looking statement, whether as a result of new information, future developments or otherwise. New factors emerge from time to time and it is not possible to predict which will arise. In addition, the Company cannot assess the impact of each factor on its business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

The following discussion and analysis of the Company's financial condition and results of operations should be read in conjunction with "Item 6. Selected Financial Data" and the consolidated financial statements and the accompanying notes included elsewhere in this Annual Report on Form 10-K. This discussion and analysis includes forward-looking statements that are subject to certain risks and uncertainties and are based on certain assumptions that the Company believes are reasonable but may prove to be inaccurate. Certain risks, uncertainties and other factors, including those set forth in "Item 1A. – Risk Factors" and elsewhere in this Annual Report on Form 10-K, may cause actual results to differ materially from those projected results discussed in the forward-looking statements appearing in this discussion and analysis. The Company assumes no obligation to update any of these forward-looking statements.

Overview

The Company operates through one segment, community banking. The Company's primary source of funds is deposits and primary use of funds is loans. Most of the Company's revenue is generated from interest on loans and investments. The Company incurs interest expense on deposits and other borrowed funds as well as noninterest expense, such as salaries and employee benefits and occupancy expenses.

The Company's operating results depend primarily on net interest income, calculated as the difference between interest income on interest-earning assets, such as loans and securities, and interest expense on interest-bearing liabilities, such as deposits and borrowings. Changes in market interest rates and the interest rates earned on interest-earning assets or paid on interest-bearing liabilities, as well as in the volume and types of interest-earning asset and interest-bearing liabilities, are usually the largest drivers of periodic changes in net interest spread, net interest margin and net interest income. Fluctuations in market interest rates are driven by many factors, including governmental monetary policies, inflation, deflation, macroeconomic developments, changes in unemployment, the money supply, political and international conditions and conditions in domestic and foreign financial markets.

Periodic changes in the volume and types of loans in the Company's loan portfolio are affected by, among other factors, economic and competitive conditions in Texas, as well as developments affecting the real estate, technology, financial services, insurance, transportation, manufacturing and energy sectors within the Company's target markets and throughout the state of Texas. The Company maintains diversity in the loan portfolio as a means of managing risk associated with fluctuations in economic conditions. The Company focuses on lending to small to medium-sized businesses and professionals in its market areas and has a diverse loan portfolio comprised primarily of core relationships. The Company carefully monitors exposure to certain asset classes to minimize the impact of a downturn in the value of such assets.

The Company seeks to remain competitive with respect to interest rates on loans and deposits, as well as prices on fee-based services, which are typically significant competitive factors within the banking and financial services

industry. Many of the Company's competitors are much larger financial institutions that have greater financial resources and compete aggressively for market share. Through the Company's relationship-driven, community banking strategy, a significant portion of its continued growth has been through referral business from existing customers and professionals in the Company's markets including attorneys, accountants and other professional service providers.

The Bank is the subject of an investigation by FinCEN regarding the Bank's compliance with the BSA and antimoney laundering laws and regulations. The Bank is cooperating with this investigation. The costs to respond to and cooperate with FinCEN's investigation have been material over the course of the period of this report, and the Bank may continue to incur material fees and expenses regarding this matter at least through the completion of FinCEN's investigation.

Results of Operations

Year Ended December 31, 2019 vs Year Ended December 31, 2018

Net income for the year ended December 31, 2019 increased 6.8%, compared to the year ended December 31, 2018. This increase is primarily due to increased net interest income and noninterest income, partially offset by a higher provision for loan losses and higher noninterest expense. See further analysis of these fluctuations in the related discussions that follow.

	Years Ended December 31,							
(Dollars in thousands, except per share data and percentages)		2019		2018	Increase (Decrease)			
Interest income	\$	153,395	\$	135,759	\$	17,636	13.0%	
Interest expense		17,407		11,098		6,309	56.8%	
Net interest income		135,988		124,661		11,327	9.1%	
Provision (recapture) for loan losses		2,385		(1,756)		4,141	235.8%	
Noninterest income		18,628		14,252		4,376	30.7%	
Noninterest expense		90,143		82,016		8,127	9.9%	
Income before income taxes		62,088		58,653		3,435	5.9%	
Income tax expense		11,571		11,364		207	1.8%	
Net income	\$	50,517	\$	47,289	\$	3,228	6.8%	
Earnings per share - basic	\$	2.03	\$	1.90				
Earnings per share - diluted		2.02		1.89				
Dividends per share		0.40		0.20				
Return on average assets		1.50%		1.50%				
Return on average shareholders' equity		9.81%		10.18%				
Average shareholders' equity to average assets		15.26%		14.72%				

Net Interest Income

Net interest income for the year ended December 31, 2019 was \$136.0 million, compared to \$124.7 million for the year ended December 31, 2018, an increase of \$11.3 million, or 9.1%. Net interest income increased in 2019, compared to 2018, primarily due to increases in average loan yields and volume, partially offset by increased average rates on interest-bearing deposits and higher average Federal Home Loan Bank advances. Loan growth during 2019 was funded through increased interest-bearing deposits, noninterest-bearing deposits and Federal Home Loan Bank advances. During 2019, the costs of interest-bearing deposits trended upward due to competitive stress on rates but remain a low-cost source of funds, as compared to other sources of funds such as debt.

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The following table presents for the periods indicated, average outstanding balances for each major category of interest-earning assets and interest-bearing liabilities, the interest income or interest expense and the average yield or rate for the periods indicated.

	Years Ended December 31,								
		2018	2018						
		Interest			Interest				
(D. Harris (Lances II)	Average Outstanding	Earned/ Interest	Average Yield/	Average Outstanding	Earned/ Interest	Average Yield/			
(Dollars in thousands)	Balance	Paid	Rate	Balance	<u>Paid</u>	Rate			
Assets									
Interest-earnings assets:	¢ 2 (00 505	¢ 1.41 200	5 420/	¢ 2 202 240	¢ 122 905	£ 100/			
Total loans (1)	\$ 2,608,505	\$ 141,388	5.42%	\$ 2,392,348	\$ 123,895	5.18%			
Securities	233,543	5,954	2.55%	227,384	6,020	2.65%			
Other interest-earning assets	243,349	5,333	2.19%	255,323	5,030	1.97%			
Equity investments	14,852	720	4.85%	15,282	814	5.32%			
Total interest-earning assets	3,100,249	\$ 153,395	4.95%	2,890,337	\$ 135,759	4.70%			
Allowance for loan losses	(24,971)			(25,063)					
Noninterest-earnings assets	299,387			290,868					
Total assets	\$ 3,374,665			\$ 3,156,142					
Liabilities and Shareholders' Equity									
Interest-bearing liabilities:									
Interest-bearing deposits	\$ 1,566,038	\$ 15,999	1.02%	\$ 1,519,643	\$ 10,586	0.70%			
Federal Home Loan Bank advances	61,589	1,386	2.25%	3,356	73	2.18%			
Repurchase agreements	1,046	3	0.29%	1,601	4	0.25%			
Note payable and junior subordinated debt		19		10,572	435	4.11%			
Total interest-bearing liabilities	1,628,673	\$ 17,407	1.07%	1,535,172	\$ 11,098	0.72%			
Noninterest-bearing liabilities:									
Noninterest-bearing deposits	1,193,527			1,134,191					
Other liabilities	37,458			22,082					
Total noninterest-bearing liabilities	1,230,985			1,156,273					
Shareholders' equity	515,007			464,697					
Total liabilities and shareholders' equity	\$ 3,374,665			\$ 3,156,142					
Net interest income	4 0,0 1,000	\$ 135,988		+ +,,	\$ 124,661				
		ψ 133,700	3.88%		ψ 12 4,001	3.98%			
Net interest spread ⁽²⁾			4.39%			4.31%			
						_			
Net interest margin—tax equivalent (4)			4.42%			4.35%			

⁽¹⁾ Includes average outstanding balances of loans held for sale.

⁽²⁾ Net interest spread is the average yield on interest-earning assets minus the average rate on interest-bearing liabilities.

⁽³⁾ Net interest margin is equal to net interest income divided by average interest-earning assets.

⁽⁴⁾ Tax equivalent adjustments of \$1.0 million and \$1.1 million for the years ended December 31, 2019 and 2018, respectively, have been computed using a federal income tax rate of 21%.

The following tables present information regarding changes in interest income and interest expense for the periods indicated for each major component of interest-earning assets and interest-bearing liabilities and distinguishes between the changes attributable to changes in volume and changes attributable to changes in interest rates. For purposes of these tables, changes attributable to both rate and volume that cannot be segregated have been allocated to rate.

	Year Ended December 31, 2019, Compared to Year Ended December 31, 2018									
		Increase (Dec	crease)	due to						
(Dollars in thousands)		Rate		Volume	Total					
Interest-earning assets:										
Total loans	\$	6,299	\$	11,194	\$	17,493				
Securities		(230)		164		(66)				
Other interest-earning assets		540		(237)		303				
Equity investments		(71)		(23)		(94)				
Total increase in interest income		6,538		11,098		17,636				
Interest-bearing liabilities:	-									
Interest-bearing deposits		5,090		323		5,413				
Federal Home Loan Bank advances		46		1,267		1,313				
Repurchase agreements		_		(1)		(1)				
Note payable and junior subordinated debt		_		(416)		(416)				
Total increase in interest expense		5,136		1,173		6,309				
Increase in net interest income	\$	1,402	\$	9,925	\$	11,327				

Provision for Loan Losses

The provision (recapture) for loan losses is an income adjustment used to maintain an allowance for loan losses at a level deemed appropriate by management to absorb inherent losses on existing loans. The provision for loan loss was \$2.4 million for 2019, compared to a recapture of \$1.8 million for 2018. The provision in 2019 resulted from increases in loans during that period. The recapture in 2018 resulted from strong credit quality, continuing low nonperforming and impaired loans, minimal charge-off history and an increase in recoveries during the year. For a description of the factors considered by our management in determining the allowance for loan losses see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Financial Condition— Allowance for Loan Losses."

Noninterest Income

During the year ended December 31, 2019, noninterest income increased \$4.4 million, compared to the year ended December 31, 2018, primarily due to increased earnings on bank-owned life insurance and increased swap origination fees. See further analysis of these fluctuations in the related discussions that follow.

	Years Ended December 31,										
(Dollars in thousands)		2019		2018		rease)					
Deposit account service charges	\$	6,554	\$	6,281	\$	273	4.3%				
Net gain on sale of assets		652		660		(8)	(1.2%)				
Card interchange fees		3,720		3,741		(21)	(0.6%)				
Earnings on bank-owned life insurance		5,011		1,815		3,196	176.1%				
Other		2,691		1,755		936	53.3%				
Total noninterest income	\$	18,628	\$	14,252	\$	4,376	30.7%				

Deposit Account Service Charges. Service charges on deposit accounts increased in the year ended December 31, 2019, compared to the year ended December 31, 2018, predominately due to an increase in non-sufficient and account analysis charges incurred by the Company's deposit customers.

Earnings on Bank-Owned Life Insurance. The Company has purchased life insurance policies on certain employees, that are carried at their cash surrender value on the consolidated balance sheet and changes in the cash surrender value of the policies are recorded in noninterest income. Earnings on bank-owned life insurance increased \$3.2 million,

during the year ended December 31, 2019, compared to the year ended December 31, 2018, due to nontaxable death benefit proceeds of \$4.7 million received under bank-owned life insurance policies. The Company recorded a gain of \$3.3 million over the carrying value during the year ended December 31, 2019.

Other. This category includes a variety of other income-producing activities, including partnership and investment fund income, other loan fees, swap origination charges, wire transfer fees, credit card program income and fee income. Other noninterest income increased during the year ended December 31, 2019, compared to the year ended December 31, 2018, primarily due to an increase of \$832,000 in swap origination fee income.

Noninterest Expense

Generally, noninterest expense is composed of employee expenses and costs associated with operating facilities, obtaining and retaining customer relationships and providing bank services. For the year ended December 31, 2019, compared to the year ended December 31, 2018, noninterest expense increased \$8.1 million, primarily due to increased salaries and employee benefits and professional and director fees, partially offset by decreased regulatory fees. See further analysis of these fluctuations in the related discussions that follow.

	Years Ended December 31,								
(Dollars in thousands)		2019		2018		Increase (D	ecrease)		
Salaries and employee benefits	\$	56,222	\$	51,524	\$	4,698	9.1%		
Net occupancy expense		9,506		9,394		112	1.2%		
Regulatory fees		1,138		2,053		(915)	(44.6%)		
Data processing		2,678		2,677		1	0.0%		
Software		1,757		1,576		181	11.5%		
Printing, stationery and office		1,302		1,161		141	12.1%		
Amortization of intangibles		894		985		(91)	(9.2%)		
Professional and director fees		7,048		3,537		3,511	99.3%		
Correspondent bank and customer related expense		268		265		3	1.1%		
Loan processing		445		448		(3)	(0.7%)		
Advertising, marketing and business development		1,831		1,824		7	0.4%		
Repossessed real estate and other assets		1		72		(71)	(98.6%)		
Security and protection expense		1,464		1,276		188	14.7%		
Telephone and communications		1,774		1,530		244	15.9%		
Other expense		3,815		3,694		121	3.3%		
Total noninterest expense	\$	90,143	\$	82,016	\$	8,127	9.9%		

Salaries and Employee Benefits. Salaries and benefits increased \$4.7 million during the year ended December 31, 2019, compared to the year ended December 31, 2018, as a result of annual salary increases in 2019, increased bonus expense and increased stock compensation expense due to restricted stock grants.

Regulatory Fees. Regulatory fees decreased \$915,000 during 2019, compared to 2018, primarily due to an FDIC deposit assessment credit received in 2019.

Professional and Director Fees. Professional and director fees include legal, audit, loan review and consulting fees. The increase in professional and director fees of \$3.5 million during the year ended December 31, 2019, compared to the year ended December 31, 2018, was primarily due to increased legal fees incurred in the Bank's response and cooperation with an investigation by FinCEN regarding the Bank's compliance with the BSA and anti-money laundering laws and regulations. The Bank incurred legal fees related to this investigation of \$3.7 million and \$193,000 during the years ended December 31, 2019 and 2018, respectively.

Income Tax Expense

The amount of income tax expense is impacted by the amounts of pre-tax income, tax-exempt income and other nondeductible expenses. Deferred tax assets and liabilities are reflected at current income tax rates in effect for the period in which the deferred tax assets and liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

Income tax expense and effective tax rates for the periods shown below were as follows:

	Years Ended December 31,						
(Dollars in thousands)		2019		2018			
Income tax expense	\$	11,571	\$	11,364			
Effective tax rate		18.64%		19.37%			

For 2019, the difference between the federal statutory rate of 21% and the effective tax rates presented in the table above was largely attributable to the non-taxable gain related to bank-owned life insurance and the effective tax rates for both 2019 and 2018 were impacted by tax exempt interest income. See "Item 8—Financial Statements and Supplementary Data—Note 21."

Year Ended December 31, 2018 vs Year Ended December 31, 2017

Net income for 2018 was \$47.3 million compared to \$27.6 million for 2017, an increase of \$19.7 million, or 71.5%. This increase is primarily due to a \$16.9 million increase in net interest income and a \$5.1 million decrease in income taxes, partially offset by a \$3.7 million increase in noninterest expense.

See further analysis of these fluctuations in the related discussions that follow.

	Years Ended December 31,										
(Dollars in thousands, except per share data)	2018			2017		Increase (Decrease)					
Interest income	\$	135,759	\$	116,659	\$	19,100	16.4%				
Interest expense		11,098		8,885		2,213	24.9%				
Net interest income		124,661		107,774		16,887	15.7%				
Provision (recapture) for loan losses		(1,756)		(338)		(1,418)	419.5%				
Noninterest income		14,252		14,204		48	0.3%				
Noninterest expense		82,016		78,292		3,724	4.8%				
Income before income taxes		58,653		44,024		14,629	33.2%				
Income tax expense		11,364		16,453		(5,089)	(30.9%)				
Net income	\$	47,289	\$	27,571	\$	19,718	71.5%				
Earnings per share - basic	\$	1.90	\$	1.23	\$	0.67					
Earnings per share - diluted	\$	1.89	\$	1.22	\$	0.67					

Net Interest Income

Net interest income for the year ended December 31, 2018 was \$124.7 million, compared to \$107.8 million for the year ended December 31, 2017, an increase of \$16.9 million, or 15.7%. Interest income increased in 2018, as compared to 2017, due to higher average loans and securities and higher average yields on loans, securities and federal funds sold. Interest expense increased in 2018, as compared to 2017, due to higher average interest-bearing deposits and higher rates on interest-bearing deposits, offset by lower interest expense in 2018 due to the payoff of our note payable in the fourth quarter of 2017. Increases in rates on interest-earning assets increased net interest income by \$10.1 million and increased rates paid on interest-bearing liabilities decreased net interest income by \$3.0 million for the year December 31, 2018, compared to the year ended December 31, 2017.

The following table presents for the periods indicated, average outstanding balances for each major category of interest-earning assets and interest-bearing liabilities, the interest income or interest expense and the average yield or rate for the periods indicated.

V F L L D L 21

Years Ended December 31,								
	'-	2018			2017			
		Interest			Interest			
	Average	Earned/	Average	Average	Earned/	Average		
	Outstanding	Interest	Yield/	Outstanding	Interest	Yield/		
(Dollars in thousands)	Balance	Paid	Rate	Balance	Paid	Rate		
Assets								
Interest-earnings assets:								
Total loans (1)	\$ 2,392,348	\$ 123,895	5.18%	\$ 2,206,541	\$ 107,368	4.87%		
Securities	227,384	6,020	2.65%	220,953	5,347	2.42%		
Other interest-earning assets	255,323	5,030	1.97%	272,715	3,204	1.17%		
Equity investments	15,282	814	5.32%	14,692	740	5.04%		
Total interest-earning assets	2,890,337	\$ 135,759	4.70%	2,714,901	\$ 116,659	4.30%		
Allowance for loan losses	(25,063)			(25,319)				
Noninterest-earnings assets	290,868			284,165				
Total assets	\$ 3,156,142			\$ 2,973,747				
Liabilities and Shareholders' Equity								
Interest-bearing liabilities:								
Interest-bearing deposits	\$ 1,519,643	\$ 10,586	0.70%	\$ 1,503,350	\$ 7,652	0.51%		
Federal Home Loan Bank advances	3,356	73	2.18%	_	_	_		
Repurchase agreements	1,601	4	0.25%	2,254	5	0.27%		
Note payable and junior subordinated debt	10,572	435	4.11%	32,990	1,228	3.72%		
Total interest-bearing liabilities	1,535,172	\$ 11,098	0.72%	1,538,594	\$ 8,885	0.58%		
Noninterest-bearing liabilities:								
Noninterest-bearing deposits	1,134,191			1,031,707				
Other liabilities	22,082			19,388				
Total noninterest-bearing liabilities	1,156,273			1,051,095				
Shareholders' equity	464,697			384,058				
Total liabilities and shareholders' equity	\$ 3,156,142			\$ 2,973,747				
Net interest income		\$ 124,661			\$ 107,774			
Net interest spread (2)			3.98%			3.72%		
Net interest margin (3)			4.31%			3.97%		
Net interest margin—tax equivalent (4)			4.35%			4.06%		

⁽¹⁾ Includes average outstanding balances of loans held for sale.

⁽²⁾ Net interest spread is the average yield on interest-earning assets minus the average rate on interest-bearing liabilities.

⁽³⁾ Net interest margin is equal to net interest income divided by average interest-earning assets.

⁽⁴⁾ Tax equivalent adjustments of \$1.1 million and \$2.3 million for the years ended December 31, 2018 and 2017, respectively, have been computed using a federal income tax rate of 21% for 2018 and 35% for 2017.

The following table presents information regarding the changes in interest income and interest expense for the periods indicated for each major component of interest-earning assets and interest-bearing liabilities and distinguishes between the changes attributable to changes in volume and changes attributable to changes in interest rates. For purposes of this table, changes attributable to both rate and volume that cannot be segregated have been allocated to rate.

Year Ended December 31,

106

7,120

73

(1)

(793)

16,887

73

(1)

(899)

9,767

	2018 Compared to 2017										
]	Increase (De									
(Dollars in thousands)		Volume		Rate		Total					
Interest-earning assets:											
Total loans	\$	9,041	\$	7,486	\$	16,527					
Securities		156		517		673					
Other interest-earning assets		(204)		2,030		1,826					
Equity investments		30		44		74					
Total increase in interest income		9,023		10,077		19,100					
Interest-bearing liabilities:											
Interest-bearing deposits		83		2,851		2,934					

Provision for Loan Losses

Note payable and junior subordinated debt

Provision (recapture) for loan losses is an income adjustment used to maintain an allowance for loan losses at a level management deems appropriate to absorb inherent losses on existing loans. For the year ended December 31, 2018, the recapture of \$1.8 million was due to strong credit quality, continuing low nonperforming and impaired loans, minimal charge-off history and an increase in recoveries during the year. A recapture of \$338,000 was recorded for the year ended December 31, 2017, primarily due to the pay-offs of certain classified and problem loans and the resulting reversal of their related allowance for loan losses. For a description of the factors considered by our management in determining the allowance for loan losses see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Financial Condition—Allowance for Loan Losses."

Noninterest Income

Noninterest income increased minimally between 2018 and 2017, although there were increases in deposit account service charges, card interchange fees and earnings on bank-owned life insurance, partially offset by decreased gains on sales of fixed assets. The major categories of noninterest income for the periods indicated below were as follows:

	For the Years Ended December 31,										
(Dollars in thousands)		2018		2017	Increase (Decrease)						
Noninterest income:											
Deposit account service charges	\$	6,281	\$	5,800	\$	481	8.3%				
Net gain on sale of assets		660		1,524		(864)	(56.7%)				
Card interchange fees		3,741		3,453		288	8.3%				
Earnings on bank-owned life insurance		1,815		1,580		235	14.9%				
Other		1,755		1,847		(92)	(5.0%)				
Total noninterest income	\$	14,252	\$	14,204	\$	48	0.3%				

Deposit Account Service Charges. We earn fees from our customers for deposit-related services and these fees are a significant component of our noninterest income. Service charges on deposit accounts were \$6.3 million for the year ended December 31, 2018, an increase of \$481,000, or 8.3%, over the same period in 2017. This increase was predominately due to an increase in non-sufficient and overdraft charges incurred by our deposit customers.

Net Gain on Sale of Assets. Net gain on sale of assets consists of the gains associated with the sale of fixed assets, Small Business Association, or SBA, loans, mortgage loans and other assets. Net gain on sale of assets was \$660,000 for the year ended December 31, 2018, a decrease of \$864,000, or 56.7%, over the same period in 2017. Net gains on sale of assets for the year ended December 31, 2018, primarily related to sales of SBA and mortgage loans. Net gain on sale of assets for the year ended December 31, 2017, primarily related to the settlement of a legal matter related to one of our branches and the sale of certain assets of two branches in 2017.

Card Interchange Fees. We earn card interchange fees from merchants as issuer of debit cards. Card interchange fees increased \$288,000 for the year ended December 31, 2018, compared to the year ended December 31, 2017, due to an increase in the volume of such transactions.

Earnings on Bank-owned Life Insurance. The Company has purchased life insurance policies on certain employees, which are carried at their cash surrender value. Changes in the cash surrender value of the policies are recorded in noninterest income. Earnings on bank-owned life insurance increased \$235,000 during the year ended December 31, 2018, compared to the year ended December 31, 2017, primarily due to the impact of purchases of additional policies in the first quarter of 2018.

Noninterest Expense

Generally, noninterest expense is composed of employee expenses and costs associated with operating our facilities, obtaining and retaining customer relationships and providing bank services. For the year ended December 31, 2018, noninterest expense totaled \$82.0 million, an increase of \$3.7 million, or 4.8%, compared to \$78.3 million for the year ended December 31, 2017. The major categories of noninterest expense for the periods indicated were as follows:

	For the Years Ended December 31,							
(Dollars in thousands)	2018	2017	Increase (De	ecrease)				
Noninterest expense:								
Salaries and employee benefits	\$ 51,524	\$ 48,573	\$ 2,951	6.1%				
Net occupancy expense	9,394	9,151	243	2.7%				
Regulatory fees	2,053	2,176	(123)	(5.7%)				
Data processing	2,677	2,629	48	1.8%				
Software	1,576	1,208	368	30.5%				
Printing, stationery and office	1,161	1,097	64	5.8%				
Amortization of intangibles	985	1,079	(94)	(8.7%)				
Professional and director fees	3,537	3,105	432	13.9%				
Correspondent bank and customer related expense	265	286	(21)	(7.3%)				
Loan processing	448	461	(13)	(2.8%)				
Advertising, marketing and business development	1,824	1,461	363	24.8%				
Repossessed real estate and other assets	72	609	(537)	(88.2%)				
Security and protection expense	1,276	1,355	(79)	(5.8%)				
Telephone and communications	1,530	1,316	214	16.3%				
Other expense	3,694	3,786	(92)	(2.4%)				
Total noninterest expense	\$ 82,016	\$ 78,292	\$ 3,724	4.8%				

Salaries and Employee Benefits. The increase in salaries and employee benefit expenses during the year ended December 31, 2018, as compared to the year ended December 31, 2017, was primarily due to increases in salaries, bonuses and stock compensation expense during 2018, partially offset by the impact of a change in control charge of \$2.5 million related to our initial public offering recorded in 2017. Salaries increased in 2018, as compared to 2017, primarily due to annual salary increases and the hiring of additional officer level employees. Stock compensation expense increased in 2018, as compared to 2017, due to the issuance of restricted stock awards during the fourth quarter of 2017 to executives, officers and other key individuals in conjunction with our initial public offering.

Net Occupancy Expenses. Net occupancy expenses were \$9.4 million and \$9.2 million for the year ended December 31, 2018 and 2017, respectively. Although we sold two branches in the third quarter of 2017, costs for repairs and maintenance and other costs related to occupancy increased in 2018.

Software. Software related expenses increased \$368,000 during the year ended December 31, 2018, as compared to the year ended December 31, 2017, primarily due to increases in software licenses.

Professional and Director Fees. Professional and director fees, which include legal, audit, loan review and consulting fees, were \$3.5 million and \$3.1 million for the year ended December 31, 2018 and 2017, respectively. The increase of \$432,000 for the year ended December 31, 2018, compared to the year ended December 31, 2017, is primarily due to increased legal, audit and consulting fees.

Professional and director fees include expenditures relating to a security incident involving the possible unauthorized access of certain personal information in the possession of the Bank. Based on a report of an independent forensic investigation firm, we believe that a phishing incident occurred where certain emails and attachments from two employee email accounts may have been accessed by an unauthorized person. We believe that these email accounts contained certain personal information for approximately 7,800 individuals. We stopped the identified unauthorized access and we contacted such individuals and reported the incident to law-enforcement authorities. Our investigation did not find any evidence that the incident involved any unauthorized access to or use of any of the Bank's internal computer systems or network, and we believe that the access was limited to information that was contained in the email accounts of the two employees. We incurred total out-of-pocket expenses of \$65,000 during 2018 related to this incident.

Advertising and Marketing Expenses. Advertising and promotion-related expenses were \$1.8 million and \$1.5 million for the year ended December 31, 2018 and 2017, respectively. The increase in 2018 was primarily due to an increase in media costs associated with the Company's branding campaign that began early in the second quarter of 2017 and continued into 2018.

Repossessed Real Estate and Other Assets. Costs related to repossessed real estate and other assets decreased \$537,000, or 88.2%, during the year ended December 31, 2018, as compared to the year ended December 31, 2017. The decrease was due to a reduction in the number of repossessed and other assets in 2018, as compared to 2017, and a resulting decrease in related costs.

Telephone and Communications. Telephone and communication costs increased \$214,000 during 2018, as compared to 2017, primarily due to increased equipment costs and monthly fees.

Income Tax Expense

The amount of income tax expense we incur is impacted by the amounts of our pre-tax income, tax-exempt income and other nondeductible expenses. Deferred tax assets and liabilities are reflected at current income tax rates in effect for the period in which the deferred tax assets and liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

For the years ended December 31, 2018 and 2017, income tax expense totaled \$11.4 million and \$16.5 million and our effective tax rate for those periods was 19.4% and 37.4%, respectively. The decrease in tax expense for the year ended December 31, 2018, compared to the year ended December 31, 2017, is due to the Tax Cuts and Jobs Act of 2017, or Tax Act, which was effective January 1, 2018. The Tax Act lowered the corporate federal income tax rate in the U.S. from 35% to 21%. As a result, we recorded a deferred tax asset remeasurement adjustment of \$3.9 million in 2017 to

reflect the impact of this rate change. The tax rate for 2017 would have been 28.6% without the impact of the deferred tax remeasurement adjustment. See "Item 8—Financial Statements and Supplementary Data—Note 21."

Financial Condition

Total assets were \$3.5 billion as of December 31, 2019, compared to \$3.3 billion as of December 31, 2018, an increase of \$199.4 million, primarily due to an increase in loans, excluding loans held for sale, of \$192.3 million and a \$12.9 million increase due to operating lease right-to-use assets, partially offset by a \$10.0 million decrease in cash and cash equivalents.

Total liabilities increased \$151.4 million, primarily due to a \$50.0 million increase in Federal Home Loan Bank advances, a \$86.1 million increase in deposits and an increase of \$15.7 million due to operating lease liabilities.

Operating lease right-to-use assets and operating lease liabilities were added due to the implementation of the new lease accounting standard. See "Item 8—Financial Statements and Supplementary Data—Note 16" for further discussion of the new lease accounting standard. See further analysis of the other changes in the related discussions that follow.

Loan Portfolio

At December 31, 2019, loans, excluding loans held for sale, were \$2.6 billion, an increase of \$192.3 million, or 7.9%, compared to \$2.5 billion at December 31, 2018. The increase in loans was primarily due to organic growth and increased capital needs of existing customers.

The loan portfolio by loan class as of the dates indicated was as follows:

December 31,									
(Dollars in thousands)		2019		2018		2017		2016	2015
Commercial and industrial	\$	527,607	\$	519,779	\$	559,363	\$	511,554	\$ 504,750
Real estate:									
Commercial real estate		900,746		795,733		738,293		697,794	693,421
Construction and development		527,812		515,533		449,211		491,626	451,219
1-4 family residential		280,192		282,011		258,584		236,882	217,301
Multi-family residential		277,209		221,194		220,305		133,210	114,366
Consumer		36,782		39,421		40,433		39,694	41,006
Agricultural		9,812		11,076		11,256		11,106	12,737
Other		86,513		68,382		40,344		38,180	64,452
Gross loans		2,646,673		2,453,129		2,317,789		2,160,046	 2,099,252
Less deferred fees and unearned									
discount		(6,125)		(6,306)		(4,785)		(4,548)	(5,680)
Less loans held for sale		(1,463)				(1,460)		(613)	 (1,562)
Loans, excluding loans held for sale	\$	2,639,085	\$	2,446,823	\$	2,311,544	\$	2,154,885	\$ 2,092,010

Credit Policies and Risk Management

The Company has lending policies and procedures in place that are designed to maximize loan income within an acceptable level of risk. The Company has centralized and thorough loan underwriting guidelines, maintains a diversified loan portfolio and has highly experienced credit officers and credit analysts.

The Company's credit culture actively supports the extension of credit based on sound, fundamental lending principles and selectively extending credit to establish long-term relationships with customers. The Company's credit officers are involved in the underwriting, structuring and pricing process at inception of the lending opportunity and remain involved through approval. The Company believes that the credit approval process provides for thorough underwriting and efficient decision-making. Most of the Company's commercial loans have personal guarantees. Substantially all the Company's loans are made to borrowers with whom the Company has ongoing relationships and are located or operating in the Company's primary market areas. The Company's reporting system provides management and the Board of Directors with frequent reports related to loan production, loan quality, concentrations of credit, loan delinquencies and

nonperforming and potential problem loans. The Company actively manages the composition of the loan portfolio, including credit concentrations. Management administers a risk-based approach to effectively identify, measure, monitor, mitigate, control and manage concentration risks.

The contractual maturity ranges of loans in the loan portfolio and loans with fixed and variable interest rates in each maturity range as of date indicated were as follows:

(Dollars in thousands)	1 Year or Less	1 Year Through 5 Years		After 5 Years		Total
December 31, 2019	 					
Commercial and industrial	\$ 280,806	\$	218,921	\$	27,880	\$ 527,607
Real estate:						
Commercial real estate	111,814		591,833		197,099	900,746
Construction and development	150,054		323,800		53,958	527,812
1-4 family residential	13,809		42,310		224,073	280,192
Multi-family residential	73,860		16,774		186,575	277,209
Consumer	24,407		12,137		238	36,782
Agricultural	8,502		1,310			9,812
Other	21,492		63,238		1,783	86,513
Gross loans	\$ 684,744	\$	1,270,323	\$	691,606	\$ 2,646,673
Fixed rate loans	\$ 177,631	\$	759,115	\$	300,661	\$ 1,237,407
Variable rate loans	507,113		511,208		390,945	1,409,266

Nonperforming Assets

Nonperforming assets include nonaccrual loans, loans that are accruing over 90 days past due and foreclosed assets. Generally, loans are placed on nonaccrual status when they become more than 90 days past due and/or the collection of principal or interest is in doubt.

The components of nonperforming assets as of the dates indicated were as follows:

	December 31,										
(Dollars in thousands)	2019	2018	2017	2016	2015						
Nonaccrual loans	\$ 977	\$ 3,490	\$ 7,646	\$ 6,239	\$ 13,722						
Accruing loans 90 or more days past due					90						
Total nonperforming loans	977	3,490	7,646	6,239	13,812						
Foreclosed assets		12	705	1,861	1,092						
Total nonperforming assets	\$ 977	\$ 3,502	\$ 8,351	\$ 8,100	\$ 14,904						
Total assets	\$ 3,478,544	\$ 3,279,096	\$ 3,081,083	\$ 2,951,522	\$ 2,882,625						
Loans, excluding loans held for sale	2,639,085	2,446,823	2,311,544	2,154,885	2,092,010						
Allowance for loan losses	25,280	23,693	24,778	25,006	25,315						
Nonaccrual loans to loans, excluding loans											
held for sale	0.04%	0.14%	0.33%	0.29%	0.66%						
Allowance for loan losses to nonaccrual loans	2,587.51%	678.88%	324.06%	400.80%	184.48%						
Nonperforming loans to loans, excluding loans											
held for sale	0.04%	0.14%	0.33%	0.29%	0.66%						
Nonperforming assets to total assets	0.03%	0.11%	0.27%	0.27%	0.52%						

Risk Gradings

As part of the on-going monitoring of the credit quality of the Company's loan portfolio and methodology for calculating the allowance for loan losses, management assigns and tracks loan grades, as described below, that are used as credit quality. See descriptions of the risk grades in "Item 8—Financial Statements and Supplementary Data—Note 6."

The internal ratings of loans as of the dates indicated were as follows:

		_	,	Special				
(Dollars in thousands)		Pass		Mention		Substandard		Total
December 31, 2019	Ф	512 417	Ф	2.062	Φ	11 007	Ф	507 607
Commercial and industrial	\$	513,417	\$	2,963	\$	11,227	\$	527,607
Real estate:								
Commercial real estate		876,207		18,570		5,969		900,746
Construction and development		515,247		12,565		_		527,812
1-4 family residential		274,731		594		4,867		280,192
Multi-family residential		277,209		_		_		277,209
Consumer		36,566		_		216		36,782
Agricultural		9,733		50		29		9,812
Other		79,860				6,653		86,513
Gross loans	\$	2,582,970	\$	34,742	\$	28,961	\$	2,646,673
				Special				
(Dollars in thousands)		Pass		Special Mention	Su	bstandard_		Total
(Dollars in thousands) December 31, 2018		Pass			Su	<u>bstandard</u>		Total
		Pass 504,425			<u>Su</u> \$	bstandard 9,586		Total 519,779
December 31, 2018	\$			Mention		_	\$	
December 31, 2018 Commercial and industrial	\$			Mention		_	\$	
December 31, 2018 Commercial and industrial	\$	504,425		<u>Mention</u> 5,768		9,586	\$	519,779
December 31, 2018 Commercial and industrial Real estate: Commercial real estate. Construction and development	\$	504,425 781,035		5,768 10,370 4,204		9,586	\$	519,779 795,733
December 31, 2018 Commercial and industrial Real estate: Commercial real estate. Construction and development 1-4 family residential.	\$	504,425 781,035 511,329 274,781		5,768 10,370		9,586 4,328	\$	519,779 795,733 515,533 282,011
December 31, 2018 Commercial and industrial Real estate: Commercial real estate. Construction and development	\$	504,425 781,035 511,329 274,781 221,194		5,768 10,370 4,204		9,586 4,328	\$	519,779 795,733 515,533 282,011 221,194
December 31, 2018 Commercial and industrial Real estate: Commercial real estate. Construction and development 1-4 family residential. Multi-family residential. Consumer.	\$	504,425 781,035 511,329 274,781 221,194 39,140		5,768 10,370 4,204 2,175		9,586 4,328 5,055	\$	519,779 795,733 515,533 282,011 221,194 39,421
December 31, 2018 Commercial and industrial Real estate: Commercial real estate. Construction and development 1-4 family residential. Multi-family residential. Consumer. Agricultural.	\$	504,425 781,035 511,329 274,781 221,194 39,140 11,048		5,768 10,370 4,204 2,175		9,586 4,328 5,055	\$	519,779 795,733 515,533 282,011 221,194 39,421 11,076
December 31, 2018 Commercial and industrial Real estate: Commercial real estate. Construction and development 1-4 family residential. Multi-family residential. Consumer.	\$ \$	504,425 781,035 511,329 274,781 221,194 39,140		5,768 10,370 4,204 2,175		9,586 4,328 5,055 35	\$ \$	519,779 795,733 515,533 282,011 221,194 39,421

Allowance for Loan Losses

The Company maintains an allowance for loan losses that represents management's best estimate of the loan losses and risks inherent in the loan portfolio. The amount of the allowance for loan losses should not be interpreted as an indication that charge-offs in future periods will necessarily occur in those amounts. In determining the allowance for loan losses, the Company estimates losses on specific loans, or groups of loans, where the probable loss can be identified and reasonably determined. The balance of the allowance for loan losses is based on internally assigned risk classifications of loans, historical loan loss rates, changes in the loan portfolio, overall portfolio quality, industry concentrations, delinquency trends, current economic factors and the estimated impact of current economic conditions on certain historical loan loss rates. See "Management's Discussion and Analysis of Financial Condition and Results of Operations —Critical Accounting Policies—Loans and Allowance for Loan Losses" and "Item 8—Financial Statements and Supplementary Data—Note 1."

In reviewing the loan portfolio, the Company considers risk elements applicable to particular loan types or categories to assess the quality of individual loans. Some of the risk elements considered include:

<u>Commercial and industrial loans</u>—the debt service coverage ratio (income from the business in excess of operating expenses compared to loan repayment requirements), the operating results of the commercial, industrial or professional enterprise, the borrower's business, professional and financial ability and expertise, the specific risks and volatility of income and operating results typical for businesses in that category and the value, nature and marketability of collateral;

<u>Commercial real estate loans and multi-family residential loans</u>—the debt service coverage ratio, operating results of the owner in the case of owner-occupied properties, the loan-to-value ratio, the age and condition of the collateral and the volatility of income, property value and future operating results typical of properties of that type;

<u>1-4 family residential mortgage loans</u>—the borrower's ability to repay the loan, including a consideration of the debt-to-income ratio and employment and income stability, the loan-to-value ratio and the age, condition and marketability of the collateral; and

<u>Construction and development loans</u>—the perceived feasibility of the project including the ability to sell developed lots or improvements constructed for resale or the ability to lease property constructed for lease, the quality and nature of contracts for presale or prelease, if any, experience and ability of the developer and loan-to-value ratio.

Activity in the allowance for loan losses for the periods indicated was as follows:

	Years Ended December 31,					
(Dollars in thousands)	2019	2018	2017	2016	2015	
Allowance for loan losses at beginning of						
period	\$ 23,693	\$ 24,778	\$ 25,006	\$ 25,315	\$ 24,952	
Provision for loan losses	2,385	(1,756)	(338)	4,575	6,950	
Charge-offs:						
Commercial and industrial	1,252	1,928	904	4,884	7,210	
Real estate:						
Commercial real estate	45	171	120	589	27	
Construction and development		1		_	_	
1-4 family residential	12	4	8	3	263	
Consumer	97	1	93	277	102	
Agricultural		_		267	_	
Other	52	3		59		
Total charge-offs	1,458	2,108	1,125	6,079	7,602	
Recoveries:						
Commercial and industrial	489	2,737	1,110	1,010	524	
Real estate:						
Commercial real estate	81	20	9	108	289	
1-4 family residential	3	6	13	6	142	
Consumer	71	3	43	45	60	
Agricultural	10	10	52	26	_	
Other	6	3	8			
Total recoveries	660	2,779	1,235	1,195	1,015	
Net (charge-offs) recoveries	(798)	671	110	(4,884)	(6,587)	
Allowance for loan losses	\$ 25,280	\$ 23,693	\$ 24,778	\$ 25,006	\$ 25,315	
Loans, excluding loans held for sale	\$ 2,639,085	\$ 2,446,823	\$ 2,311,544	\$ 2,154,885	\$ 2,092,010	
Total average loans	2,608,505	2,392,348	2,206,541	2,140,917	2,068,827	
Allowance for loan losses to loans,	, ,	, ,	, ,-	, -,	, , .	
excluding loans held for sale	0.96%	0.97%	1.07%	1.16%	1.21%	
Net charge-offs (recoveries) to total						
average loans	0.03%	(0.03%)		0.23%	0.32%	
5		, ,				

See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Year Ended December 31, 2019 vs Year Ended December 31, 2018—Provision for Loan Losses" for discussion of the changes in the provision for loan losses and discussion of the recovery in 2018.

The allowance for loan losses by loan category as of the dates shown was as follows:

					Decemb	oer 31,				
	20	119	20	18	20	17	20	16	20	15
(Dollars in thousands)	Amount	Percent								
Commercial and industrial	\$ 7,671	30.3 %	\$ 7,719	32.6 %	\$ 7,257	29.3 %	\$ 6,409	25.6 %	\$ 4,746	18.7 %
Real estate: Commercial										
real estate Construction	7,975	31.6 %	6,730	28.4 %	10,375	41.9 %	10,770	43.1 %	7,058	27.9 %
and development 1-4 family	4,446	17.6 %	4,298	18.1 %	3,482	14.0 %	4,598	18.4 %	4,504	17.8 %
residential Multi-family	2,257	8.9 %	2,281	9.6 %	1,326	5.4 %	1,286	5.1 %	2,295	9.1 %
residential	1,699	6.7 %	1,511	6.4 %	1,419	5.7 %	916	3.7 %	762	3.0 %
Consumer	388	1.5 %	387	1.6 %	566	2.3 %	353	1.4 %	363	1.4 %
Agricultural	74	0.3 %	62	0.3 %	68	0.3 %	79	0.3 %	93	0.4 %
Other	770	3.1 %	705	3.0 %	285	1.1 %	595	2.4 %	5,494	21.7 %
Total allowance										
for loan losses	\$ 25,280	100.0 %	\$ 23,693	100.0 %	\$ 24,778	100.0 %	\$ 25,006	100.0 %	\$ 25,315	100.0 %

Securities

As of December 31, 2019, the carrying amount of the Company's securities totaled \$231.3 million compared to \$230.0 million as of December 31, 2018, an increase of \$1.3 million, or 0.6%. Amortized cost decreased \$5.5 million as a result of maturities, sales, calls and paydowns outpacing purchases. Net unrealized gains (losses) of the security portfolio was a net gain of \$3.0 million at December 31, 2019 and a net loss of \$3.8 million at December 31, 2018. This change of \$6.8 million was primarily due to changing market interest rates.

The book value of the securities portfolio as of the dates indicated was as follows:

	December 31,							
(Dollars in thousands)		2019		2018	Increase (Decrease)		crease)	
Securities available for sale:								
Debt securities:								
State and municipal securities	\$	53,279	\$	57,691	\$	(4,412)	(7.6%)	
U.S. agency securities:								
Debt securities		_		16,881		(16,881)	(100.0%)	
Collateralized mortgage obligations		55,989		65,414		(9,425)	(14.4%)	
Mortgage-backed securities		120,847		88,859		31,988	36.0%	
Equity securities:		1,147		1,088		59	5.4%	
Debt securities held to maturity:								
Mortgage-backed securities		_		31		(31)	(100.0%)	
Total securities	\$	231,262	\$	229,964	\$	1,298	0.6%	
Mortgage-backed securities	\$	120,847 1,147	\$	88,859 1,088 31	\$	31,988 59 (31)	36.0% 5.4% (100.0%)	

The Company's mortgage-backed securities at December 31, 2019 and 2018, were agency securities. The Company does not hold any Fannie Mae or Freddie Mac preferred stock, corporate equity, collateralized debt obligations, collateralized loan obligations, structured investment vehicles, private label collateralized mortgage obligations, subprime, Alt-A or second lien elements in the securities portfolio.

Contractual maturities and weighted-average yields by security type based on estimated annual income divided by the average amortized cost of the Company's debt securities portfolio as of the date indicated was as follows:

	1 Ye or Le		After 1 to 5 ye		After 5 Y		After 10 Yea		Tota	l .
(Dollars in thousands)	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Total	Yield
December 31, 2019										
State and municipal securities	\$ 1,360	2.7%	\$ 1,409	2.5%	\$ 8,132	2.7%	\$ 42,378	2.9%	\$ 53,279	2.9%
U.S. agency securities:										
Collateralized mortgage obligations Mortgage-backed	_	_	_	_	4,803	2.5%	51,186	2.4%	55,989	2.4%
securities	25	2.3%	1,736	3.8%	1,939	2.8%	117,147	2.6%	120,847	2.6%
Other securities	1,147	2.3%	´—	_		_		_	1,147	_
Total debt securities	\$ 2,532	2.5%	\$ 3,145	3.2%	\$ 14,874	2.6%	\$ 210,711	2.6%	\$ 231,262	2.6%

The contractual maturity of a collateralized mortgage obligation or mortgage-backed security is the date at which the last underlying mortgage matures and is not a reliable indicator of their expected life because borrowers have the right to prepay their obligations at any time. The weighted-average life of the securities portfolio was 4.3 years with an estimated modified duration of 3.9 years as of December 31, 2019.

A portion of the securities have contractual maturities extending beyond 10 years, bear fixed rates of interest and are collateralized by residential mortgages. Repayment of principal on these bonds is primarily dependent on the cash flows received from payments on the underlying collateral to the bond issuer and therefore, the likelihood of prepayment is impacted by the economic environment. During a period of increasing interest rates, fixed rate mortgage-backed securities do not tend to experience heavy prepayments and as a result, the average lives of these securities are lengthened. If interest rates fall, prepayments tend to increase and as a result the lives of these securities are shortened.

Deposits

Total deposits were \$2.9 billion at December 31, 2019, an increase of \$86.1 million, or 3.1%, compared to December 31, 2018. Noninterest-bearing deposits as of December 31, 2019, were \$1.2 billion, an increase of \$1.8 million, or 0.2%, compared to December 31, 2018. Total interest-bearing account balances as of December 31, 2019, were \$1.7 billion, an increase of \$84.3 million, or 5.3%, from December 31, 2018. The changes in deposits from December 31, 2018 to December 31, 2019 were due to normal fluctuations in customer activities.

Deposits as of the dates shown below were as follows:

	December 31,							
(Dollars in thousands) Interest-bearing demand accounts		2019		2018		Increase (Decrease)		
		369,744	\$	387,457	\$	(17,713)	(4.6%)	
Money market accounts		805,942		737,770		68,172	9.2%	
Saving accounts		92,183		96,962		(4,779)	(4.9%)	
Certificates and other time deposits,								
\$100,000 or greater		208,018		189,007		19,011	10.1%	
Certificates and other time deposits, less								
than \$100,000		191,640		172,028		19,612	11.4%	
Total interest-bearing deposits		1,667,527		1,583,224		84,303	5.3%	
Noninterest-bearing deposits		1,184,861		1,183,058		1,803	0.2%	
Total deposits	\$	2,852,388	\$	2,766,282	\$	86,106	3.1%	

Uninsured certificates of deposits as of the date indicated below were as follows:

(Dollars in thousands)	 December 31, 2019
Three months or less	\$ 27,098
Over three months through six months	6,001
Over six months through 12 months	48,500
Over 12 months	18,346
Total	\$ 99,945

Average balances and average rates paid on deposits for the dates indicated were as follows:

	Years Ended December 31,					
	2019			2018		
(Dollars in thousands)	Average Balance	Average Rate		Average Balance	Average Rate	
Interest-bearing demand accounts\$	352,678	0.25 %	\$	362,498	0.23 %	
Savings accounts	93,192	0.06 %		94,754	0.06 %	
Money market accounts	745,435	1.28 %		714,565	0.87 %	
Certificates and other time deposits, \$100,000 or greater.	191,770	1.36 %		173,160	0.79 %	
Certificates and other time deposits, less than \$100,000	182,963	1.61 %		174,666	1.23 %	
Total interest-bearing deposits	1,566,038	1.02 %		1,519,643	0.70 %	
Noninterest-bearing deposits	1,193,527	_		1,134,191	_	
Total deposits	2,759,565	0.58 %	\$	2,653,834	0.40 %	

The ratio of average noninterest-bearing deposits to average total deposits was 43.3% and 42.7% for the years ended December 31, 2019 and 2018, respectively.

Borrowings

The Company has a loan agreement with Frost Bank, which provides for a \$30.0 million revolving line of credit. At December 31, 2019, there were no outstanding borrowings on this line of credit and the Company did not draw on this line of credit during 2019 or 2018. See "Item 8—Financial Statements and Supplementary Data—Note 11."

The Federal Home Loan Bank allows the Bank to borrow on a blanket floating lien status collateralized by certain loans. At December 31, 2019 and 2018, total borrowing capacity of \$1.0 billion and \$919.9 million, respectively, was available under this arrangement. During the year ended December 31, 2019, funds were borrowed under this agreement on both a short-term basis and long-term basis and at December 31, 2019, \$50.0 million of Federal Home Loan Bank advances were outstanding. See "Liquidity and Capital Resources—Contractual Obligations" below for maturity information. During the year ended December 31, 2018, funds were borrowed under this agreement on a short-term basis, and as of December 31, 2018, there were no outstanding Federal Home Loan Bank advances. The average balances for Federal Home Loan Bank advances outstanding at December 31, 2019 and 2018 was \$61.6 million and \$3.4 million, respectively, and the weighted-average interest rate for the years ended December 31, 2019 and 2018 was 2.25% and 2.18%, respectively.

The Company maintains four federal funds lines of credit with commercial banks that provide for the availability to borrow up to an aggregate of \$75.0 million. There were no funds under these lines of credit outstanding as of December 31, 2019 and 2018.

Liquidity and Capital Resources

Liquidity

Liquidity involves the ability to raise funds to support asset growth and acquisitions or reduce assets to meet deposit withdrawals and other payment obligations, to maintain reserve requirements and otherwise to operate on an ongoing basis and manage unexpected events. The Company's primary source of funds is deposits and the primary use of

funds is loans. Historically, the cost of the Company's deposits has been lower than other sources of funds available, such as debt. The Company does not expect a change in the primary source or use of funds in the foreseeable future.

The composition of funding sources and uses as a percentage of average total assets for the periods indicated was as follows:

	Years Ended December 31,		
	2019	2018	
Sources of funds:			
Deposits:			
Interest-bearing	46.4 %	48.1 %	
Noninterest-bearing	35.4 %	35.9 %	
Federal Home Loan Bank advances	1.8 %	0.1 %	
Repurchase agreements	— %	0.1 %	
Note payable and junior subordinated debt	— %	0.4 %	
Other liabilities	1.1 %	0.7 %	
Shareholders' equity	15.3 %	14.7 %	
Total sources	100.0 %	100.0 %	
Uses of funds:			
Loans	77.3 %	75.8 %	
Securities	6.9 %	7.2 %	
Other interest-earning assets	7.2 %	8.1 %	
Equity securities	0.5 %	0.5 %	
Other noninterest-earning assets	8.1 %	8.4 %	
Total uses	100.0 %	100.0 %	
Average loans to average deposits	94.5 %	90.1 %	

As of December 31, 2019, total cash and cash equivalents was \$372.1 million, compared to \$382.1 million as of December 31, 2018, a decrease of \$10.0 million. The decrease was primarily due to cash used in investing activities of \$189.7 million, partially offset by cash provided by financing of \$123.6 million and \$56.1 million of cash provided by operations. See "Item 8—Financial Statements and Supplementary Data—Consolidated Statement of Cash Flows" for the year ended December 31, 2019.

As of December 31, 2019, the Company had no exposure to future cash requirements associated with known uncertainties or capital expenditure of a material nature.

Contractual Obligations

In the normal course of operations, the Company enters into certain contractual obligations, such as obligations for operating leases, certificates of deposits and borrowings. Future cash payments associated with the Company's contractual obligations, as of the dates indicated were as follows:

(Dollars in thousands)	Less than 1 year	1 year to 3 years	3 year to 5 years	Greater than 5 years	Total
December 31, 2019					
Federal Home Loan Bank advances	\$ —	\$ 10,000	\$ 40,000	\$ —	\$ 50,000
Non-cancelable future operating leases	2,025	4,836	4,394	10,231	21,486
Certificates of deposit	298,218	70,490	30,950	_	399,658
Total	\$ 300,243	\$ 85,326	\$ 75,344	\$ 10,231	\$ 471,144
December 31, 2018					
Non-cancelable future operating leases	\$ 2,118	\$ 4,363	\$ 4,565	\$ 10,048	\$ 21,094
Certificates of deposit	241,963	108,436	10,636	_	361,035
Junior subordinated debt	1,571			_	1,571
Total	\$ 245,652	\$ 112,799	\$ 15,201	\$ 10,048	\$ 383,700

Off-Balance Sheet Items

In the normal course of business, the Company enters into various transactions, which in accordance with GAAP, are not included in the consolidated balance sheets. These transactions are entered into to meet the customer financing needs. These transactions include commitments to extend credit and standby and commercial letters of credit, which involve, to varying degrees, elements of credit risk and interest rate risk in excess of the amounts recognized in our consolidated balance sheets.

Commitments associated with outstanding standby and commercial letters of credit and commitments to extend credit expiring by period as of the dates indicated below were as follows:

	Less than	1 year to	3 year to	Greater than	
(Dollars in thousands)	1 year	3 years	5 years	5 years	Total
December 31, 2019					
Standby letters of credit	\$ 14,990	\$ 8,557	\$ —	\$ —	\$ 23,547
Commitments to extend credit	485,304	263,647	34,425	10,674	794,050
Total	\$ 500,294	\$ 272,204	\$ 34,425	\$ 10,674	\$ 817,597
December 31, 2018					
Standby letters of credit	\$ 22,789	\$ 3,940	\$ 5,000	\$ —	\$ 31,729
Commitments to extend credit	486,480	267,099	14,415	63,642	831,636
Total	\$ 509,269	\$ 271,039	\$ 19,415	\$ 63,642	\$ 863,365

Standby letters of credit are conditional commitments issued to guarantee the performance of a customer to a third-party. In the event of nonperformance by the customer, the Company has rights to the underlying collateral, which can include commercial real estate, physical plant and property, inventory, receivables, cash and/or marketable securities. The Company's credit risk associated with issuing letters of credit is essentially the same as the risk involved in extending loan facilities to our customers.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being fully drawn upon, the total commitment amounts disclosed above do not necessarily represent future cash requirements.

Capital Resources

Total shareholders' equity increased to \$535.7 million as of December 31, 2019, compared to \$487.6 million as of December 31, 2018, an increase of \$48.1 million, or 9.9%, primarily due to the current year income of \$50.5 million, a \$5.4 million increase in other comprehensive income and \$2.4 million of stock compensation expense, partially offset by \$10.1 million in dividends to common shareholders declared during 2019.

In July 2019, the Company's Board of Directors authorized a share repurchase program under which the Company may repurchase up to \$40.0 million of the Company's common stock through September 30, 2020. During 2019, 100 shares were repurchased at \$27.98 per share and returned to the status of authorized but unissued shares of common stock.

As a general matter, FDIC insured depository institutions and their holding companies are required to maintain minimum capital relative to the amount and types of assets they hold. The Company and the Bank are both subject to regulatory capital requirements. At December 31, 2019 and 2018, the Company and the Bank were in compliance with all applicable regulatory capital requirements at the bank holding company and bank levels, and the Bank was classified as "well capitalized" for purposes of the FDIC's prompt corrective action regulations. The OCC or the FDIC may require the Bank to maintain capital ratios above the required minimums and the Federal Reserve may require the Company to maintain capital ratios above the required minimums. See "Item 8—Financial Statements and Supplementary Data—Note 20."

Interest Rate Sensitivity and Market Risk

Market risk refers to the risk of loss arising from adverse changes in interest rates, foreign currency exchange rates, commodity prices and other relevant market rates and prices. As a financial institution, the Company's primary component of market risk is interest rate volatility. The Company is not subject to foreign exchange or commodity price risk and does not own any trading assets. The Company does not enter into instruments such as leveraged derivatives, financial options, financial future contracts or forward delivery contracts to reduce interest rate risk.

Interest rate risk is the potential of economic losses due to future interest rate changes. These economic losses can be reflected as a loss of future net interest income and/or a decrease in current fair market values. The objective is to measure the effect on net interest income and to adjust the balance sheet to minimize the inherent risk while at the same time maximizing income. Fluctuations in interest rates will ultimately impact both the level of income and expense recorded on most of the Company's assets and liabilities and the market value of all interest-earning assets and interest-bearing liabilities, other than those which have a short-term to maturity.

The Company has asset, liability and funds management policies that provide the guidelines for effective funds management and has established a measurement system for monitoring the net interest rate sensitivity position. The Company's exposure to interest rate risk is managed by the Funds Management Committee of the Bank. The committee formulates strategies based on appropriate levels of interest rate risk with consideration of the impact on earnings and capital of the current outlook on interest rates, potential changes in interest rates, regional economies, liquidity, business strategies and other factors. The committee meets regularly to review, among other things, the relationships between interest-earning assets and interest-bearing liabilities, the sensitivity of assets and liabilities to interest rate changes, the book and market values of assets and liabilities, unrealized gains and losses, purchase and sale activities, commitments to originate loans and the maturities of investments and borrowings. Additionally, the committee reviews liquidity, cash flow flexibility, maturities of deposits and consumer and commercial deposit activity.

The Company uses interest rate risk simulation models and shock analyses to test the interest rate sensitivity of net interest income and fair value of equity and the impact of changes in interest rates on other financial metrics. Contractual maturities and re-pricing opportunities of loans are incorporated in the model, as are prepayment assumptions, maturity data and call options within the investment portfolio. Average life of non-maturity deposit accounts are based on standard regulatory decay assumptions and are incorporated into the model. The assumptions used are inherently uncertain and the model cannot precisely measure future net interest income or precisely predict the impact of fluctuations in market interest rates on net interest income. Actual results will differ from the model's simulated results due to timing, magnitude and frequency of interest rate changes as well as changes in market conditions and the application and timing of various management strategies.

On a quarterly basis, two simulation models are run, including a static balance sheet and dynamic growth balance sheet. These models test the impact on net interest income and fair value of equity from changes in market interest rates under various scenarios. Under the static and dynamic growth models, rates are shocked instantaneously and ramped rate changes over a 12-month horizon based upon parallel and non-parallel yield curve shifts. Parallel shock scenarios assume instantaneous parallel movements in the yield curve compared to a flat yield curve scenario. Non-parallel simulation involves analysis of interest income and expense under various changes in the shape of the yield curve. The Company's internal policy regarding internal rate risk simulations currently specifies that for instantaneous parallel shifts of the yield curve, estimated net income at risk for the subsequent one-year period should not decline by more than 10% for a 100 basis-point shift, 20% for a 200-basis point shift and 30% for a 300-basis point shift.

Simulated change in net interest income and fair value of equity over a 12-month horizon as of the dates indicated below were as follows:

	December	31, 2019	December	31, 2018	
Change in Interest Rates (Basis Points)	Percent Change in Net Interest Income	Percent Change in Fair Value of Equity	Percent Change in Net Interest Income	Percent Change in Fair Value of Equity	
+ 300	15.8 %	10.2 %	16.7 %	(3.1)%	
+ 200	10.9 %	10.4 %	11.6 %	(0.4)%	
+ 100	5.4 %	8.7 %	6.1 %	1.1 %	
Base	<u> </u>	— %	 %	— %	
-100	(4.5)%	(14.6)%	(6.8)%	(7.6)%	

The results are primarily due to behavior of demand, money market and savings deposits during such rate fluctuations. Historically, interest rates on these deposits have changed more slowly than changes in the discount and federal funds rates. This assumption is incorporated into the simulation model and is generally not fully reflected in a gap analysis. The assumptions incorporated into the model are inherently uncertain and, as a result, the model cannot precisely measure future net interest income or precisely predict the impact of fluctuations in market interest rates on net interest income. Actual results will differ from the model's simulated results due to timing, magnitude and frequency of interest rate changes as well as changes in market conditions and the application and timing of various strategies.

LIBOR Transition

The London Interbank Offered Rate, or LIBOR, is used as an index rate for the Company's interest-rate swaps and approximately 13.5% of the Company's loans at December 31, 2019. It is expected that a number of private-sector banks that have been reporting information used to set LIBOR will stop doing so after 2021 when their reporting commitment ends. As a result, LIBOR may no longer be available as an index or may be seen as no longer representative of the market. Alternative reference rates are being identified, but existing contracts may not have been written to allow the use of these alternatives. The Company is evaluating the risks related to this transition and its evaluation and mitigation of risks related to the discontinuation of LIBOR may span several reporting periods through 2021.

Impact of Inflation

The Company's consolidated financial statements and related notes included elsewhere in this Annual Report on Form 10-K have been prepared in accordance with GAAP. GAAP requires the measurement of financial position and operating results in terms of historical dollars, without considering changes in the relative value of money over time due to inflation or recession.

Unlike many industrial companies, substantially all the Company's assets and liabilities are monetary in nature. As a result, interest rates have a more significant impact on the Company's performance than the effects of general levels of inflation. Interest rates may not necessarily move in the same direction or in the same magnitude as the prices of goods and services. However, other operating expenses do reflect general levels of inflation.

Critical Accounting Policies

The Company's accounting policies are described in "Item 8—Financial Statements and Supplementary Data—Note 1." The Company believes that the following accounting policies involve a higher degree of judgment and complexity:

Allowance for Loan Losses

The allowance for loan losses represents management's estimate of probable and reasonably estimable credit losses inherent in the loan portfolio. In determining the allowance, the Company estimates losses on individual impaired loans, or groups of loans which are not impaired, where the probable loss can be identified and reasonably estimated. On a quarterly basis, the risk inherent in the loan portfolio based on qualitative and quantitative trends in the portfolio is assessed, including the internal risk classification of loans, historical loss rates, changes in the nature and volume of the

loan portfolio, industry or borrower concentrations, delinquency trends, detailed reviews of significant loans with identified weaknesses and the impacts of local, regional and national economic factors on the quality of the loan portfolio.

Determining the amount of the allowance is considered a critical accounting estimate, as it requires significant judgment and the use of subjective measurements, including management's assessment of overall portfolio quality. The Company maintains the allowance at an amount it believes is sufficient to provide for estimated losses inherent in the loan portfolio at each balance sheet date. Fluctuations in the provision for loan losses may result from management's assessment of the adequacy of the allowance. Changes in these estimates and assumptions are possible and may have a material impact on the allowance, and therefore the Company's financial position, liquidity or results of operations. For a description of the factors considered in determining the allowance for loan losses see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Financial Condition—Allowance for Loan Losses" and "Item 8—Financial Statements and Supplementary Data—Note 1."

Fair Values of Financial Instruments

The fair values of the Company's financial instruments are based upon quoted market prices, where available. If quoted market prices are not available, fair value is estimated based upon models that primarily use observable market-based parameters as inputs. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

Goodwill and Other Intangibles

Goodwill, which is excess purchase price over the fair value of net assets from acquisitions, is evaluated for impairment at least annually and on an interim basis if events or circumstances indicate that it is likely an impairment has occurred. Qualitative factors are assessed to determine if it is likely that the fair value of a reporting unit is less than its carrying amount. If it is determined that it is likely that the fair value of a reporting unit is less than its carrying amount, the fair value of the reporting unit is compared with the carrying amount of the reporting unit. The fair value of net assets is estimated based on an analysis of market value. Impairment exists if the fair value of the reporting unit at the date of the test is less than the goodwill recorded. If goodwill is impaired, a loss would then be recognized in the consolidated financial statements to the extent of the impairment.

Determining the fair value of goodwill is considered a critical accounting estimate because the allocation of the fair value of goodwill to assets and liabilities requires significant management judgment and the use of subjective measurements. Variability in the market and changes in assumptions or subjective measurements used to allocate fair value are reasonably possible and may have a material impact on the Company's financial position, liquidity or results of operations.

The Company's other intangible assets include core deposits, loan servicing assets and customer relationship intangibles, which can be distinguished from goodwill because of contractual or other legal rights or because the asset is capable of being sold or exchanged either on its own or in combination with a related contract, asset, or liability. Other intangible assets are tested for impairment whenever events or changes in circumstances indicate the carrying amount of the assets may not be recoverable from future undiscounted cash flows. If impaired, the assets are recorded at fair value.

Emerging Growth Company

The JOBS Act permits an "emerging growth company" to take advantage of an extended transition period to comply with new or revised accounting standards applicable to public companies. The Company decided not to take advantage of this provision and is complying with new or revised accounting standards to the same extent that compliance is required for non-emerging growth companies. The decision to opt out of the extended transition period under the JOBS Act is irrevocable.

Recently Issued Accounting Pronouncements

See "Item 8—Financial Statements and Supplementary Data—Note 1."

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Interest Rate Sensitivity and Market Risk" for a discussion of how the Company manages market risk.

Item 8. Financial Statements and Supplementary Data

The Company's financial statements and accompanying notes are included in "Item 15 — Exhibits and Financial Statement Schedules."

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

Evaluation of disclosure controls and procedures. As of the end of the period covered by this Annual Report on Form 10-K, the Company carried out an evaluation, under the supervision and with the participation of its management, including its Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of its disclosure controls and procedures. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives and management was required to apply judgment in evaluating its controls and procedures. Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) were effective as of the end of the period covered by this Annual Report on Form 10-K.

Changes in internal control over financial reporting. There were no changes in the Company's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended December 31, 2019, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Report on management's assessment of internal control over financial reporting. Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act). The Company's internal control system is a process designed to provide reasonable assurance regarding the preparation and fair presentation of published financial statements in accordance with GAAP. All internal control systems, no matter how well designed, have inherent limitations and can only provide reasonable assurance with respect to financial reporting.

As of December 31, 2019, management assessed the effectiveness of the Company's internal control over financial reporting based on the criteria for effective internal control over financial reporting established in "Internal Control—Integrated Framework," issued by the Committee of Sponsoring Organizations ("COSO") of the Treadway Commission in 2013. This assessment included controls over the preparation of the schedules equivalent to the basic financial statements in accordance with the instructions for the Consolidated Financial Statements for Bank Holding Companies (Form FR Y-9C) to meet the reporting requirements of Section 112 of the Federal Deposit Insurance Improvement Act. Management's assessment determined that the Company maintained effective internal controls over financial reporting as of December 31, 2019.

This Annual Report on Form 10-K does not include an attestation report of the Company's registered public accounting firm due to a transition period established by rules of the SEC for an emerging growth company.

Item 9B. Other Information.

None.

PART III.

Item 10. Directors, Executive Officers and Corporate Governance

Code of Ethics.

We have adopted a code of business conduct and ethics (the "Code of Ethics") that applies to all employees, including executive officers, and to directors. The Code of Ethics is available on the Corporate Governance page of our website at www.communitybankoftx.com. If we were to amend or waive any provision of our Code of Ethics that applies to our principal executive officer, principal financial officer, principal accounting officer or any person performing similar functions, we intend to satisfy our disclosure obligations with respect to any such waiver or amendment by posting such information on our internet website set forth above.

All other information called for by this item is set forth in the Definitive Proxy Statement relating to the 2020 Annual Meeting of Shareholders, or the 2020 Proxy Statement, to be filed with the SEC pursuant to Regulation 14A under the Exchange Act within 120 days of the end of the fiscal year ended December 31, 2019 and is incorporated herein by reference.

Item 11. Executive Compensation

The information called for by this item is set forth in the 2020 Proxy Statement, to be filed with the SEC within 120 days of the end of the fiscal year ended December 31, 2019 and is incorporated herein by reference to the 2020 Proxy Statement.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Certain information required by this item is included under the caption "Securities Authorized for Issuance Under Equity Compensation Plans" in Part II, Item 5 of this Annual Report on Form 10-K. The other information called for by this item is set forth in the 2020 Proxy Statement, to be filed with the SEC within 120 days of the end of the fiscal year ended December 31, 2019 and is incorporated herein by reference to the 2020 Proxy Statement.

Item 13. Certain Relationships and Related Transactions and Director Independence

The information called for by this item is set forth in our Definitive Proxy Statement relating to the 2020 Proxy Statement, to be filed with the SEC within 120 days of the end of the fiscal year ended December 31, 2019 and is incorporated herein by reference to the 2020 Proxy Statement.

Item 14. Principal Accounting Fees and Services

The information called for by this item is set forth in our Definitive Proxy Statement relating to the 2020 Proxy Statement, to be filed with the SEC within 120 days of the end of the fiscal year ended December 31, 2019 and is incorporated herein by reference to the 2020 Proxy Statement.

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PART IV.

Item 15. Exhibits, Financial Statements Schedules

All supplemental schedules to the consolidated financial statements have been omitted as inapplicable or because the required information is included in our consolidated financial statements or the notes thereto included in this Annual Report on Form 10-K.

Exhibit Index

Exhibit	
Number	Description of Exhibit
3.1	First Amended and Restated Certificate of Formation of CBTX, Inc. (incorporated by reference to Exhibit 3.1 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
3.2	Second Amended and Restated Bylaws of CBTX, Inc. (incorporated by reference to Exhibit 3.2 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
4.1	Specimen Common Stock Certificate (incorporated by reference to Exhibit 4.1 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
4.2*	Description of Registrant's Securities
10.1	Second Amended and Restated Loan Agreement between CBTX, Inc., as borrower and Frost Bank, as lender, dated as of December 13, 2019 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed with the Commission on December 17, 2019, File No. 001-38280)
10.2	Revolving Promissory Note between CBTX, Inc., as borrower and Frost Bank, as lender, dated as of December 13, 2019 (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed with the Commission on December 17, 2019, File No. 001-38280)
10.3	Pledge and Security Agreement between CBTX, Inc., as borrower and Frost Bank, as lender, dated as of December 13, 2018 (incorporated by reference to Exhibit 10.3 to the Company's Form 8-K filed with the Commission on December 14, 2018, File No. 001-38280)
10.4†	Amended and Restated Employment Agreement between CBTX, Inc. and Robert R. Franklin, Jr., dated October 28, 2017 (incorporated by reference to Exhibit 10.4 to the Company's Form S-1 filed with the Commission on October 30, 2017, File No. 333-220930)
10.4.1†	2017 Salary Continuation Agreement between CommunityBank of Texas, N.A. and Robert R. Franklin, Jr., dated October 28, 2017 (incorporated by reference to Exhibit 10.4.1 to the Company's Form S-1 filed with the Commission on October 30, 2017, File No. 333-220930)
10.5†	Employment Agreement between CBFH, Inc. and Robert T. Pigott, Jr., dated March 6, 2013 (incorporated by reference to Exhibit 10.5 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
10.6†	Employment Agreement between CBFH, Inc. and J. Pat Parsons, dated May 21, 2008 (incorporated by reference to Exhibit 10.6 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)

10.7†	Amendment to Employment Agreement between CBFH, Inc. and J. Pat Parsons, dated December 31, 2008 (incorporated by reference to Exhibit 10.7 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
10.8†	Amendment to Employment Agreement between CBFH, Inc. and J. Pat Parsons, dated March 6, 2013 (incorporated by reference to Exhibit 10.8 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
10.9†*	Employment Agreement between Community Bank of Texas, N.A. and Travis Jaggers, dated January 4, 2016.
10.10†	CBTX, Inc. 2017 Omnibus Incentive Plan (incorporated by reference to Exhibit 10.9 to the Company's Form S-1 filed with the Commission on October 30, 2017, File No. 333-220930)
10.11†	Form of Restricted Stock Award Agreement under the CBTX, Inc. 2017 Omnibus Incentive Plan (incorporated by reference to Exhibit 10.10 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
10.12†	Form of Restricted Stock Unit Award Agreement under the CBTX, Inc. 2017 Omnibus Incentive Plan (incorporated by reference to Exhibit 10.11 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
10.13†	Form of Stock Option Award Agreement under the CBTX, Inc. 2017 Omnibus Incentive Plan (incorporated by reference to Exhibit 10.12 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
10.14†	Form of Stock Appreciation Right Award Agreement under the CBTX, Inc. 2017 Omnibus Incentive Plan (incorporated by reference to Exhibit 10.13 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
10.15†	VB Texas, Inc. 2006 Stock Option Plan (incorporated by reference to Exhibit 10.14 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
10.16†	CBFH, Inc. 2014 Stock Option Plan (incorporated by reference to Exhibit 10.15 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
10.17†	Form of Stock Option Award Agreement and Notice of Stock Option Award under the CBFH, Inc. 2014 Stock Option Plan (incorporated by reference to Exhibit 10.16 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
10.18†	Executive Deferred Compensation Agreement between CommunityBank of Texas, NA and J. Pat Parsons, dated December 30, 2011 (incorporated by reference to Exhibit 10.17 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
10.19†	Acknowledgment Agreement between CommunityBank of Texas, NA and J. Pat Parsons, effective as of January 1, 2015 (incorporated by reference to Exhibit 10.18 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
10.20†	Form of Indemnification Agreement between CBTX, Inc. and its directors and certain officers (incorporated by reference to Exhibit 10.19 to the Company's Form S-1 filed with the Commission on October 13, 2017, File No. 333-220930)
21.1*	Subsidiaries of CBTX, Inc.

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23.1*	Consent of Grant Thornton LLP
31.1*	Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1**	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2**	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101*	The following materials from CBTX's Annual Report on Form 10-K for the year ended December 31, 2019, formatted in XBRL (Extensible Business Reporting Language), furnished herewith: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Operations, (iii) Consolidated Statements of Comprehensive Income (Loss), (iv) Consolidated Statements of Changes in Shareholders' Equity, (v) Consolidated Statements of Cash Flows and (vi) Notes to Consolidated Financial Statements.

Item 16. Form 10-K Summary

None.

^{*} Filed with this Annual Report on Form 10-K
** Furnished with this Annual Report on Form 10-K

[†] Indicates a management contract or compensatory plan.

SIGNATURES

Pursuant to the requirements of the Securities Act of 1933, the registrant has duly caused this registration statement to be signed on its behalf by the undersigned, thereunto duly authorized in Houston, Texas, on February 26, 2020.

CBTX, INC.

By:

/s/ Robert R. Franklin, Jr. Robert R. Franklin, Jr.

Chairman, President and Chief Executive Officer

Pursuant to the requirements of the Securities Act of 1933, this registration statement has been signed by the following persons in the capacities indicated on the dates set forth below.

Signature	<u>Title</u>	Date
/s/ Robert R. Franklin, Jr. Robert R. Franklin, Jr.	Chairman, President and Chief Executive Officer (Principal Executive Officer)	February 26, 2020
/s/ Robert T. Pigott, Jr. Robert T. Pigott, Jr.	Senior Executive Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)	February 26, 2020
/s/ Michael A. Havard Michael A. Havard	Director	February 26, 2020
/s/ Tommy W. Lott Tommy W. Lott	Director	February 26, 2020
/s/ Glen W. Morgan Glen W. Morgan	Director	February 26, 2020
/s/ J. Pat Parsons J. Pat Parsons	Vice Chairman	February 26, 2020
/s/ Joe E. Penland, Sr. Joe E. Penland, Sr.	Director	February 26, 2020
/s/ Wayne A. Reaud Wayne A. Reaud	Director	February 26, 2020
/s/ Joseph B. Swinbank Joseph B. Swinbank	Director	February 26, 2020
/s/ Sheila G. Umphrey Sheila G. Umphrey	Director	February 26, 2020
/s/ John E. Williams, Jr. John E. Williams, Jr.	Director	February 26, 2020
/s/ William E. Wilson, Jr. William E. Wilson, Jr.	Director	February 26, 2020

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders CBTX, Inc.

Opinion on the financial statements

We have audited the accompanying consolidated balance sheets of CBTX, Inc. (a Texas corporation) and subsidiary (the "Company") as of December 31, 2019 and 2018, the related consolidated statements of income, comprehensive income, changes in shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2019, and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2019 and 2018, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2019, in conformity with accounting principles generally accepted in the United States of America.

Basis for opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ GRANT THORNTON LLP

We have served as the Company's auditor since 2015.

Dallas, Texas February 26, 2020 **Item 1. Financial Statements**

CBTX, INC. AND SUBSIDIARY

Consolidated Balance Sheets

(Dollars in thousands, except par value and per share amounts)

	December 31,		
	2019	2018	
ASSETS			
	¢ 51.250	¢ 54.450	
Cash and due from banks	\$ 51,259	\$ 54,450	
Interest-bearing deposits at other financial institutions	320,805	327,620	
Total cash and cash equivalents	372,064	382,070	
Securities	231,262	229,964	
Equity investments	16,710	13,026	
Loans held for sale	1,463	_	
Loans, net of allowance for loan loss of \$25,280 and \$23,693 at December 31, 2019 and	2 (12 00 7		
2018, respectively.	2,613,805	2,423,130	
Premises and equipment, net of accumulated depreciation of \$32,923 and \$29,867 at		-1	
December 31, 2019 and 2018, respectively	50,875	51,622	
Goodwill	80,950	80,950	
Other intangible assets, net of accumulated amortization of \$15,809 and \$14,915 at			
December 31, 2019 and 2018, respectively	4,938	5,775	
Bank-owned life insurance	71,881	71,525	
Operating lease right-to-use asset	12,926		
Deferred tax asset, net.	7,432	7,201	
Other assets	14,238	13,833	
Total assets	\$ 3,478,544	\$ 3,279,096	
LIABILITIES AND SHAREHOLDERS' EQUITY			
Liabilities			
Noninterest-bearing deposits	\$ 1,184,861	\$ 1,183,058	
Interest-bearing deposits	1,667,527	1,583,224	
Total deposits	2,852,388	2,766,282	
Federal Home Loan Bank advances	50,000	_	
Repurchase agreements	485	2,498	
Junior subordinated debt		1,571	
Operating lease liabilities	15,704	_	
Other liabilities	24,246	21,120	
Total liabilities	2,942,823	2,791,471	
Commitments and contingencies (Note 17)	<u> </u>		
Shareholders' equity			
Preferred stock, \$0.01 par value, 10,000,000 shares authorized, no shares issued	_	_	
Common stock, \$0.01 par value, 90,000,000 shares authorized, 25,837,048 and			
25,777,693 shares issued at December 31, 2019 and 2018, respectively, 24,979,702			
and 24,907,421 shares outstanding at December 31, 2019 and 2018, respectively	258	258	
Additional paid-in capital	346,559	344,497	
Retained earnings	201,080	160,626	
Treasury stock, at cost, 857,346 and 870,272 shares held at December 31, 2019 and	201,000	100,020	
2018, respectively	(14,562)	(14,781)	
Accumulated other comprehensive gain (loss), net of tax of \$634 and (\$791) at	(14,502)	(17,701)	
December 31, 2019 and 2018, respectively	2,386	(2,975)	
Total shareholders' equity	535,721	487,625	
Total liabilities and shareholders' equity			
Total habilities and shareholders equity	\$ 3,478,544	\$ 3,279,096	

See accompanying notes to consolidated financial statements.

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CBTX, INC. AND SUBSIDIARY Consolidated Statements of Income (Dollars in thousands, except per share amounts)

	v	ıded December	Jacambar 31			
	 2019	ears Li	2018	31,	2017	
Interest income	 					
Interest and fees on loans	\$ 141,388	\$	123,895	\$	107,368	
Securities	5,954		6,020		5,347	
Other interest-earning assets	5,333		5,030		3,204	
Equity investments	720		814		740	
Total interest income	 153,395		135,759	-	116,659	
Interest expense	 					
Deposits	15,999		10,586		7,652	
Federal Home Loan Bank advances	1,386		73		-,,,,,,	
Repurchase agreements	3		4		5	
Note payable and junior subordinated debt	19		435		1,228	
Total interest expense.	 17,407		11,098		8,885	
Net interest income	 135,988		124,661		107,774	
Provision (recapture) for loan losses	2,385		(1,756)		(338)	
· · · · · · · · · · · · · · · · · · ·	 133,603		126,417		108,112	
Net interest income after provision for loan losses	 133,003		120,417	-	100,112	
Noninterest income	6.551		6 201		5 900	
Deposit account service charges	6,554		6,281		5,800	
Net gain on sale of assets	652		660		1,524	
Card interchange fees	3,720		3,741		3,453	
Earnings on bank-owned life insurance	5,011		1,815		1,580	
Other	 2,691		1,755		1,847	
Total noninterest income	 18,628		14,252		14,204	
Noninterest expense						
Salaries and employee benefits	56,222		51,524		48,573	
Net occupancy expense	9,506		9,394		9,151	
Regulatory fees	1,138		2,053		2,176	
Data processing	2,678		2,677		2,629	
Software	1,757		1,576		1,208	
Printing, stationery and office	1,302		1,161		1,097	
Amortization of intangibles	894		985		1,079	
Professional and director fees	7,048		3,537		3,105	
Correspondent bank and customer related transaction						
expenses	268		265		286	
Loan processing costs	445		448		461	
Advertising, marketing and business development	1,831		1,824		1,461	
Repossessed real estate and other asset expense	1		72		609	
Security and protection expense	1,464		1,276		1,355	
Telephone and communications	1,774		1,530		1,316	
Other expenses	 3,815		3,694		3,786	
Total noninterest expense	 90,143		82,016		78,292	
Net income before income tax expense	62,088		58,653		44,024	
Income tax expense	 11,571		11,364		16,453	
Net income	\$ 50,517	\$	47,289	\$	27,571	
Earnings per common share	 ·		-			
Basic	\$ 2.03	\$	1.90	\$	1.23	
Diluted	\$ 2.02	\$	1.89	\$	1.22	

See accompanying notes to consolidated financial statements.

CBTX, INC. AND SUBSIDIARY Consolidated Statements of Comprehensive Income (Dollars in thousands)

	Years Ended December 31,					
		2019		2018		2017
Net income	\$	50,517	\$	47,289	\$	27,571
Change in unrealized gains (losses) on securities available for sale arising during the period, net		6,728		(3,302)		897
Reclassification adjustments for net realized gains included in net income		57		29		27
Change in related deferred income tax		(1,424)		687		(391)
Other comprehensive income (loss), net of tax		5,361		(2,586)		533
Total comprehensive income	\$	55,878	\$	44,703	\$	28,104

See accompanying notes to consolidated financial statements.

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CBTX, INC. AND SUBSIDIARY Consolidated Statements of Changes in Shareholders' Equity (Dollars in thousands, except share amounts)

	Common	Stock	Additional Paid-In	Retained	Treasui	y Stock	Accumulated Other Comprehensive	
	Shares	Amount	Capital	Earnings	Shares	Amount	Income (Loss)	Total
Balance at December 31, 2016	22,971,504	230	278,501	95,274	(909,432)	(15,446)	(922)	357,637
Sale of common stock in initial public offering, net of offering costs of			,	,	, ,	, , ,	,	·
\$7,241	2,760,000	27	64,492	_	_	_	_	64,519
Net income	_	_	_	27,571	_	_	_	27,571
per share		_		(4,561)			_	(4,561)
Exercise of stock options		_	(73)	_	11,160	190	_	117
Stock-based compensation expense	_	_	329	_	_	_	_	329
Other comprehensive loss, net of tax				69			533	602
Balance at December 31, 2017	25,731,504	\$ 257	\$ 343,249	\$ 118,353	(898,272)	\$ (15,256)	\$ (389)	\$ 446,214
Net income	_	_	_	47,289	_	_	_	47,289
per share	_	_	_	(5,016)	_	_	_	(5,016)
shares withheld for employee tax liabilities	46,189	1	(172)	_	_	_	_	(171)
Exercise of stock options	´ —	_	(181)	_	28,000	475	_	294
Stock-based compensation expense	_	_	1,601	_	_	_	_	1,601
Other comprehensive loss, net of tax	_	_	´ —	_	_	_	(2,586)	(2,586)
Balance at December 31, 2018	25,777,693	\$ 258	\$ 344,497	\$ 160,626	(870,272)	\$ (14,781)	\$ (2,975)	\$ 487,625
Net income	_	_	_	50,517	_	_	_	50,517
per share	_	_	_	(10,063)	_	_	_	(10,063)
liabilities	59,455	_	(239)	_	_	_	_	(239)
shares withheld for employee tax liabilities	_	_	(98)	_	12,926	219	_	121
Stock-based compensation expense	_	_	2,402	_	_	_	_	2,402
Shares repurchased	(100)	_	(3)	_	_	_	_	(3)
Other comprehensive income, net of	, ,						5 261	5 261
tax	25.837.048	\$ 258	\$ 346,559	\$ 201,080	(857,346)	\$ (14,562)	\$ 2,386	5,361
Balance at December 31, 2019	23,837,048	\$ 258	\$ 346,559	\$ 201,080	(837,346)	3 (14,302)	3 2,386	\$ 535,721

See accompanying notes to consolidated financial statements.

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CBTX, INC. AND SUBSIDIARY Consolidated Statements of Cash Flows (Dollars in thousands)

(Dollars in thousands)		1 7.	21			
		2019	Years Ended December 3			2017
Cash flows from operating activities:		2017		2010	_	2017
Net income	\$	50,517	\$	47,289	\$	27,571
Adjustments to reconcile consolidated net income to net cash provided by	<u>-</u>		· ·		•	. , ,
operating activities:						
Provision (recapture) for loan losses		2,385		(1,756)		(338)
Depreciation expense		3,203		3,309		3,353
Amortization of intangibles		894		985		1,079
Amortization of premiums on securities		1,194		1,091		1,294
Amortization of lease right-to-use assets		1,343				
Accretion of lease liabilities		534		_		
Earnings on bank-owned life insurance		(5,011)		(1,815)		(1,580)
Stock-based compensation expense		2,402		1,601		329
Deferred income tax (benefit) provision		(1,657)		(734)		2,932
Net gains on sales of assets		(652)		(660)		(1,524)
Earnings on securities		(18)		(54)		(50)
Valuation adjustments on repossessed real estate and other assets		(10)		(31)		341
Change in operating assets and liabilities:						311
Loans held for sale		(1,185)		1,921		(420)
Other assets		81		994		(3,156)
Operating lease liabilities		(1,895))) 1		(3,130)
Other liabilities		3,955		(2,850)		5,759
		5,573		2,032		8,019
Total adjustments	-					
Net cash provided by operating activities.		56,090	-	49,321		35,590
Cash flows from investing activities:		((51,000)		(405.970)		(255 525)
Purchases of securities		(651,908)		(495,870)		(355,525)
Proceeds from sales, calls and maturities of securities		625,550		462,842		317,284
Principal repayments of securities		30,726		21,962		20,692
Net increase in loans		(226,817)		(147,416)		(187,030)
Sales of loan participations.		31,868		45,921		46,067
Purchases of loan participations		(2,314)		(35,281)		(18,491)
Proceeds from sales of Small Business Administration loans		4,423		1,972		2,173
Net contributions to equity investments		(3,684)		(800)		(162)
Redemption (purchases) of bank-owned life insurance		4,655		(1,700)		(15,000)
Net (purchases) sales of premises and equipment		(2,488)		(1,293)		1,985
Proceeds from sales of repossessed real estate and other assets		141		1,054		2,574
Net decrease in time deposits in other banks		_		600		
Proceeds from insurance claims		108		287		
Net cash used in investing activities		(189,740)		(147,722)		(185,433)
Cash flows from financing activities:						
Net increase in noninterest-bearing deposits		1,803		73,269		84,364
Net increase (decrease) in interest-bearing deposits		84,303		90,041		(22,152)
Net increase in Federal Home Loan Bank advances		50,000		_		_
Net (decrease) increase in securities sold under agreements to repurchase		(2,013)		973		(818)
Repayments of note payable		_		_		(27,679)
Redemption of trust preferred securities		(1,571)		(5,155)		
Proceeds from sale of stock in initial public offering		_				71,760
Offering costs for initial public offering		_		_		(7,241)
Dividends paid on common stock		(8,757)		(4,979)		(4,412)
Payments to tax authorities for stock-based compensation		(239)		(171)		
Proceeds from exercise of stock options		121		294		117
Repurchase of common stock		(3)		_		_
Net cash provided by financing activities		123,644		154,272	_	93,939
Net decrease in cash, cash equivalents and restricted cash		(10,006)		55,871		(55,904)
Cash, cash equivalents and restricted cash, beginning		382,070		326,199		382,103
Cash, cash equivalents and restricted cash, ending	\$	372,064	\$	382,070	\$	326,199
Cash, Cash equivalents and restricted cash, chang	Φ	312,004	Ф	304,070	φ	320,139

See accompanying notes to consolidated financial statements.

CBTX, INC. AND SUBSIDIARY Notes to Consolidated Financial Statements

NOTE 1: BASIS OF PRESENTATION, NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING AND REPORTING POLICIES

<u>Nature of Operations</u>—CBTX, Inc., or the Company, or CBTX, operates 35 branches, 19 in the Houston market area, 15 in Beaumont/East Texas market area and one in Dallas through its wholly-owned subsidiary, CommunityBank of Texas, N.A., or the Bank. The Bank provides relationship-driven commercial banking products and services primarily to small and mid-sized businesses and professionals with operations within the Bank's markets. The Bank operates under a national charter and therefore is subject to regulation by the Office of the Comptroller of the Currency, or OCC, and the Federal Deposit Insurance Corporation, or FDIC. The Company is subject to regulation by the Board of Governors of the Federal Reserve System.

<u>Basis of Presentation</u>—The accompanying consolidated financial statements include the accounts of the Company and the Bank. All material intercompany balances and transactions have been eliminated in consolidation.

<u>Reclassification</u>—Within interest income, equity investment income for 2018 and 2017 has been reclassified from other interest-earning assets to a separate line and within interest expense, interest expense on notes payable and junior subordinated debt have been combined. On the December 31, 2018 balance sheet, repossessed real estate and other assets were combined with other assets. These reclassifications were made to conform to the 2019 financial statement presentation in the consolidated statements of income and consolidated balance sheets.

<u>Segment Reporting</u>—The Company has one reportable segment. The Company's activities are inter-related, and each activity is dependent and assessed based on how each of the activities of the Company supports the others. For example, lending is dependent upon the ability of the Company to fund itself with deposits and borrowings while managing the interest rate and credit risk. Accordingly, all significant operating decisions are based upon analysis of the Company as one segment or unit. The Company's chief operating decision-maker, the Chief Executive Officer, uses the consolidated results to make operating and strategic decisions.

<u>Use of Estimates</u>—In preparing financial statements in conformity with accounting principles generally accepted in the United States, or GAAP, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the consolidated balance sheets and reported amounts of revenues and expenses during the reporting periods. Actual results could differ from these estimates. Material estimates that are particularly susceptible to significant change in the near term include, but are not limited to, determination of the allowance for loan losses and fair values of financial instruments and goodwill and other intangible assets.

Cash and Due from Banks—Cash, cash equivalents and restricted cash include cash, interest-bearing and noninterest-bearing transaction accounts with other banks and federal funds sold. A majority of cash, cash equivalents and time deposits of the Company are maintained with major financial institutions in the United States, or U.S., and have original maturities less than 90 days. Interest-bearing deposit accounts with these financial institutions may exceed the amount of insurance provided on such deposits; however, these deposits typically may be redeemed upon demand and therefore, bear minimal risk. The Company periodically evaluates the stability of the financial institutions with which it has deposits to monitor this credit risk. The Company has cash deposits in correspondent financial institutions in excess of the amount insured by the FDIC in the amount of \$100.0 million and \$99.4 million at December 31, 2019 and 2018, respectively.

The Bank is required to maintain regulatory reserves with the Federal Reserve Bank and the reserve requirements for the Bank were \$18.6 million and \$18.5 million at December 31, 2019 and 2018, respectively. At December 31, 2019 and 2018, the Company had \$3.1 million and \$1.6 million in cash collateral used in its interest rate swap transactions. The Federal Reserve Bank reserve requirements and the cash collateral used in interest rate swap transactions are considered restricted cash.

<u>Loans</u>—Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off, are measured at historical cost and generally reported at their outstanding unpaid principal balances, net of any

unearned income, charge-offs and unamortized deferred fees and costs. Interest income is accrued on the unpaid principal balance. Loan origination fees and certain direct origination costs are deferred and recognized as adjustments to interest income over the lives of the related loans. The Company records lines of credit at their funded portion. All unfunded amounts for loans in process and credit lines are reported as unfunded commitments.

Government Guaranteed Loans—The Company originates loans that are partially guaranteed by the Small Business Administration, or SBA, and the Company may sell the guaranteed portion of these loans as market conditions and pricing allow for a gain to be recorded on the sale. Loan sales are recorded when control over the transferred asset has been relinquished. Control over the transferred portion is deemed to be surrendered when the assets have been removed from the Company, the transferree obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets and the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

In calculating the gain on sale of SBA loans, the Company's investment in the loan is allocated among the unguaranteed portion of the loan, the servicing amount retained, and the guaranteed portion of the loan sold, based on the relative fair market value of each portion. The gain on the sold portion of the loan is recognized based on the difference between the sale proceeds and the allocated investment.

Nonperforming and Impaired Loans—Nonperforming loans includes loans which have been categorized by management as nonaccrual because of delinquency status or because collection of principal and interest is doubtful. Loans restructured in a troubled debt restructuring are not considered nonperforming if the loans are not delinquent and otherwise performing in accordance with their restructured terms.

When the payment of principal or interest on a loan is delinquent for 90 days or more, or earlier in some cases, the loan is placed on nonaccrual status, unless the loan is in the process of collection or renewal and the underlying collateral fully supports the carrying value of the loan. If the decision is made to continue accruing interest on the loan, periodic reviews are made to confirm the accruing status of the loan and the probability that the Company will collect all principal and interest amounts outstanding.

When a loan is placed on nonaccrual status, interest accrued and uncollected during any period prior to the judgment of uncollectability is charged to operations, unless the loan is well secured with collateral values sufficient to ensure collection of both principal and interest. Generally, any payments received on nonaccrual loans are applied first to outstanding loan amounts, reducing the Company's recorded investment in the loan and next to the recovery of charged-off principal or interest amounts. Any excess is treated as recovery of lost interest. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Loans are considered impaired if, based on current information and events, it is probable that the Company will be unable to collect all amounts due in accordance with the original contractual terms of the loan agreement, including scheduled principal and interest payments. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Interest income received on impaired loans is either applied against principal or realized as interest income, according to management's judgment as to the collectability of principal.

<u>Troubled Debt Restructurings</u>— From time to time, the Company modifies loan agreements with borrowers. A modified loan is considered a troubled debt restructuring if the borrower is experiencing financial difficulties and the borrower has been granted a concession. Modifications to loan terms may include interest rate reductions, principal forgiveness, restructuring amortization schedules and other actions intended to minimize potential losses. Interest is generally accrued on such loans in accordance with the new terms. Loans restructured in a troubled debt restructuring are not considered nonperforming if the loans are not delinquent and otherwise performing in accordance with their restructured terms.

Allowance for Loan Losses—The allowance for loan losses represents management's estimate of probable losses inherent in the loan portfolio. Credit exposures deemed to be uncollectible are charged against these accounts. Cash recovered on previously charged-off amounts is recorded as a recovery to these accounts. The allowance for loan losses does not include amounts related to accrued interest receivable as accrued interest receivable is reversed when a loan is placed on nonaccrual or is charged-off.

The Company employs a systematic methodology for determining the allowance for loan losses that consists of two components: (i) specific valuation allowances based on probable losses on certain loans and (ii) historical valuation allowances based on historical average loss experience for similar loans with similar characteristics and trends adjusted, as necessary, to reflect the impact of current conditions and further adjusted for general economic conditions and other risk factors both internal and external to the Company.

A specific allowance is established for loans considered impaired when the carrying value of the loan is more than the present value of expected cash flows discounted at the loan's effective interest rate or, as a practical expedient, the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. The Company uses fair market value, less reasonable and customary costs to sell, for collateral dependent loans. In certain instances, a specific allowance will be established to protect against market deterioration.

The allowance on the remaining portfolio segments is calculated using historical loss rates adjusted for qualitative factors. Criticized and classified loans, not deemed impaired, are subject to an allowance based on the historical loss migration analysis by grade adjusted for qualitative factors. Pass loans are subject to an allowance based on historical losses by product type adjusted for qualitative factors.

The general component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and historical losses in the portfolio. The general valuation factor is based upon a more qualitative analysis of risk. Various risks are considered in the determination of the environmental adjustment factor such as asset quality, lending management and staff, loan policies and procedures, loan review, credit concentrations, loan volumes, collateral values, compliance and economic trends on both a local and national level.

A majority of the loan portfolio is comprised of loans to businesses and individuals in the Houston metropolitan and Beaumont/East Texas area. This geographic concentration subjects the loan portfolio to the general economic conditions within this area. The risks created by this concentration have been considered by management in the determination of the adequacy of the allowance for loan losses.

Loans Held for Sale—Loans held for sale include mortgage loans originated with the intent to sell on the secondary market. Loans held for sale are carried at the lower of cost or estimated fair value on an individual loan basis. These loans are held for an interim period, usually less than 30 days. Accordingly, these loans are classified as held for sale and are carried at cost, which is determined on an aggregate basis and deemed to be the equivalent of fair value based on the short-term nature of the loans.

<u>Securities</u>—Securities that the Company intends to hold for an indefinite period of time are classified as available for sale, carried at fair value and unrealized gains and losses are excluded from earnings and reported as accumulated other comprehensive income (loss), net of taxes in shareholders' equity until realized.

Securities that the Company has both the positive intent and ability to hold to maturity are classified as held to maturity and are carried at cost, adjusted for the amortization of premiums and the accretion of discounts. Securities are evaluated for other-than-temporary impairment, or OTTI, on at least a quarterly basis and more frequently when economic or market conditions warrant such an evaluation.

Premiums and discounts are amortized and accreted to income using the level-yield method of accounting, adjusted for prepayments as applicable. The specific identification method of accounting is used to compute gains or losses on the sales of these assets.

<u>Equity Investments</u>—The Company's equity investments are carried at cost and evaluated for impairment at least annually and on an interim basis if an event or circumstance indicates that it is likely that an impairment has occurred as these investments do not have readily determinable fair values.

<u>Premises and Equipment</u>—Premises and equipment are carried at cost, less accumulated depreciation. Depreciation expense is computed on the straight-line method over the estimated useful lives of the assets. Land is carried at cost. Leasehold improvements are amortized over the life of the lease, plus renewal options or the estimated useful lives, whichever is shorter. Buildings are depreciated over a period not to exceed 32 years. Depending upon the type of furniture and equipment, the depreciation period will range from three to 10-years. Bank vehicles are amortized over a period of

three years. Gains and losses on dispositions are included in other noninterest income. During periods of real estate development, interest on construction costs is capitalized if considered material by management.

Operating Leases— The Company leases certain office space, stand-alone buildings and land are recognized as operating lease right-of-use assets and operating lease liabilities in the consolidated balance sheets. Lease liabilities represent the Company's liability to make lease payments under these leases, on a discounted basis and are amortized on a straight-line basis over the lease term for each related lease agreement. Right-of-use assets represent the Company's right to use, or control the use of, leased assets for their lease term and are amortized over the lease term of the related lease agreement. See further discussion of Accounting Standards Update, or ASU 2016-02, Leases (Topic 842) below. The Company does not recognize short-term operating leases on the consolidated balance sheets. A short-term lease has term of 12 months or less and does not have a purchase option that is likely to be exercised. The Company subleases certain facilities to outside parties; however, these leases are not significant.

Goodwill and Other Intangible Assets—Goodwill is not amortized and is evaluated for impairment at least annually as of December 31 and on an interim basis if an event or circumstance indicates that it is likely that an impairment has occurred. Impairment would exist if the fair value of the reporting unit at the date of the test is less than the goodwill recorded on the financial statements. If an impairment of goodwill exists, a loss would then be recognized in the consolidated financial statements to the extent of the impairment.

The Company's identified intangibles are core deposits, customer relationship intangibles and loan servicing assets. Core deposit and customer relationship intangible assets are tested for impairment whenever events or changes in circumstances indicate the carrying amount of the assets may not be recoverable from future undiscounted cash flows. Servicing assets are assessed for impairment or increased obligation based on fair value at each reporting date.

Core deposit intangibles are amortized over a seven to 10-year period using an accelerated method in keeping with the anticipated benefits derived from those core deposits. Customer relationship intangibles are amortized over a 15-year period on a straight-line basis.

Servicing assets are recognized as separate assets when rights are acquired through the sale of financial assets. Servicing assets are initially recorded at fair market value and amortized in proportion to and over the service period and assessed for impairment or increased obligation based on fair value at each reporting date. Fair value is based on the gross coupon less an assumed contractual servicing cost or based upon discounted cash flows using market-based assumptions. Servicing assets are amortized into noninterest expense in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets. Servicing fee income is recorded for fees earned from servicing loans. The fees are based on a contractual percentage of the outstanding principal or a fixed amount per loan and are recorded as income when earned.

<u>Bank-owned Life Insurance</u>—The Company has purchased life insurance policies on covered individuals, which are recorded at their cash surrender value. Changes in the cash surrender value of the policies are recorded in noninterest income. Gains or losses and proceeds from maturities are recognized upon the death of a covered employee, on receipt of a death notice or other verified evidence.

Repossessed Real Estate and Other Assets—Real estate and other assets acquired through repossession or foreclosure are held for sale and are initially recorded at the fair value of the asset less estimated costs to sell. Outstanding loan balances are reduced to reflect this value through charges to the allowance for loan losses. If the fair value of the repossessed real estate and other assets declines after foreclosure, adjustments to reflect changes in fair value are recognized in income in the period such determinations are assessed. Any developmental costs associated with foreclosed property under construction are capitalized and considered in determining the fair value of the property. Any operating expenses of these assets, net of related income and gains and losses on their disposition are included in other noninterest income or expense.

Other Assets—Other assets include accrued interest receivables on loans and investments, derivative financial instruments assets, prepaid expenses, repossessed real estate and other assets.

Other Liabilities—Other liabilities include accrued interest payable on deposits, accrued bonuses, deferred compensation, derivative financial instruments liabilities and other liabilities.

Repurchase Agreements—The Company utilizes securities sold under repurchase agreements to facilitate the needs of our customers and to facilitate short-term borrowing needs. Securities sold under agreements to repurchase are stated at the amount of cash received in the transaction. The Company monitors collateral levels on a continuous basis and may be required to provide additional collateral based on the fair value of the underlying securities.

<u>Derivative Financial Instruments</u>—All derivatives are recorded at fair value on the balance sheet. Derivatives executed with the same counterparty are generally subject to master netting arrangements. Fair value amounts recognized for derivatives and fair value amounts recognized for the right/obligation to reclaim/return cash collateral are not offset for financial reporting purposes. The Company had no derivative instruments that qualified for hedge accounting during the periods reported herein, but it may in the future as circumstances arise.

<u>Fair Value Measurements</u>—Fair values of financial instruments are based upon quoted market prices, where available. If such quoted market prices are not available, fair value is estimated based upon models that primarily use observable market-based parameters as inputs. Fair value estimates involve uncertainties and matters of significant judgment regarding interest rates, credit risk, prepayments and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect the estimates.

Revenue Recognition—Accounting Standards Codification (Topic 606) or ASU 2014-09 requires entities to recognize revenue in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. A majority of the Company's revenue is derived from interest income on financial assets, which is not within the scope of ASC 606. Income from changes in the cash surrender value of bank-owned life insurance is also not within the scope of ASC 606.

The Company's revenue-generating activities that are within the scope of ASC 606 are included in noninterest income in the consolidated income statements as deposit account service charges, net gain on sale of assets, card interchange fees and other noninterest income. The Company generally fully satisfies its performance obligations on its contracts with customers as services are rendered and the transaction prices are typically fixed and charged at a point in time based on activity.

Income Taxes—The Company prepares and reports income taxes on a consolidated basis. Deferred tax assets and liabilities are reflected at income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. A valuation allowance, if needed, reduces deferred tax assets to the expected amount most likely to be realized. Realization of deferred tax assets is dependent upon the generation of a sufficient level of future taxable income and recoverable taxes paid in prior years. Although realization is not assured, management believes it is more likely than not that the deferred tax assets will be realized.

The Company may recognize the tax benefit of an uncertain tax position if it is more likely than not that the tax position will be sustained upon examination by the taxing authorities based on the technical merits of the position. For tax positions meeting the more likely than not threshold, the amount recognized in the financial statements would be the benefit that has a greater than 50% likelihood of being realized upon ultimate settlement with the relevant tax authority.

Company includes any interest expense assessed by taxing authorities in interest expense and any penalties related to income taxes in other expense on its consolidated statements of income.

<u>Transfers of Financial Assets</u>—Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when the assets have been isolated from the Company, the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets and the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

The Company's loan participations sold subject to this guidance which met the conditions to be treated as a sale were recorded as such. Any securities sold under agreements to repurchase that did not meet the sale criteria are treated as a secured borrowing with pledge of collateral and included in securities available for sale and repurchase agreements in the Company's consolidated balance sheets.

<u>Stock-Based Compensation</u>—Stock-based compensation is recognized as compensation cost in the consolidated statements of income based on the fair value on the date of grant. A Black-Scholes model is utilized to estimate the fair value of stock options and the market value of the Company's common stock at the date of grant is used as the estimate of fair value of restricted stock. Compensation expense for awards not based on performance criteria is recognized over the required service period, on a straight-line basis. The impact of forfeitures is recognized as they occur.

The number of shares earned under the Company's performance-based restricted stock award agreements is based on the achievement of certain levels of certain performance goals. The fair value of performance-based restricted stock is estimated based on the market value of the Company's common stock at the date of grant. Compensation expense for performance-based restricted stock is recognized for the probable award level over the period estimated to achieve the performance conditions and other goals, on a straight-line basis. If the probable award level and/or the period estimated to be achieved change, compensation expense will be adjusted via a cumulative catch-up adjustment to reflect these changes. The performance conditions and other goals must be achieved within five years or the awards expire.

<u>Earnings Per Share</u>—Basic earnings per common share is computed as net income available to common shareholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per common share is computed using the weighted-average shares determined for the basic earnings per share computation plus the potential dilution that could occur if outstanding stock options were exercised and restricted stock awards were vested and converted into common stock using the treasury stock method.

<u>Share Repurchase Program</u>—In July 2019, the Company's Board of Directors authorized a share repurchase program under which the Company may repurchase up to \$40.0 million of the Company's common stock through September 30, 2020. During 2019, 100 shares were repurchased at \$27.98 per share and retired and returned to the status of authorized but unissued shares.

Accounting Standards Recently Adopted

The Company adopted ASU 2016-02, Leases (Topic 842) on January 1, 2019, using the effective date as the date of initial adoption. The Company elected to apply certain practical expedients for transition, and under those expedients the Company did not reassess prior accounting decisions regarding the identification, classification and initial direct costs for leases existing at the effective date. The Company also elected to use hindsight in determining lease term when considering options to extend the lease and excluded short-term leases (defined as lease terms of 12 months or less). The Company elected to separate non-lease components from lease components in its application of ASU 2016-02. At adoption, the Company recorded right-of-use assets totaling \$13.2 million, which represented the Company's right to use, or control the use of, specified assets for their lease terms, and the Company recorded lease liabilities totaling \$15.5 million, which represented the Company's liability to make lease payments under these leases. Accrued lease obligations and lease incentive liabilities totaling \$2.3 million that were in other liabilities at December 31, 2018 were reversed as part of the adoption during the first quarter of 2019. The ASU 2016-02 standard applied to all leases existing at the date of initial adoption. The Company's financial statements and related footnotes were not updated for ASU 2016-02 for dates and periods before the date of adoption. See Note 16.

Accounting Standards Not Yet Adopted

ASU 2016-13, Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. ASU 2016-13 requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions and reasonable and supportable forecasts and requires enhanced disclosures related to the significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization's portfolio. In addition, ASU 2016-13 amends the accounting for credit losses on available for sale debt securities and purchased financial assets with credit deterioration. The amendments affect loans, debt securities, other receivables, off-balance sheet credit exposures, and any other financial assets not excluded from the scope that have the contractual right to receive cash. The Company's adoption of ASU 2016-13 was effective on January 1, 2020.

The Company has completed its evaluation and assessment of ASU 2016-13 and finalized the impact upon adoption of ASU 2016-13 on the consolidated financial statements. The Company developed a functional working group, with the assistance of an outside consultant, which is comprised of individuals from various areas including credit, risk management, and accounting, among others. The Company has determined an aged based vintage model, or the Vintage

Model, to be the most appropriate model as it provides the best predictor of credit risks associated with the loan portfolio and reasonably captures the expected life of loan losses associated with each segment of loans. The aging of the loans is determined by an identifiable credit decision date, and the loans will be segmented into pools based on similar risks characteristics and credit risk indicators. The methodology associated with utilizing the Vintage Model takes into consideration historical loss rates associated with each segment as well as other qualitative factors and economic forecasts to derive an allowance for credit losses associated with expected credit losses within the loan portfolio. The Company has finalized the processes and internal controls related to the estimation process, model development and validation, as well as system configuration. Existing technology has been adapted to conform to the requirements of ASU 2016-13 and the Company has utilized a third-party vendor solution to assist in the application of ASU 2016-13.

The implementation of ASU 2016-13 also impacted the methodology for determining an allowance for credit losses associated with the Company's off-balance sheet credit exposures. These exposures primarily related to unfunded commitments with borrowers through line of credit or letter of credit arrangements. The Company has utilized similar methodology associated with the Vintage Model and considers historical utilization rates to determine an appropriate allowance for credit losses.

The adoption of ASU 2016-13 will require changes to the Company's accounting policies and disclosures for credit losses on financial instruments. The adoption of ASU 2016-13 did not have any impact on held-to-maturity securities as the Company did not hold any as of December 31, 2019. Additionally, the Company assessed the impact of ASU 2016-13 on the available for sale securities utilizing various qualitative factors and determined there to be no credit losses within the portfolio requiring an allowance upon adoption. The Company did not have any purchased financial assets with credit deterioration as of January 1, 2020.

The Company has determined that the expected adoption of ASU 2016-13 will increase the allowance for credit losses by approximately \$874,000 associated with the loan portfolio and increase other liabilities by approximately \$3.0 million pertaining to an allowance for credit losses associated with the Company's unfunded commitments through a one-time cumulative effect adjustment to retained earnings. As the Company is currently finalizing the execution of its implementation controls and processes in which the estimate may be subject to further refinement, the ultimate impact of the adoption of ASU 2016-13 as of January 1, 2020 could differ from current expectations.

<u>Cash Flow Reporting</u>—Supplemental disclosures of cash flow information are as follows for the periods shown below:

	Years Ended December 31,							
(Dollars in thousands)		2019		2018		2017		
Supplemental disclosures of cash flow information:								
Cash paid for taxes	\$	13,710	\$	11,627	\$	13,752		
Cash paid for interest		17,040		10,803		9,094		
Supplemental disclosures of non-cash flow information:								
Dividends accrued		1,306		43		11		
Operating lease right-to-use asset obtained in exchange for lease								
liabilities		14,499		_		_		
Repossessed real estate and other assets		121		349		881		

NOTE 2: SECURITIES

The amortized cost and fair values of investments in securities as of the dates shown below were as follows:

(Dollars in thousands)	A	Amortized Cost	Uı	Gross nrealized Gains	U	Gross nrealized Losses	F	Fair Value
December 31, 2019								
Debt securities available for sale:								
State and municipal securities	\$	51,525	\$	1,761	\$	(7)	\$	53,279
U.S. agency securities:								
Collateralized mortgage obligations		55,784		324		(119)		55,989
Mortgage-backed securities		119,787		1,315		(255)		120,847
Equity securities		1,155		_		(8)		1,147
Total	\$	228,251	\$	3,400	\$	(389)	\$	231,262
Debt securities held to maturity:								
Mortgage-backed securities	\$		\$		\$	_	\$	_
(Dollars in thousands)	A	Amortized Cost	Uı	Gross nrealized Gains		Gross nrealized Losses	F	Fair Value
December 31, 2018			Uı	nrealized		nrealized	F	Sair Value
December 31, 2018 Debt securities available for sale: State and municipal securities			**************************************	nrealized		nrealized		57,691
December 31, 2018 Debt securities available for sale: State and municipal securities		Cost		nrealized Gains	_	nrealized Losses		57,691
December 31, 2018 Debt securities available for sale: State and municipal securities. U.S. agency securities: Debt securities.		57,972 17,315		nrealized Gains	_	nrealized Losses (626) (434)		57,691 16,881
December 31, 2018 Debt securities available for sale: State and municipal securities. U.S. agency securities: Debt securities. Collateralized mortgage obligations.		57,972 17,315 66,438		Gains 345	_	(626) (434) (1,122)		57,691 16,881 65,414
December 31, 2018 Debt securities available for sale: State and municipal securities U.S. agency securities: Debt securities Collateralized mortgage obligations. Mortgage-backed securities		57,972 17,315 66,438 90,845		nrealized Gains 345 98	_	(626) (434) (1,122) (2,216)		57,691 16,881 65,414 88,859
December 31, 2018 Debt securities available for sale: State and municipal securities. U.S. agency securities: Debt securities. Collateralized mortgage obligations.		57,972 17,315 66,438		nrealized Gains 345 98	_	(626) (434) (1,122) (2,216) (41)		57,691 16,881 65,414 88,859 1,088
December 31, 2018 Debt securities available for sale: State and municipal securities. U.S. agency securities: Debt securities. Collateralized mortgage obligations. Mortgage-backed securities Equity securities.	\$	57,972 17,315 66,438 90,845 1,129	\$	345 — 98 230	\$	(626) (434) (1,122) (2,216)	\$	57,691 16,881 65,414 88,859

The amortized cost and estimated fair value of securities by contractual maturities as of the dates shown below were as follows:

Available for Sale	Held to Maturity			
	ortized Cost	Fair Value		
19				
ng in:				
\$ 2,535 \$ 2,532 \$	_ 5	\$ —		
years	_			
10 years	_			
\$ 228,251 \$ 231,262 \$		\$ —		
ng in:				
\$ 3,224 \$ 3,188 \$	_ 9	\$ —		
		_		
		_		
	31	32		
\$ 233,699 \$ 229,933 \$	31	\$ 32		
\$\frac{\\$ \ 228,251 \}{8} \frac{\\$ 231,262 \}{8}\$ Its Ing in: \$\frac{3,224}{22,784} \\$ 3,188 \\$ Ityears. \$\frac{22,784}{13,127} \frac{13,062}{130,62} \$\frac{194,564}{191,313}\$				

Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Securities with a carrying amount of \$20.4 million, \$56.5 million and \$6.1 million were sold during the years ended December 31, 2019, 2018 and 2017, respectively. At December 31, 2019 and 2018, securities with a carrying amount of approximately \$50.8 million and \$49.9 million, respectively, were pledged to secure public deposits, repurchase agreements and for other purposes required or permitted by law.

The Company held 27 and 100 securities at December 31, 2019 and 2018, respectively, that were in a gross unrealized loss position for 12 months or more as illustrated in the table below. The unrealized losses are attributable primarily to changes in market interest rates relative to those available when the securities were acquired. The fair value of these securities is expected to recover as the securities reach their maturity or re-pricing date, or if changes in market rates for such investments decline. Management does not believe that any of the securities that the Company holds are impaired due to reasons of credit quality and believes the unrealized losses detailed in the tables below are temporary. No impairment loss has been recorded in the Company's consolidated statements of income for the years ended December 31, 2019, 2018 and 2017.

Securities with unrealized losses as of the dates shown below, aggregated by investment category and the length of time were as follows:

		Less Than T	welve N	Ionths		Twelve Mo	nths or More		
(Dollars in thousands)		Fair Value	τ	Gross Inrealized Losses		Fair Value	Gross Unrealized Losses		
December 31, 2019								<u> </u>	
Debt securities available for sale:									
State and municipal securities U.S. agency securities:	\$	3,539	\$	(7)	\$	106	\$	_	
Collateralized mortgage obligations		10,687		(46)		7,994		(73)	
Mortgage-backed securities		11,628		(26)		21,745		(229)	
Equity securities		´—		_		1,147		(8)	
1 7	\$	25,854	\$	(79)	\$	30,992	\$	(310)	
December 31, 2018									
Debt securities available for sale:									
State and municipal securities U.S. agency securities:	\$	20,892	\$	(324)	\$	6,584	\$	(302)	
Debt securities						16,882		(434)	
Collateralized mortgage obligations		8,854		(81)		46,157		(1,041)	
		,		` ′		46,183		(1,041) $(1,848)$	
Mortgage-backed securities		21,745		(368)		,		`	
Equity securities	Φ.	<u> </u>	Ф	(772)	ф	1,088	Φ.	(41)	
	3	51,491	\$	(773)	\$	116,894	3	(3,666)	

NOTE 3: EQUITY INVESTMENTS

The Company's unconsolidated investments that are considered equity securities as they represent ownership interests such as common or preferred stock were as follows for the dates indicated below.

	Decem	ıber 31,	
(Dollars in thousands)	 2019		2018
Federal Reserve stock	\$ 9,271	\$	9,271
Federal Home Loan Bank stock	4,249		1,250
The Independent Bankers Financial Corporation stock	141		141
Community Reinvestment Act investments	3,049		2,364
	\$ 16,710	\$	13,026

Banks that are members of the Federal Home Loan Bank are required to maintain a stock investment in the Federal Home Loan Bank calculated as a percentage of aggregate outstanding mortgages, outstanding Federal Home Loan Bank advances and other financial instruments. As a member of the Federal Reserve System, the Bank is required to annually subscribe to Federal Reserve Bank stock in specific ratios to the Bank's equity. Although Federal Home Loan Bank and Federal Reserve Bank stock are considered equity securities, they do not have readily determinable fair values because ownership is restricted, and they lack a market. These investments can be sold back only at their par value of \$100

per share and can only be sold to the Federal Home Loan Banks or Federal Reserve Banks or to another member institution. In addition, the equity ownership rights are more limited than would be the case for a public company because of the oversight role exercised by regulators in the process of budgeting and approving dividends. As a result, these investments are carried at cost and evaluated for impairment.

The Company also holds an investment in the stock of The Independent Bankers Financial Corporation, which has limited marketability. As a result, this investment is carried at cost and evaluated for impairment.

The Company has investments in two private investment funds and a limited partnership. These investments are qualified Community Reinvestment Act, or CRA, investments under the Small Business Investment Company program of the SBA. There are limited to no observable price changes in orderly transactions for identical investments or similar investments from the same issuers that are actively traded, and as a result, these investments are stated at cost. At December 31, 2019 and 2018, the Company had \$4.9 million and \$3.0 million, respectively, in outstanding unfunded commitments to these funds, which are subject to call. The Company entered into a new CRA investment agreement in December 2019, with a commitment of \$2.5 million and as of December 31, 2019, the Company had made no investments into this fund.

The Company's equity investments are evaluated for impairment based on an assessment of qualitative indicators. Impairment indicators to be considered include, but are not limited to (i) a significant deterioration in the earnings, performance, credit rating, asset quality or business prospects of the investee, (ii) a significant adverse change in the regulatory, economic or technological environment of the investee, (iii) a significant adverse change in the general market conditions of either the geographical area or the industry in which the investee operates, (iv) a bona fide offer to purchase, an offer by the investee to sell, or completed auction process for the same or similar investment for an amount less than the carrying amount of the investment. There were no such qualitative indicators as of December 31, 2019.

NOTE 4: LOANS

Loans by loan class as of the dates shown below were as follows:

			Decem	iber 3	1,	
(Dollars in thousands)		2019			2018	
Commercial and industrial	\$	527,607	19.9%	\$	519,779	21.2%
Real estate:						
Commercial real estate		900,746	34.0%		795,733	32.4%
Construction and development		527,812	19.9%		515,533	21.0%
1-4 family residential		280,192	10.6%		282,011	11.5%
Multi-family residential		277,209	10.5%		221,194	9.0%
Consumer		36,782	1.4%		39,421	1.6%
Agriculture		9,812	0.4%		11,076	0.5%
Other		86,513	3.3%		68,382	2.8%
Total gross loans		2,646,673	100.0%		2,453,129	100.0%
Less allowance for loan loss		(25,280)			(23,693)	
Less deferred loan fees and unearned discounts		(6,125)			(6,306)	
Less loans held for sale		(1,463)				
Loans, net	\$	2,613,805		\$	2,423,130	
	_			_		

Accrued interest receivable for loans is \$7.5 million and \$6.8 million at December 31, 2019 and 2018, respectively and is included in other assets in the consolidated balance sheets.

Loan Participations Purchased and Sold

From time to time, the Company will acquire and dispose of interests in loans under participation agreements with other financial institutions. Loan participations purchased and sold during the years ending December 31, 2019, 2018 and 2017, by loan class, are summarized as follows:

(Dollars in thousands)	P	rticipations urchased uring the Period		rticipations Sold uring the Period
December 31, 2019	_	1 CI IOU	_	1 Ci iou
Commercial real estate	\$	2,314	\$	31,868
December 31, 2018				
Commercial and industrial	\$	7,000	\$	1,620
Commercial real estate		28,281		35,000
Construction and development		_		9,301
1	\$	35,281	\$	45,921
December 31, 2017			-	
Commercial and industrial	\$		\$	23,000
Commercial real estate		12,885		20,505
Construction and development		5,606		2,562
•	\$	18,491	\$	46,067

Loans Guaranteed by the SBA

The Company participates in the SBA loan program. When advantageous, the Company will sell the guaranteed portions of these loans with servicing retained. SBA loans that were sold with servicing retained during the years ended December 31, 2019, 2018 and 2017 were \$4.4 million, \$2.0 million and \$2.2 million, respectively. Net gains recognized on sales of SBA loans were \$330,000, \$153,000 and \$149,000 for the years ended December 31, 2019, 2018 and 2017, respectively and are included in net gain on sales of assets in the consolidated income statements.

NOTE 5: LOAN PERFORMANCE

Nonaccrual loans, segregated by loan class, as of the dates shown below were as follows:

	Decem	ber 31	,
(Dollars in thousands)	 2019		2018
Commercial and industrial	\$ 596	\$	1,317
Real estate:			
Commercial real estate	67		1,517
1-4 family residential	314		656
Total nonaccrual loans	\$ 977	\$	3,490

Interest income that would have been earned under the original terms of the nonaccrual loans was \$57,000 \$163,000 and \$402,000 for the years ended December 31, 2019, 2018 and 2017, respectively.

The following is an aging analysis of the Company's past due loans, segregated by loan class, as of the dates shown below:

	20 to	o 59 davs	60 4	to 89 days		days or reater	T	otal past	т	otal current			90 days t due and
(Dollars in thousands)		ast due		ast due	- 0	ast due	10	due	1	loans	Т	otal loans	accruing
December 31, 2019									_				 <u>s</u>
Commercial and industrial	\$	664	\$	31	\$	240	\$	935	\$	526,672	\$	527,607	\$
Real estate:													
Commercial real estate		865		_				865		899,881		900,746	_
Construction and development.		_		532		_		532		527,280		527,812	_
1-4 family residential		499		_				499		279,693		280,192	_
Multi-family residential		_		_		_		_		277,209		277,209	_
Consumer		43		_		_		43		36,739		36,782	_
Agriculture		_		_		_		_		9,812		9,812	_
Other							_			86,513		86,513	
Total loans	\$	2,071	\$	563	\$	240	\$	2,874	\$	2,643,799	\$ 2	2,646,673	\$
December 31, 2018													
Commercial and industrial	\$	178	\$	881	\$	154	\$	1,213	\$	518,566	\$	519,779	\$ _
Real estate:													
Commercial real estate		68		1,089		605		1,762		793,971		795,733	_
Construction and development.		359		4,204		_		4,563		510,970		515,533	_
1-4 family residential		395		111		36		542		281,469		282,011	_
Multi-family residential		_		_		_		_		221,194		221,194	_
Consumer		28		_		_		28		39,393		39,421	_
Agriculture		_		_		_		_		11,076		11,076	_
Other										68,382		68,382	
Total loans	\$	1,028	\$	6,285	\$	795	\$	8,108	\$	2,445,021	\$ 2	2,453,129	\$

Loans restructured due to the borrower's financial difficulties during the years ending December 31, 2019 and 2018, which remain outstanding as of the end of those periods were as follows:

]	Post-m	odificat	ion rec	orded inv	vestn	nent
(Dollars in thousands)	Number of Loans	Ou R	modification tstanding tecorded vestment	tructured syments		tended aturity	Matu Resti	tended irity and ructured yments	Ex	xtended Maturity, Restructured Payments and Adjusted Interest Rate
December 31, 2019										
Commercial and industrial	3	\$	202	\$ 39	\$		\$	163	\$	_
1-4 family residential	1		111	_				_		115
Total	4	\$	313	\$ 39	\$		\$	163	\$	115
December 31, 2018										
Commercial and industrial	6	\$	1,419	\$ 916	\$		\$	503	\$	_
Commercial real estate	3		1,406	1,406		_		_		_
Other	1		1,646	<u> </u>						1,646
Total	10	\$	4,471	\$ 2,322	\$		\$	503	\$	1,646

The recorded investment in troubled debt restructurings was \$8.8 million and \$11.4 million as of December 31, 2019 and 2018, respectively. At December 31, 2019 and 2018, \$393,000 and \$1.8 million of restructured loans were nonaccrual loans and \$8.4 million and \$9.6 million of restructured loans were accruing interest as of those periods. At December 31, 2019 and 2018, the Company had outstanding commitment to potentially fund \$2.0 million and \$2.1 million on a line of credit previously restructured.

There were no loans modified as a troubled debt restructured loan within the previous 12 months and for which there was a payment default. For purposes of this disclosure, a default is a loan modified as a troubled debt restructuring where the borrower is 90 days past due or results in the foreclosure and repossession of the applicable collateral.

NOTE 6: ALLOWANCE FOR LOAN LOSSES

Activity in the allowance for loan losses, segregated by loan class, for the years indicated below was as follows:

						Real E	stat	e								
	Co	mmercial and	Co	mmercial	Coı	nstruction and	1-	4 family	Mu	ılti-family						
(Dollars in thousands)	in	dustrial	re	al estate	dev	elopment	re	sidential	re	sidential	Cor	ısumer	Agri	culture	Other	Total
December 31, 2019																
Beginning balance	\$	7,719	\$	6,730	\$	4,298	\$	2,281	\$	1,511	\$	387	\$	62	\$ 705	\$ 23,693
Provision for loan loss		715		1,209		148		(15)		188		27		2	111	2,385
Charge-offs		(1,252)		(45)		_		(12)		_		(97)		_	(52)	(1,458)
Recoveries		489		81				3				71		10	6	660
Net (charge-offs) recoveries		(763)		36		_		(9)		_		(26)		10	(46)	(798)
Ending balance	\$	7,671	\$	7,975	\$	4,446	\$	2,257	\$	1,699	\$	388	\$	74	\$ 770	\$ 25,280
Period-end amount allocated to:																
Specific reserve	\$	416	\$	_	\$	_	\$	15	\$	_	\$	_	\$	_	\$ 6	\$ 437
General reserve		7,255		7,975		4,446		2,242		1,699		388		74	764	24,843
Total	\$	7,671	\$	7,975	\$	4,446	\$	2,257	\$	1,699	\$	388	\$	74	\$ 770	\$ 25,280

			_			Real E	stat	e								
	Co	mmercial and	Co	mmercial	Coı	nstruction and	1-	4 family	Mu	lti-family						
(Dollars in thousands)	in	dustrial	r	eal estate	dev	elopment	re	sidential	re	sidential	Co	nsumer	Agr	iculture	Other	Total
December 31, 2018										,						
Beginning balance	\$	7,257	\$	10,375	\$	3,482	\$	1,326	\$	1,419	\$	566	\$	68	\$ 285	\$ 24,778
Provision (recapture) for loan loss		(347)		(3,494)		817		953		92		(181)		(16)	420	(1,756)
Charge-offs		(1,928)		(171)		(1)		(4)		_		(1)		_	(3)	(2,108)
Recoveries		2,737		20				6				3		10	3	2,779
Net (charge-offs) recoveries		809		(151)		(1)		2		_		2		10		671
Ending balance	\$	7,719	\$	6,730	\$	4,298	\$	2,281	\$	1,511	\$	387	\$	62	\$ 705	\$ 23,693
Period-end amount allocated to:							_									
Specific reserve	\$	525	\$	44	\$	_	\$	89	\$	_	\$	_	\$	_	\$ 100	\$ 758
General reserve		7,194		6,686		4,298		2,192		1,511		387		62	605	22,935
Total	\$	7,719	\$	6,730	\$	4,298	\$	2,281	\$	1,511	\$	387	\$	62	\$ 705	\$ 23,693

						Real E	stat	e								
	Cor	mmercial and	Co	mmercial	Co	nstruction and	1-	4 family	Mı	ulti-family						
(Dollars in thousands)	in	dustrial	r	eal estate	dev	elopment	re	sidential	re	esidential	Co	nsumer	Agri	culture	Other	Total
December 31, 2017																
Beginning balance	\$	6,409	\$	10,770	\$	4,598	\$	1,286	\$	916	\$	353	\$	79	\$ 595	\$ 25,006
Provision (recapture) for loan loss.		642		(284)		(1,116)		35		503		263		(63)	(318)	(338)
Charge-offs		(904)		(120)		_		(8)		_		(93)		_	_	(1,125)
Recoveries		1,110		9				13				43		52	- 8	1,235
Net (charge-offs) recoveries .		206		(111)				5				(50)		52	8	110
Ending balance	\$	7,257	\$	10,375	\$	3,482	\$	1,326	\$	1,419	\$	566	\$	68	\$ 285	\$ 24,778
Period-end amount allocated to:			_										-			
Specific reserve	\$	852	\$	64	\$	_	\$	119	\$	_	\$	_	\$	_	\$ —	\$ 1,035
General reserve		6,405		10,311		3,482		1,207		1,419		566		68	285	23,743
Total	\$	7,257	\$	10,375	\$	3,482	\$	1,326	\$	1,419	\$	566	\$	68	\$ 285	\$ 24,778

Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories. In addition to the amounts indicated in the tables above, the Company had a reserve for loan losses on unfunded commitments of \$378,000 recorded in other liabilities as of December 31, 2019 and 2018.

Risk Grading

As part of the on-going monitoring of the credit quality of the Company's loan portfolio and methodology for calculating the allowance for loan losses, management assigns and tracks loan grades, as described below, that are used as credit quality indicators.

<u>Pass</u>—Credits in this category contain an acceptable amount of risk.

<u>Special Mention</u>—Credits in this category contain more than the normal amount of risk and are referred to as "special mention" in accordance with regulatory guidelines. These credits possess clearly identifiable temporary weaknesses or trends that, if not corrected or revised, may result in a condition that exposes the Company to higher level of risk of loss.

<u>Substandard</u>—Credits in this category are "substandard" in accordance with regulatory guidelines and of unsatisfactory credit quality with well-defined weaknesses or weaknesses that jeopardize the liquidation of the debt. Credits in this category are inadequately protected by the current sound worth and paying capacity of the obligor or the collateral pledged, if any. Often, the assets in this category will have a valuation allowance representative of management's estimated loss that is probable to be incurred. Loans deemed substandard and on nonaccrual status are considered impaired and are individually evaluated for impairment.

<u>Doubtful</u>—Credits in this category are considered "doubtful" in accordance with regulatory guidelines, are placed on nonaccrual status and may be dependent upon collateral having a value that is difficult to determine or upon some near-term event which lacks certainty. Generally, these credits will have a valuation allowance based upon management's best estimate of the losses probable to occur in the liquidation of the debt.

<u>Loss</u>—Credits in this category are considered "loss" in accordance with regulatory guidelines and are considered uncollectible and of such little value as to question their continued existence as assets on the Company's financial statements. Such credits are to be charged off or charged down when payment is acknowledged to be uncertain or when the timing or value of payments cannot be determined. This category does not intend to imply that the debt or some portion of it will never be paid, nor does it in any way imply that the debt will be forgiven.

The Company had no loans graded "loss" or "doubtful" at December 31, 2019 and 2018.

Loans by risk grades and loan class as of the dates shown below were as follows:

(Dollars in thousands)	 Pass	Special Mention	Su	bstandard_	_1	Total Loans
December 31, 2019						
Commercial and industrial	\$ 513,417	\$ 2,963	\$	11,227	\$	527,607
Real estate:						
Commercial real estate	876,207	18,570		5,969		900,746
Construction and development	515,247	12,565		_		527,812
1-4 family residential	274,731	594		4,867		280,192
Multi-family residential	277,209	_		_		277,209
Consumer	36,566	_		216		36,782
Agriculture	9,733	50		29		9,812
Other	79,860	_		6,653		86,513
Total loans	\$ 2,582,970	\$ 34,742	\$	28,961	\$	2,646,673
(Dollars in thousands)	Pass	Special Mention	Su	bstandard	1	Total Loans
December 31, 2018	 	 				
Commercial and industrial	\$ 504,425	\$ 5,768	\$	9,586	\$	519,779
Real estate:						
Commercial real estate	781,035	10,370		4,328		795,733
Construction and development	511,329	4,204		_		515,533
1-4 family residential	274,781	2,175		5,055		282,011
Multi-family residential	221,194	_		_		221,194
Consumer	39,140	246		35		39,421
Agriculture	11,048	_		28		11,076
Other				6,813		68,382
	61,569			0,013		00,302

Loan Impairment Assessment

The recorded investment in impaired loans, as of the dates shown below, by loan class and disaggregated based on the Company's impairment methodology were as follows:

(Dollars in thousands)	Unpai Contract Princip Balanc	Inv w	ecorded estment ith No owance	Ir	Recorded nvestment h Allowance	ent Recorded			elated owance	R In	Average Recorded Evestment ar-to-Date	
December 31, 2019												
Commercial and industrial	\$ 1,1	11	\$	300	\$	699	\$	999	\$	416	\$	2,452
Real estate:												
Commercial real estate	1,4	07		1,404		_		1,404				2,165
1-4 family residential	3,7	61		2,166		1,485		3,651		15		4,020
Consumer	2	10		210				210		_		128
Other	6,6	53		5,411		1,242		6,653		6		6,825
Total loans	\$ 13,1	42	\$	9,491	\$	3,426	\$ 1	12,917	\$	437	\$	15,590

(Dollars in thousands)	Unpaid Contractual Principal Balance	Recorded Investment with No Allowance	Recorded Investment with Allowance	Total Recorded Related Investment Allowance		Average Recorded Investment Year-to-Date
December 31, 2018						
Commercial and industrial	\$ 4,378	\$ 3,642	\$ 635	\$ 4,277	\$ 525	\$ 5,771
Real estate:						
Commercial real estate	4,128	3,374	596	3,970	44	6,135
Construction and development	_	_	_			139
1-4 family residential	4,551	2,612	1,824	4,436	89	4,597
Consumer	_					7
Other	6,814	5,572	1,241	6,813	100	7,841
Total loans	\$ 19,871	\$ 15,200	\$ 4,296	\$ 19,496	\$ 758	\$ 24,490

Interest income recognized on impaired loans was \$665,000, \$996,000 and \$1.1 million for the years ended December 31, 2019, 2018 and 2017, respectively.

The recorded investment in loans as of the dates shown below by loan class and based on the Company's impairment methodology was as follows:

		December 31, 20	19	December 31, 2018				
(Dollars in thousands)	Individually Evaluated for Impairment	Collectively Evaluated for Total Impairment Loans		Individually Collectively Evaluated for Impairment Impairment		Total Loans		
Commercial and industrial	\$ 999	\$ 526,608	\$ 527,607	\$ 4,277	\$ 515,502	\$ 519,779		
Real estate:								
Commercial real estate	1,404	899,342	900,746	3,970	791,763	795,733		
Construction and development.	_	527,812	527,812		515,533	515,533		
1-4 family residential	3,651	276,541	280,192	4,436	277,575	282,011		
Multi-family residential		277,209	277,209		221,194	221,194		
Consumer	210	36,572	36,782		39,421	39,421		
Agriculture	_	9,812	9,812		11,076	11,076		
Other	6,653	79,860	86,513	6,813	61,569	68,382		
Total	\$ 12,917	\$ 2,633,756	\$ 2,646,673	\$ 19,496	\$ 2,433,633	\$ 2,453,129		

At December 31, 2019 and 2018, the allowance allocated to specific reserves for loans individually evaluated for impairment was \$437,000 and \$758,000, respectively.

NOTE 7: PREMISES AND EQUIPMENT

The components of premises and equipment as the dates shown below were as follows:

	December 31,				
(Dollars in thousands)		2019	2018		
Land	\$	13,466	\$	13,466	
Buildings and leasehold improvements		53,869		52,188	
Furniture and equipment		15,917		15,426	
Vehicles		203		232	
Construction in progress		343		177	
	<u> </u>	83,798	·	81,489	
Less accumulated depreciation		(32,923)		(29,867)	
Premises and equipment, net	\$	50,875	\$	51,622	

Depreciation expense was \$3.2 million, \$3.3 million and \$3.4 million for the years ended December 31, 2019, 2018 and 2017, respectively, which is included in net occupancy expense on the Company's consolidated statements of income. A net loss of \$32,000 on dispositions of premises and equipment for the year ended December 31, 2019 and net gains of \$31,000 and \$742,000 for the years ended December 31, 2018 and 2017, respectively, were recognized and are included in net gain on sale of assets in the consolidated statements of income.

NOTE 8: GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill was \$81.0 million at December 31, 2019 and 2018 and there have been no changes in goodwill during those years. Based on the results of the Company's assessment, management does not believe any impairment of goodwill or other intangible assets existed at December 31, 2019 or 2018.

Other intangibles, net of accumulated amortization, were as follows as of the dates shown below:

(Dollars in thousands)	Weighted- Average Remaining Amortization Period	I	Gross ntangible Assets		Accumulated Amortization						Net tangible Assets
December 31, 2019		· <u></u>									
Core deposits	4.2 years	\$	13,750	\$	(12,979)	\$	771				
Customer relationships	9.0 years		6,629		(2,651)		3,978				
Servicing assets	12.8 years		368		(179)		189				
Total other intangible assets, net		\$	20,747	\$	(15,809)	\$	4,938				
December 31, 2018											
Core deposits	5.2 years	\$	13,750	\$	(12,561)	\$	1,189				
Customer relationships	10.0 years		6,629		(2,209)		4,420				
Servicing assets	14.4 years		311		(145)		166				
Total other intangible assets, net		\$	20,690	\$	(14,915)	\$	5,775				

Servicing Assets

Changes in the related servicing assets as of the dates shown indicated below were as follows:

	Years Ended December 31,						
(Dollars in thousands)		2019		2018			
Balance at beginning of year	\$	166	\$	209			
Increase from loan sales		87		38			
Decrease from serviced loans paid off or foreclosed		(30)		(48)			
Amortization		(34)		(33)			
Balance at end of period	\$	189	\$	166			

Estimated future amortization for core deposits and customer relationship intangible assets was as follows for the date shown below:

(Dollars in thousands)	December 31, 2019
2020	768
2021	675
2022	584
2023	495
2024	459
Thereafter	1,768
Total	\$ 4,749

NOTE 9: BANK-OWNED LIFE INSURANCE

During 2019, the Company received proceeds in the amount of \$4.7 million as the owner and beneficiary under a bank-owned life insurance policy as the result of the death of a former employee, and the Company recorded a gain of \$3.3 million.

Bank-owned life insurance policies and the net change in cash surrender value during the periods shown below were as follows:

	Years Ended December 31,								
(Dollars in thousands)		2019		2018	2017				
Balance at beginning of period	\$	71,525	\$	68,010	\$	51,430			
Purchases		_		1,700		15,000			
Redemptions		(4,655)							
Net change in cash surrender value		5,011		1,815		1,580			
Balance at end of period	\$	71,881	\$	71,525	\$	68,010			

NOTE 10: DEPOSITS

Deposits as of the dates shown below were as follows:

	December 31,			1,
(Dollars in thousands)		2019		2018
Interest-bearing demand accounts	\$	369,744	\$	387,457
Money market accounts		805,942		737,770
Saving accounts		92,183		96,962
Certificates and other time deposits, \$100,000 or greater		208,018		189,007
Certificates and other time deposits, less than \$100,000		191,640		172,028
Total interest-bearing deposits		1,667,527		1,583,224
Noninterest-bearing deposits		1,184,861		1,183,058
Total deposits	\$	2,852,388	\$	2,766,282

Scheduled maturities of time deposits as of the date shown below were as follows:

(Dollars in thousands)	Dece	mber 31, 2019
Three months or less	\$	77,801
Over three months through six months		57,362
Over six months through 12 months		163,055
Over 12 months through three years		70,490
Over three years		30,950
Total	\$	399,658

At December 31, 2019 and 2018, the Company had \$56.8 million and \$51.5 million in deposits from public entities and brokered deposits of \$128.9 million and \$104.5 million, respectively. Accrued interest payable for deposits was \$931,000 and \$594,000 at December 31, 2019 and 2018, respectively, and is included in other liabilities in the consolidated balance sheets. The Company had no major concentrations of deposits at December 31, 2019 or 2018 from any single or related groups of depositors.

NOTE 11: LINES OF CREDIT

Frost Line of Credit

The Company has entered into a loan agreement with Frost Bank, which provides for a \$30.0 million revolving line of credit, or Line of Credit Agreement. The Company can make draws on the Line of Credit Agreement for a period of 24 months, which began on December 13, 2019, after which the Company will not be permitted to make further draws and the outstanding balance will amortize over a period of 60 months. Interest accrues on outstanding borrowings at a rate equal to the maximum "Latest" U.S. prime rate of interest per annum and payable quarterly in the first 12 months and thereafter quarterly principal and interest payments are required over a term of 60 months. The entire outstanding balance and unpaid interest is payable in full on December 13, 2026.

The Company may prepay the principal amount of the Line of Credit without premium or penalty. The obligations of the Company under the Line of Credit Agreement are secured by a valid and perfected first priority lien on all of the issued and outstanding shares of capital stock of the Bank.

Covenants made under the Line of Credit Agreement include, among other things, the Company maintaining tangible net worth of not less than \$300 million, the Company maintaining free cash flow coverage ratio of not less than 1.25 to 1.00, the Bank's Texas Ratio (as defined in the Line of Credit Agreement) not to exceed 15%, the Bank's Total Capital Ratio (as defined under the Line of Credit Agreement) of not less than 12% and restrictions on the ability of the Company and its subsidiaries to incur certain additional debt. The Company was in compliance with these covenants at December 31, 2019.

Additional Lines of Credit

The Federal Home Loan Bank allows us to borrow on a blanket floating lien status collateralized by certain loans. At December 31, 2019 and 2018, total borrowing capacity of \$1.0 billion and \$919.9 million, respectively, was available under this arrangement. During the year ended December 31, 2019, funds were borrowed under this agreement on both a short-term basis and long-term basis, and at December 31, 2019, \$50.0 million of Federal Home Loan Bank advances were outstanding. During the year ended December 31, 2018, funds were borrowed under this agreement on a short-term basis only, and at December 31, 2018, there were no outstanding Federal Home Loan Bank advances. The average balances for Federal Home Loan Bank advances outstanding at December 31, 2019 and 2018 was \$61.6 million and \$3.4 million, respectively, and the weighted-average interest rate for the years ended December 31, 2019 and 2018 was 2.25% and 2.18%, respectively.

(Dollars in thousands)	Decen	nber 31, 2019
2020	\$	
2021		_
2022		10,000
2023		20,000
2024		20,000
Thereafter		_
Total	\$	50,000

At December 31, 2019 and 2018, the Company maintained four federal funds lines of credit with commercial banks that provide for the availability to borrow up to an aggregate of \$75.0 million in federal funds. There were no funds under these lines of credit outstanding as of December 31, 2019 and 2018.

NOTE 12: JUNIOR SUBORDINATED DEBT

Prior to being acquired in 2007 by the Company, County Bancshares, Inc. received proceeds of junior subordinated debt held by a trust funded by common securities, all of which were purchased by County Bancshares, Inc. and trust preferred securities in the amount of \$5.5 million that were held by other investors. Funds raised by the trust totaling \$5.7 million were loaned to County Bancshares, Inc. in the form of junior subordinated debt. This debt was transferred to the Company at the date of acquisition. In 2015, the Company purchased \$4.1 million of the outstanding preferred securities, reducing the outstanding preferred securities to \$1.6 million.

In November 2018, the County Bancshares Trust I, or County Trust, agreed to redeem all of the County Trust's issued and outstanding trust preferred securities upon concurrent redemption made by the Company of its junior subordinated debt securities held by the County Trust on January 7, 2019. The Company paid \$5.7 million to pay its obligation for the junior subordinated debt, including accrued and unpaid interest. The Company received \$4.1 million from the redemption of the preferred securities.

NOTE 13: RELATED PARTY TRANSACTIONS

In the ordinary course of business, the Company, through the Bank, has and expects to continue to conduct routine banking business with related parties, including its executive officers and directors. Related parties also include shareholders and their affiliates who directly or indirectly have 5% or more beneficial ownership in the Company.

<u>Loans</u>—In the opinion of management, loans to related parties were on substantially the same terms, including interest rates and collateral, as those prevailing at the time of comparable transactions with other persons and did not involve more than a normal risk of collectability or present any other unfavorable features to the Company. The Company had approximately \$158.7 million and \$168.9 million in loans to related parties at December 31, 2019 and 2018, respectively. At December 31, 2019 and 2018, there were no loans made to related parties deemed nonaccrual, past due, restructured or classified as potential problem loans.

Activity in loans to related parties as of the periods shown below was as follows:

	Years Ended December 31,				
(Dollars in thousands)		2019	2018		
Beginning balance	\$	168,851	\$	205,768	
New loans		15,934		107,303	
Repayments		(26,058)		(144,220)	
Ending balance	\$	158,727	\$	168,851	

<u>Unfunded Commitments</u>—At December 31, 2019 and 2018, the Company had approximately \$48.7 million and \$55.7 million in unfunded loan commitments to related parties, respectively.

<u>Deposits</u>—The Company held related party deposits of approximately \$233.9 million and \$311.2 million at December 31, 2019 and 2018, respectively.

<u>Advertising</u>—The Company incurred advertising expenses of approximately \$97,000 and \$94,000 for the years ended December 31, 2019 and 2018, respectively, to a vendor that is solely owned by a director of the Company.

NOTE 14: FAIR VALUE DISCLOSURES

The Company uses fair value measurements to record fair value adjustments to certain assets and to determine fair value disclosures. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction occurring in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. In estimating fair value, the Company uses valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. Such valuation techniques are consistently applied.

Inputs to valuation techniques refer to the assumptions used in pricing the asset or liability. Valuation inputs are categorized in a three-level hierarchy that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

<u>Level 1 Inputs</u>—Unadjusted quoted prices in active markets for identical assets and liabilities that the reporting entity has the ability to access at the measurement date.

<u>Level 2 Inputs</u>—Other observable inputs that may 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 or other inputs that are observable for the asset or liability such as interest rates, volatilities, prepayment speeds, loss severities, credit risks and default rates or inputs that are observable or can be corroborated by observable market data.

<u>Level 3 Inputs</u>—Unobservable inputs that reflect an entity's own assumptions that market participants would use in pricing the assets or liabilities.

During the years ended December 31, 2019 and 2018, there were no transfers of assets or liabilities within the levels of the fair value hierarchy.

In general, fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon models that primarily use observable market-based parameters as inputs. Valuation adjustments may be made to ensure that assets and liabilities are recorded at fair value. These adjustments may include amounts to reflect counterparty credit quality and creditworthiness, among other things, as well as unobservable parameters. Any such valuation adjustments are applied consistently over time.

The Company's valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While management believes the Company's valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value could result in different estimates of fair value. Fair value estimates are based on judgments regarding current economic conditions, risk characteristics of the various instruments and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision.

Financial Instruments Measured at Fair Value on a Recurring Basis

The Company's assets and liabilities measured at fair value on a recurring basis include the following:

<u>Debt Securities Available for Sale</u>—Debt securities classified as available for sale are recorded at fair value. For those debt securities classified as Level 2, the Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, market consensus prepayments speeds, credit information and the security's terms and conditions, among other things. The Company reviews the prices supplied by the independent pricing service, as well as their underlying pricing methodologies for reasonableness.

Equity Securities Available for Sale—Equity securities are classified as available for sale and are recorded at fair value. The fair value measurements are based on observable data obtained from a third-party pricing service. The Company reviews the prices supplied by the services against publicly available information. The equity securities are mutual funds publicly traded on the Nasdaq and the fair value is determined by using unadjusted quoted market prices which are considered Level 1 inputs.

<u>Interest Rate Swaps</u>—The Company obtains fair value measurements for its interest rate swaps from an independent pricing service which uses the income approach. The income approach calls for the utilization of valuation techniques to convert future cash flows as due to be exchanged per the terms of the financial instrument, into a single present value amount. Measurement is based on the value indicated by the market expectations about those future amounts as of the measurement date. The proprietary curves of the independent pricing service utilize pricing models derived from industry standard analytic tools, considering both Level 1 and Level 2 inputs.

Financial assets and financial liabilities measured at fair value on a recurring basis as of the dates shown below were as follows:

	December 31,						
(Dollars in thousands)		2019		2018			
Fair value of financial assets:							
Level 1 inputs: securities available for sale - equity securities	\$	1,147	\$	1,088			
Level 2 inputs:							
Debt securities available for sale							
State and municipal securities		53,279		57,691			
U.S. Agency Securities:							
Debt securities		_		16,881			
Collateralized mortgage obligations		55,989		65,414			
Mortgage-backed securities		120,847		88,859			
Interest rate swaps		2,638		962			
Total fair value of financial assets	\$	233,900	\$	230,895			
Fair value of financial liabilities:	-		-				
Level 2 inputs: interest rate swaps	\$	2,638	\$	962			
Total fair value of financial liabilities	\$	2,638	\$	962			

Financial Instruments Measured at Fair Value on a Non-recurring Basis

A portion of financial instruments are measured at fair value on a non-recurring basis and are subject to fair value adjustments in certain circumstances. Financial assets measured at fair value on a non-recurring basis during the dates shown below include certain impaired loans reported at the fair value of the underlying collateral if repayment is expected solely from the collateral or a discounted cash flow method if not. Prior to foreclosure, estimated fair values for collateral is estimated based on Level 3 inputs based on customized discounting criteria. The Company's financial assets measured at fair value on a non-recurring basis are certain impaired loans and as of the dates shown below were as follows:

	December 31,											
		2019					2018					
(Dollars in thousands)	In	ecorded vestment with llowance		lelated lowance		Net	In	ecorded vestment with llowance		elated owance		Net
Level 3 inputs						1,00						
Impaired loans:												
Commercial and industrial	\$	699	\$	416	\$	283	\$	635	\$	525	\$	110
Commercial real estate		_				_		596		44		552
1-4 family residential		1,485		15		1,470		1,824		89		1,735
Consumer						_		_				
Other		1,242		6		1,236		1,241		100		1,141
Total impaired loans	\$	3,426	\$	437	\$	2,989	\$	4,296	\$	758	\$	3,538

Non-Financial Assets and Non-Financial Liabilities Measured at Fair Value on a Non-recurring Basis

The Company's non-financial assets measured at fair value on a non-recurring basis for the periods reported are foreclosed assets (upon initial recognition or subsequent impairment). The Company's other non-financial assets whose fair value may be measured on a non-recurring basis when there is evidence of impairment and may be subject to impairment adjustments include goodwill and intangible assets, among other assets.

The fair value of foreclosed assets may be estimated using level 2 inputs based on observable market data or Level 3 inputs based on customized discounting criteria less estimated selling costs. There were no write-downs of foreclosed assets for fair value remeasurement subsequent to initial foreclosure during the years ended December 31, 2019 and 2018. There were no outstanding foreclosed assets as of December 31, 2019.

The fair value of repossessed real estate and other foreclosed assets is estimated using Level 2 inputs and, as of the dates shown below, were as follows:

	December 31,						
(Dollars in thousands)		2019	2	2018			
Foreclosed assets remeasured at initial recognition:							
Carrying value of foreclosed assets prior to measurement	\$	_	\$	13			
Charge-offs recognized in the allowance for loan losses				(1)			
Fair value	\$		\$	12			

Financial Instruments Reported at Amortized Cost

Fair market values and carrying amounts of financial instruments that are reported at cost as of the dates shown below were as follows:

	December 31,							
		20	019			20	018	
	F . W .		Carrying				Carrying	
(Dollars in thousands)		Fair Value		Amount		Fair Value		Amount
Financial assets:								
Level 1 inputs:								
Cash and due from banks	\$	372,064	\$	372,064	\$	382,070	\$	382,070
Level 2 inputs:								
Debt securities held to maturity		_				32		31
Bank-owned life insurance		71,881		71,881		71,525		71,525
Accrued interest receivable		8,742		8,742		8,227		8,227
Servicing asset		189		189		166		166
Level 3 inputs:								
Loans, including held for sale, net		2,654,362		2,615,268		2,432,753		2,423,130
Other investments		16,710		16,710		13,026		13,026
Total financial assets	\$	3,123,948	\$	3,084,854	\$	2,907,799	\$	2,898,175
Financial liabilities:								
Level 1 inputs:								
Noninterest-bearing deposits	\$	1,184,861	\$	1,184,861	\$	1,183,058	\$	1,183,058
Level 2 inputs:								
Interest-bearing deposits		1,651,359		1,667,527		1,522,366		1,583,224
Federal Home Loan Bank advances		48,822		50,000		_		_
Repurchase agreements		485		485		2,498		2,498
Junior subordinated debt						1,571		1,571
Accrued interest payable		1,005		1,005		653		653
Total financial liabilities	\$	2,886,532	\$	2,903,878	\$	2,710,146	\$	2,771,004
	<u> </u>		_		_		_	

The estimated fair value amounts of financial instruments have been determined by the Company using available market information and appropriate valuation methodologies. However, considerable judgment is required to interpret data to develop the estimates of fair value and as such the fair values shown above are not necessarily indicative of the amounts the Company will realize. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

NOTE 15: DERIVATIVE FINANCIAL INSTRUMENTS

The Company has outstanding interest rate swap contracts in which the Bank entered into an interest rate swap with a customer and entered into an offsetting interest rate swap with another financial institution at the same time. These interest rate swap contracts are not designated as hedging instruments for mitigating interest rate risk of the Bank. The objective of the transactions is to allow the Bank's customers to effectively convert a variable rate loan to a fixed rate.

In connection with each swap transaction, the Bank agrees to pay interest to the customer on a notional amount at a variable interest rate and receive interest from the customer on a similar notional amount at a fixed interest rate. At the same time, the Bank agrees to pay a third-party financial institution the same fixed interest rate on the same notional amount and receive the same variable interest rate on the same notional amount. Because the Bank acts as an intermediary for its customer, changes in the fair value of the underlying derivative contracts are designed to offset each other and would not significantly impact the Company's operating results except in certain situations where there is a significant deterioration in the customer's credit worthiness or that of the counterparties. At December 31, 2019 and 2018, no such deterioration was determined by management.

At December 31, 2019 and 2018, the Company had 19 and 13 interest rate swap agreements outstanding with borrowers and financial institutions, respectively. These derivative instruments are not designated as accounting hedges and changes in the net fair value are recognized in noninterest income or expense. Fair value amounts are included in other assets and other liabilities. Interest rates on the Company's swap agreements are based on the London Interbank Offered Rate of the U.S. Dollar deposits in Europe, or LIBOR. Derivative instruments outstanding as of the dates shown below were as follows:

(Dollars in thousands) December 31, 2019	Classification	Notional Amounts	Fair Value	Fixed Rate	Floating Rate	Weighted Average Maturity (Years)
Interest rate swaps with customers	Other Assets	\$ 69,189	\$ 2,599	4.40% - 5.89%	LIBOR 1M + 2.50% - 3.00%	6.65
Interest rate swaps with financial institution	Other Assets	5,987	39	4.00%	LIBOR 1M + 2.50%	6.71
Interest rate swaps with customers	Other Liabilities	5,987	(39)	4.00%	LIBOR 1M + 2.50%	6.71
Interest rate swaps with financial institution	Other Liabilities	69,189 \$ 150,352	(2,599)	4.40% - 5.89%	LIBOR 1M + 2.50% - 3.00%	6.65

(Dollars in thousands)	Classification	Notional Amounts		Fair Value	Fixed Rate	Floating Rate	Average Maturity (Years)	
December 31, 2018								
Interest rate swaps with customers	Other Assets	\$ 8,901	\$	169	5.45% -	LIBOR 1M +	6.22	
					7.25%	2.50% - 3.20%		
Interest rate swaps with financial	Other Assets	32,923		793	4.00% -	LIBOR 1M +	7.78	
institution					5.37%	2.50% - 3.25%		
Interest rate swaps with customers	Other	32,923		(793)	4.00% -	LIBOR 1M +	7.78	
•	Liabilities			, ,	5.37%	2.50% - 3.25%		
Interest rate swaps with financial	Other	8,901		(169)	5.45% -	LIBOR 1M+	6.22	
institution	Liabilities	,		, ,	7.25%	2.50% - 3.20%		
Total derivatives		\$ 83,648	\$					

NOTE 16: OPERATING LEASES

The Company leases certain office space, stand-alone buildings and land are recognized as operating lease right-of-use assets and operating lease liabilities in the consolidated balance sheets. Lease liabilities represent the Company's liability to make lease payments under these leases, on a discounted basis and at December 31, 2019, totaled \$15.7 million. The weighted-average discount rate for the year ended December 31, 2019 was 3.54%. The discount rate is estimated based on Federal Home Loan Bank advance rates applicable to the remaining terms.

Right-of-use assets represent the Company's right to use, or control the use of, leased assets for their lease term and at December 31, 2019, totaled \$12.9 million. During the year ended December 31, 2019, the Company obtained \$1.3 million of right-of-use assets in exchange for new operating lease liabilities related to two leases commenced in that period.

The weighted-average remaining lease term for operating leases outstanding at December 31, 2019 was 11.2 years. Cash paid for amounts included in the measurement of operating lease liabilities for the year ended December 31, 2019 totaled \$1.9 million. The Company's leases have no variable costs.

Lease costs for the period shown below were as follows:

(Dollars in thousands)	 ar Ended iber 31, 2019
Operating lease cost	\$ 1,876
Short-term lease cost	61
Sublease income	 (153)
Total lease cost	\$ 1,784

A maturity analysis of operating lease liabilities as of the date shown below was as follows:

(Dollars in thousands)	Dece	mber 31, 2019
2020	\$	2,025
2021		2,362
2022		2,474
2023		2,478
2024		1,916
Thereafter		10,231
Total undiscounted lease liability		21,486
Less:		
Discount on cash flows		(3,741)
Lease signed, but not yet commenced		(2,041)
Total operating lease liability	\$	15,704

NOTE 17: COMMITMENTS AND CONTINGENCIES AND FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK

Financial Instruments with Off-Balance-Sheet Risk

Weighted

In the normal course of business, the Company enters into various transactions, which in accordance with GAAP, are not included in its consolidated balance sheets. The Company enters into these transactions to meet the financing needs of its customers. These financial instruments include commitments to extend credit for loans in process and standby letters of credit. The Company uses the same credit policies in making these commitments and conditional obligations as it does for on-balance-sheet instruments.

Commitments to extend credit and standby letters of credit as of the dates shown below were as follows:

	December 31,			
(Dollars in thousands)		2019		2018
Commitments to extend credit, variable interest rate	\$	652,611	\$	726,277
Commitments to extend credit, fixed interest rate		141,439		105,359
	\$	794,050	\$	831,636
Standby letters of credit	\$	23,547	\$	31,729

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being fully drawn upon, the total commitment amounts disclosed above do not necessarily represent future cash requirements.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third-party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to the Company's customers.

Litigation

The Company is subject to claims and lawsuits which arise primarily in the ordinary course of business. Based on information presently available and advice received from legal counsel representing the Company, it is the opinion of management that the disposition or ultimate determination of such claims and lawsuits will not have a material adverse effect on the financial position or results of operations of the Company.

NOTE 18: EMPLOYEE BENEFIT PLANS AND DEFERRED COMPENSATION ARRANGEMENTS

Employee Benefit Plans

The Company maintains a 401(k) employee benefit plan and substantially all employees that complete three months of service may participate. The Company matches a portion of each employee's contribution and may, at its discretion, make additional contributions. During the years ended December 31, 2019 and 2018, the Company contributed \$1.9 million and \$1.7 million to the plan, respectively.

Executive Deferred Compensation Arrangements

The Company established an executive incentive compensation arrangement with several officers of the Bank, in which these officers are eligible for performance-based incentive bonus compensation. As part of this compensation arrangement, the Company contributes one-fourth of the incentive bonus amount into a deferred compensation account. The deferred amounts accrue at a market rate of interest and are payable to the employees upon separation from the Bank provided vesting arrangements have been met. At December 31, 2019 and 2018, the amount payable, including interest, for this deferred plan was \$2.7 million and \$2.5 million, respectively, and is included in other liabilities in the consolidated balance sheets.

Salary Continuation Agreements

The Company entered into a salary continuation arrangement in 2008 with the Company's then President and CEO that calls for payments of \$100,000 per year for a period of 10 years commencing at age 65. Payments under the plan began during 2014. The Company's liability was \$335,000 and \$421,000 at December 31, 2019 and 2018, respectively, which is included in other liabilities in the consolidated balance sheets and equals the present value of the benefits expected to be provided.

In October 2017, the Company entered into a salary continuation arrangement with the Company's President and CEO that calls for payments of \$200,000 per year payable for a period of 10 years commencing at age 70. Payments under the plan will begin in 2024. The Company's liability was \$437,000 and \$219,000 at December 31, 2019 and 2018, respectively, and is included in other liabilities in the consolidated balance sheets. The liability will continue to accrue

over the remaining period until payments commence such that the accrued amount at the eligibility date will equal the present value of all the future benefits expected to be paid.

NOTE 19: STOCK-BASED COMPENSATION

The Company acquired a stock option plan which originated under VB Texas, Inc. as a part of a merger of the two companies. The options granted to employees must be exercised within 10 years from the date of grant and vesting schedules are determined on an individual basis. At the merger date, all outstanding options became fully vested and were converted to options of the Company's common stock at an exchange ratio equal to the acquisition exchange rate for common shares. No options were granted under this plan after October 24, 2016.

In May 2014, the Company adopted the 2014 Stock Option Plan, or the 2014 Plan. The 2014 Plan was approved by the Company's shareholders and limits the number of shares that may be optioned to 1,127,200. The 2014 Plan provides that no options may be granted after May 20, 2024. Options granted under the 2014 Plan expire 10 years from the date of grant and become exercisable in installments over a period of one to five years, beginning on the first anniversary of the date of grant. At December 31, 2019, 963,200 shares were available for future grant under the 2014 Plan.

In September 2017, the Company adopted the 2017 Omnibus Incentive Plan, or the 2017 Plan. The 2017 Plan authorizes the Company to grant options and performance-based and non-performance based restricted stock awards as well as various other types of stock-based and other awards that are not stock-based to eligible employees, consultants and non-employee directors up to an aggregate of 600,000 shares of common stock. At December 31, 2019, 314,913 shares were available for future grant under the 2017 Plan.

Stock option activity for the periods shown below was as follows:

	Years Ended December 31,							
	2	2019		2	2018			
	Number of Shares Underlying Options		Weighted Average Exercise Price	Number of Shares Underlying Options	Weighted Average Exercise Price			
Outstanding at beginning of period	232,322	\$	16.66	260,322	\$	16.00		
Granted	_		_	_				
Exercised	(15,244)		12.74	(28,000)		10.52		
Forfeited/expired	(4,000)		17.73	_				
Outstanding at end of period	213,078		16.92	232,322		16.66		

A summary of stock options as of the date shown below was as follows:

	December 31, 2019							
Stock Options		Exercisable		Unvested		Outstanding		
Number of shares underlying options		148,879		64,199		213,078		
Weighted-average exercise price per share	\$	15.62	\$	19.94	\$	16.92		
Aggregate intrinsic value (in thousands)	\$	2,307	\$	718	\$	3,025		
Weighted-average remaining contractual term (years)		4.9		6.9		5.5		

The fair value of the Company's restricted stock awards is estimated based on the market value of the Company's common stock at the date of grant. Restricted stock shares are considered fully issued at the time of the grant and the grantee becomes the record owner of the restricted stock and has voting, dividend and other shareholder rights. The shares of restricted stock are non-transferable and subject to forfeiture until the restricted stock vests and any dividends with respect to the restricted stock are subject to the same restrictions, including the risk of forfeiture.

Non-performance based restricted stock grants vest over the service period in equal increments over a period of two to five years, beginning on the first anniversary of the date of grant.

The number of shares earned under the Company's performance-based restricted stock award agreements is based on the achievement of certain branch production goals. Compensation expense for performance-based restricted stock is recognized for the probable award level over the period estimated to achieve the performance conditions and other goals,

on a straight-line basis. If the probable award level and/or the period estimated to be achieved change, compensation expense will be adjusted via a cumulative catch-up adjustment to reflect these changes. The performance conditions goals must be achieved within five years or the awards expire. The number of performance-based shares granted presented in the table below is based upon the attainment of the maximum number of shares possible to be earned.

Restricted stock activity for the periods shown below was as follows:

	Non-perform	Based	Performance-based			
		V	Veighted		W	eighted eighted
		A	Average		A	verage
	Number of		rant Date	Number of	Grant Date Fair Value	
	Shares	Fa	air Value	Shares		
Outstanding at December 31, 2017	212,580	\$	26.71	_	\$	
Granted	21,500		30.44	24,000		_
Vested	(51,307)		27.04	_		_
Forfeited	(1,000)		28.64			_
Outstanding at December 31, 2018	181,773	\$	27.05	24,000	\$	34.46
Granted	44,492		31.64	_		_
Vested	(61,590)		27.20	(6,000)		34.46
Forfeited	(3,232)		29.99			_
Outstanding at December 31, 2019	161,443	\$	28.20	18,000	\$	34.46

A summary of restricted stock as of the date shown below was as follows:

	December 31, 2019						
Restricted Stock	Non-p	erformance Based	Pe	rformance-based			
Number of shares underlying restricted stock		161,443		18,000			
Weighted-average grant date fair value per share	\$	28.20	\$	34.46			
Aggregate fair value (in thousands)	\$	5,024	\$	560			
Weighted-average remaining vesting period (years)		2.9		2.8			

The Company's stock compensation plans allow employees to elect to have shares withheld to satisfy their tax liabilities related to options exercised or restricted stock vested or to pay the exercise price of the options. During the periods shown below, the shares of stock options exercised, restricted stock vested, shares withheld, and shares issued were as follows:

	Exercised/Vested	Shares Withheld	Shares Issued
Year Ended December 31, 2019			_
Stock options	15,244	(2,318)	12,926
Non-performance based restricted stock	61,590	(6,672)	54,918
Performance-based restricted stock	6,000	(1,463)	4,537
Year Ended December 31, 2018			
Stock options	28,000	_	28,000
Non-performance based restricted stock	51,307	(5,118)	46,189
Performance-based restricted stock	_	· —	_

For the years ended December 31, 2019, 2018 and 2017, stock compensation expense was \$2.4 million, \$1.6 million and \$329,000, respectively. As of December 31, 2019, there was approximately \$4.8 million of total unrecognized compensation expense related to unvested stock options, non-performance based restricted stock and performance-based restricted, which is expected to be recognized in the Company's consolidated statements of income over a weighted-average period of 2.8 years.

NOTE 20: REGULATORY MATTERS

Banks and bank holding companies are subject to various regulatory capital requirements administered by state and federal banking agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators about components, risk weighting and other factors.

The Company and the Bank's Common Equity Tier 1 capital includes common stock and related capital surplus, net of treasury stock, and retained earnings. In connection with the adoption of the Basel III Capital Rules, the Company and the Bank elected to opt-out of the requirement to include most components of accumulated other comprehensive income in Common Equity Tier 1. Common Equity Tier 1 for both the Company and the Bank is reduced by goodwill and other intangible assets, net of associated deferred tax liabilities, and subject to transition provisions.

The Basel III Capital Rules require the Company and the Bank to maintain (i) a minimum ratio of Common Equity Tier 1 capital to risk-weighted assets of at least 4.5%, plus a 2.5% "capital conservation buffer" (which is added to the 4.5% Common Equity Tier 1 capital ratio as that buffer is phased in, effectively resulting in a minimum ratio of Common Equity Tier 1 capital to risk-weighted assets of at least 7.0% upon full implementation), (ii) a minimum ratio of Tier 1 capital to risk-weighted assets of at least 6.0%, plus the capital conservation buffer (which is added to the 6.0% Tier 1 capital ratio as that buffer is phased in, effectively resulting in a minimum Tier 1 capital ratio of 8.5% upon full implementation), (iii) a minimum ratio of Total capital (that is, Tier 1 plus Tier 2) to risk-weighted assets of at least 8.0%, plus the capital conservation buffer (which is added to the 8.0% total capital ratio as that buffer is phased in, effectively resulting in a minimum total capital ratio of 10.5% upon full implementation) and (iv) a minimum leverage ratio of 4.0%, calculated as the ratio of Tier 1 capital to average quarterly assets.

The implementation of the capital conservation buffer began on January 1, 2016 at the 0.625% level and was phased in over a four-year period (increasing by that amount on each subsequent January 1, until it reached 2.5% on January 1, 2019). The Basel III Capital Rules also provide for a "countercyclical capital buffer" that is applicable to only certain covered institutions and does not have any current applicability to the Company and the Bank. The capital conservation buffer is designed to absorb losses during periods of economic stress and, as detailed above, effectively increases the minimum required risk-weighted capital ratios. Banking institutions with a ratio of Common Equity Tier 1 capital to risk-weighted assets below the effective minimum (4.5% plus the capital conservation buffer and, if applicable, the countercyclical capital buffer) will face constraints on dividends, equity repurchases, and compensation based on the amount of the shortfall.

The Company and the Bank are subject to the regulatory capital requirements administered by the Federal Reserve and, for the Bank, the OCC. Regulatory authorities can initiate certain mandatory actions if the Company or the Bank fail to meet the minimum capital requirements, which could have a direct material effect on the Company's financial statements. Management believes, that as of December 31, 2019 and 2018, the Company and the Bank met all capital adequacy requirements to which they were subject.

Dividend Restrictions

In the ordinary course of business, the Company may be dependent upon dividends from the Bank to provide funds for the payment of dividends to shareholders and to provide for other cash requirements. Banking regulations may limit the amount of dividends that may be paid. Approval by regulatory authorities is required if the effect of dividends declared would cause the regulatory capital of the Bank to fall below specified minimum levels. Approval is also required if dividends declared exceed the net profits for that year combined with the retained net profits for the preceding two years.

At December 31, 2019 and 2018, the Company and the Bank, were "well capitalized" based on the ratios presented below. Actual and required capital ratios as the dates shown below for the Company and the Bank were as follows for the dates presented:

	Actu	al	Minim Capital Re for Capital A Purpo	quired dequacy	Minin Capital R Basel Fully Pha	equired III	Requireo Considero Capita	ed Well
(Dollars in thousands)	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio
December 31, 2019			`					
Common Equity Tier I to Risk-Weighted Assets:								
Consolidated	\$ 448,445	15.52%	\$ 129,997	4.50%	\$ 202,218	7.00%	N/A	N/A
Bank Only	\$ 406,675	14.08%	\$ 129,988	4.50%	\$ 202,203	7.00%	\$ 187,760	6.50%
Tier I Capital to Risk- Weighted Assets:								
Consolidated	\$ 448,445	15.52%	\$ 173,330	6.00%	\$ 245,550	8.50%	N/A	N/A
Bank Only	\$ 406,675	14.08%	\$ 173,317	6.00%	\$ 245,532	8.50%	\$ 231,089	8.00%
Total Capital to Risk- Weighted Assets:								
Consolidated	\$ 474,104	16.41%	\$ 231,106	8.00%	\$ 303,327	10.50%	N/A	N/A
Bank Only	\$ 432,334	14.97%	\$ 231,089	8.00%	\$ 303,304	10.50%	\$ 288,861	10.00%
Tier 1 Leverage Capital to Average Assets:								
Consolidated	\$ 448,445	13.11%	\$ 136,798	4.00%	\$ 136,798	4.00%	N/A	N/A
Bank Only	\$ 406,675	11.90%	\$ 136,754	4.00%	\$ 136,754	4.00%	\$ 170,943	5.00%
December 31, 2018 Common Equity Tier I to								
Risk-Weighted Assets:								
Consolidated		14.71%	\$ 123,885		\$ 192,710	7.00%	N/A	N/A
Bank Only	\$ 363,140	13.19%	\$ 123,877	4.50%	\$ 192,697	7.00%	\$ 178,933	6.50%
Tier I Capital to Risk- Weighted Assets:								
Consolidated	\$ 406,257	14.76%	\$ 165,180	6.00%	\$ 234,005	8.50%	N/A	N/A
Bank Only	\$ 363,140	13.19%	\$ 165,169	6.00%	\$ 233,989	8.50%	\$ 220,225	8.00%
Total Capital to Risk- Weighted Assets:								
Consolidated	\$ 430,238	15.63%	\$ 220,240	8.00%	\$ 289,065	10.50%	N/A	N/A
Bank Only Tier 1 Leverage Capital	\$ 387,211	14.07%	\$ 220,225	8.00%	\$ 289,046	10.50%	\$ 275,282	10.00%
to Average Assets:	¢ 406 257	12 740/	¢ 127.250	4.000/	¢ 127.250	4.000/	T .T / A	NT/A
Consolidated	\$ 406,257 \$ 363,140	12.74% 11.41%	\$ 127,350 \$ 127,350	4.00% 4.00%	\$ 127,350 \$ 127,350	4.00% 4.00%	N/A \$ 159,188	N/A 5.00%
Bank Only	\$ 505,140	11.4170	\$ 147,330	T.0070	\$ 127,330	4.0070	φ 1 <i>39</i> ,100	5.0070

NOTE 21: INCOME TAXES

The components of the provision for income tax expense for the periods listed below were as follows:

	For the Years Ended December 31,								
(Dollars in thousands)		2019		2018		2017			
Current federal income tax	\$	12,988	\$	11,908	\$	13,364			
Current state income tax		240		190		157			
Deferred income tax		(1,657)		(734)		2,932			
Total income tax expense	\$	11,571	\$	11,364	\$	16,453			

Income tax expense for the periods listed below differs from the applicable statutory rate of 21% for the years ended December 31, 2019 and 2018 and 35% for the year ended December 31, 2017 as follows:

	For th	e Years	Ended Decen	ıber 31	ι,
(Dollars in thousands)	2019		2018	2017	
Tax expense calculated at statutory rate	\$ 13,038	\$	12,317	\$	15,408
Increase (decrease) resulting from:					
State income tax	190		150		102
Tax exempt interest income	(807)		(834)		(1,504)
Life insurance	(1,047)		(381)		(553)
Impact of tax law rate change	_		_		3,857
Other	 197		112		(857)
Total income tax expense	\$ 11,571	\$	11,364	\$	16,453
Effective tax rate	18.64%		19.37%		37.37%

The Tax Cuts and Jobs Act of 2017 became effective January 1, 2018 and lowered the corporate federal income tax rate in the U.S. from 35% to 21%. Based upon this tax law enactment, the Company analyzed and remeasured its deferred tax positions to the new tax rate and recorded a \$3.9 million adjustment to income tax expense in the consolidated income statement for the year ended December 31, 2017.

Deferred income taxes are provided for differences between the financial statement carrying amount of existing assets and liabilities and their respective tax basis. The components of the net deferred tax asset for the periods shown below were as follows:

	 Decem	ber 31,	
(Dollars in thousands)	 2019		2018
Deferred tax assets:			
Allowance for possible credit losses	\$ 5,308	\$	4,976
Compensation related	3,068		2,681
Deferred loan origination fees and loan costs	1,261		1,312
Loan related	253		137
Unrealized loss on securities available for sale	_		790
Operating lease liabilities	3,298		
Other	 8		230
Total deferred tax assets	 13,196		10,126
Deferred tax liabilities:			
Accumulated depreciation	(1,140)		(1,203)
Operating lease right-to-use asset	(2,714)		_
Compensation 481(a) adjustment	(238)		(476)
Core deposit intangibles	(997)		(1,178)
Unrealized loss on securities available for sale	(634)		_
Other	 (41)		(68)
Total deferred tax liabilities	 (5,764)		(2,925)
Net Deferred Tax Asset	\$ 7,432	\$	7,201

As of December 31, 2019, the tax years that remain subject to examination by the major tax jurisdictions under the statute of limitations are from the year 2015 forward for the State of Texas and from the year 2016 forward for federal. When necessary, the Company would include interest expense assessed by taxing authorities in interest expense and penalties related to income taxes in other expense on its consolidated statements of income. The Company did not record any interest or penalties related to income tax for the years ended December 31, 2019, 2018 and 2017. For the years ended December 31, 2019 and 2018, management has determined there were no material uncertain tax positions.

NOTE 22: EARNINGS PER SHARE

The computation of basic and diluted earnings per share for the periods shown is below.

		Ye	ars En	ded December	r 31 ,	
(Dollars in thousands, except per share data)		2019		2018		2017
Net income for common shareholders	\$	50,517	\$	47,289	\$	27,571
Weighted-average shares (thousands)	•					
Basic weighted-average shares outstanding		24,926		24,859		22,457
Dilutive effect of outstanding stock options and unvested						
restricted stock awards		127		159		116
Diluted weighted-average shares outstanding		25,053		25,018		22,573
Earnings per share:	•					
Basic	\$	2.03	\$	1.90	\$	1.23
Diluted	\$	2.02	\$	1.89	\$	1.22

For the years ended December 31, 2019 and 2018, the Company has excluded from diluted weighted-average shares, the impact of 2,400 and 3,000 shares of unvested non-performance based restricted stock as they are anti-dilutive and 18,000 and 24,000 shares of performance-based restricted stock, respectively, as they are contingently issuable and the performance conditions for these issuances have not been met.

NOTE 23: PARENT COMPANY

The following balance sheets, statements of income and statements of cash flows for CBTX, Inc. should be read in conjunction with the consolidated financial statements and the related notes.

Balance Sheets	Decen	ıber 31,	
(Dollars in thousands)	2019		2018
Assets			
Cash and due from banks	\$ 44,130	\$	44,189
Investment in subsidiary	493,951		445,754
Deferred tax asset, net	131		145
Other assets	438		911
Total assets	\$ 538,650	\$	490,999
Liabilities and shareholders' equity	 		
Liabilities			
Junior subordinated debt	\$ _	\$	1,571
Other liabilities	2,929		1,803
Total liabilities	2,929		3,374
Shareholders' equity			
Common stock	258		258
Additional paid-in capital	346,559		344,497
Retained earnings	201,080		160,626
Treasury stock	(14,562)		(14,781)
Accumulated other comprehensive loss	2,386		(2,975)
Total shareholders' equity	535,721		487,625
Total liabilities and shareholders' equity	\$ 538,650	\$	490,999

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Statements of Income			S EII	ded Decembe	er 31.	,
(Dollars in thousands)		2019		2018		2017
Interest income	Ф	_	Ф	107	Φ	1.40
Other	\$	5	\$	187	\$	142
Interest expense		1.5		1.5		007
Note payable		15		15		906
Junior subordinated debt		4		420		322
Total interest expense		19		435		1,228
Net interest expense		(14)		(248)		(1,086)
Noninterest income						
Dividend income from subsidiary		8,901		7,800		8,806
Total noninterest income		8,901		7,800		8,806
Noninterest expense						
Salaries and employee benefits		673		755		344
Data processing		13		44		37
Printing, stationery and office		8		12		20
Professional and director fees		652		728		842
Other expenses		201		196		17
Total noninterest expense		1,547		1,735	_	1,260
Income before income tax benefit and equity in undistributed income of		1,0		1,700	_	1,200
subsidiary		7,340		5,817		6,460
Income tax benefit		(341)		(437)		(1,518)
Income before equity in undistributed income of subsidiary		7,681		6,254	_	7,978
Equity in undistributed income of subsidiary		42,836		41,035		19,593
Net income	\$	50,517	\$	47,289	\$	27,571
Statements of Cash Flows		Year	rs En	ded Decembe	er 31,	,
(Dollars in thousands)		2019		2018	_	2017
Cash flows from operating activities:						
Net income	\$	50,517	\$	47,289	\$	27,571
Adjustments to reconcile consolidated net income to net cash provided						
by operating activities:						
by operating activities: Equity in undistributed net income loss of subsidiary		(42 836)		(41 035)		(19 593)
Equity in undistributed net income loss of subsidiary		(42,836)		(41,035)		(19,593)
Equity in undistributed net income loss of subsidiary Stock-based compensation expense		2,402		1,601		329
Equity in undistributed net income loss of subsidiary Stock-based compensation expense Deferred tax provision (benefit)						329
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense. Deferred tax provision (benefit)		2,402 14		1,601 (4)		329 391
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets		2,402 14 473		1,601 (4) 1,549		329 391 (1,216)
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities.		2,402 14 473 (180)		1,601 (4) 1,549 (836)		329 391 (1,216 552
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities. Total adjustments		2,402 14 473 (180) (40,127)		1,601 (4) 1,549 (836) (38,725)		329 391 (1,216) 552 (19,537
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities. Total adjustments Net cash provided by operating activities.		2,402 14 473 (180)	<u></u>	1,601 (4) 1,549 (836)		329 391 (1,216 552
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities. Total adjustments Net cash provided by operating activities. Cash flows from investing activities:		2,402 14 473 (180) (40,127)		1,601 (4) 1,549 (836) (38,725)		329 391 (1,216) 552 (19,537
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities. Total adjustments Net cash provided by operating activities. Cash flows from investing activities: Cash flows from financing activities:		2,402 14 473 (180) (40,127)		1,601 (4) 1,549 (836) (38,725)		329 391 (1,216 552 (19,537 8,034
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities. Total adjustments Net cash provided by operating activities. Cash flows from investing activities: Repayment of note payable		2,402 14 473 (180) (40,127) 10,390 —		1,601 (4) 1,549 (836) (38,725) 8,564		329 391 (1,216 552 (19,537 8,034
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities. Total adjustments Net cash provided by operating activities. Cash flows from investing activities: Cash flows from financing activities:		2,402 14 473 (180) (40,127)		1,601 (4) 1,549 (836) (38,725)		329 391 (1,216 552 (19,537 8,034
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities. Total adjustments Net cash provided by operating activities. Cash flows from investing activities: Repayment of note payable		2,402 14 473 (180) (40,127) 10,390 —		1,601 (4) 1,549 (836) (38,725) 8,564		329 391 (1,216 552 (19,537 8,034 ————————————————————————————————————
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities. Total adjustments Net cash provided by operating activities. Cash flows from investing activities: Repayment of note payable Redemption of trust preferred securities.		2,402 14 473 (180) (40,127) 10,390 —		1,601 (4) 1,549 (836) (38,725) 8,564		329 391 (1,216 552 (19,537 8,034 (27,679 64,519
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities. Total adjustments Net cash provided by operating activities. Cash flows from investing activities: Cash flows from financing activities: Repayment of note payable Redemption of trust preferred securities. Proceeds from sale of common stock in initial public offering Dividends paid on common stock		2,402 14 473 (180) (40,127) 10,390 — (1,571)		1,601 (4) 1,549 (836) (38,725) 8,564 — (5,155)		329 391 (1,216 552 (19,537 8,034 — (27,679 — 64,519
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities. Total adjustments Net cash provided by operating activities. Cash flows from investing activities: Cash flows from financing activities: Repayment of note payable Redemption of trust preferred securities. Proceeds from sale of common stock in initial public offering Dividends paid on common stock Payments to tax authorities for stock-based compensation.		2,402 14 473 (180) (40,127) 10,390 — (1,571) — (8,757)		1,601 (4) 1,549 (836) (38,725) 8,564 —— (5,155) —— (4,979)		329 391 (1,216 552 (19,537 8,034 ————————————————————————————————————
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities. Total adjustments Net cash provided by operating activities. Cash flows from investing activities: Cash flows from financing activities: Repayment of note payable Redemption of trust preferred securities. Proceeds from sale of common stock in initial public offering Dividends paid on common stock Payments to tax authorities for stock-based compensation Proceeds from exercise of stock options.		2,402 14 473 (180) (40,127) 10,390 — (1,571) — (8,757) (239) 121		1,601 (4) 1,549 (836) (38,725) 8,564 —— (5,155) —— (4,979) (171)		329 391 (1,216) 552 (19,537
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities. Total adjustments Net cash provided by operating activities. Cash flows from investing activities: Repayment of note payable Redemption of trust preferred securities. Proceeds from sale of common stock in initial public offering Dividends paid on common stock Payments to tax authorities for stock-based compensation Proceeds from exercise of stock options. Repurchase of common stock		2,402 14 473 (180) (40,127) 10,390 — (1,571) — (8,757) (239) 121 (3)		1,601 (4) 1,549 (836) (38,725) 8,564 —— (5,155) —— (4,979) (171) 294 ——		329 391 (1,216 552 (19,537 8,034 ————————————————————————————————————
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities. Total adjustments Net cash provided by operating activities. Cash flows from investing activities: Repayment of note payable Redemption of trust preferred securities. Proceeds from sale of common stock in initial public offering Dividends paid on common stock Payments to tax authorities for stock-based compensation Proceeds from exercise of stock options. Repurchase of common stock Net cash (used) provided in financing activities		2,402 14 473 (180) (40,127) 10,390 — (1,571) — (8,757) (239) 121 (3) (10,449)		1,601 (4) 1,549 (836) (38,725) 8,564 — (5,155) — (4,979) (171) 294 — (10,011)		329 391 (1,216 552 (19,537 8,034 ————————————————————————————————————
Equity in undistributed net income loss of subsidiary. Stock-based compensation expense Deferred tax provision (benefit) Change in operating assets and liabilities: Other assets Other liabilities. Total adjustments Net cash provided by operating activities. Cash flows from investing activities: Repayment of note payable Redemption of trust preferred securities. Proceeds from sale of common stock in initial public offering Dividends paid on common stock Payments to tax authorities for stock-based compensation Proceeds from exercise of stock options. Repurchase of common stock		2,402 14 473 (180) (40,127) 10,390 — (1,571) — (8,757) (239) 121 (3)		1,601 (4) 1,549 (836) (38,725) 8,564 —— (5,155) —— (4,979) (171) 294 ——		329 391 (1,216 552 (19,537 8,034 — (27,679 64,519 (4,412

109

44,189

45,636

NOTE 24: QUARTERLY FINANCIAL DATA (UNAUDITED)

Unaudited quarterly financial data for the periods indicated below was as follows:

			Y	ear Ended De	cemb	per 31, 2019		
(Dollars in thousands)	Fir	st Quarter	Sec	ond Quarter	Thi	rd Quarter	Four	th Quarter
Interest income	\$	36,985	\$	38,649	\$	39,193	\$	38,568
Interest expense		3,657		4,350		4,618		4,782
Net interest income		33,328		34,299		34,575		33,786
Provision (recapture) for loan losses		1,147		807		579		(148)
Net interest income after provision (recapture) for loan								
losses		32,181		33,492		33,996		33,934
Noninterest income		3,493		7,303		4,115		3,717
Noninterest expense		22,585		23,403		22,045		22,110
Income before income taxes		13,089		17,392		16,066		15,541
Income tax expense		2,599		3,077		2,990		2,905
Net income	\$	10,490	\$	14,315	\$	13,076	\$	12,636
Earnings per share:								
Basic	\$	0.42	\$	0.57	\$	0.52	\$	0.51
Diluted	\$	0.42	\$	0.57	\$	0.52	\$	0.50
					_			
(Dallars in thousands)	Fi	at Owantan		ear Ended De			Fann	uth Owanton
(Dollars in thousands)		st Quarter	Sec	ond Quarter	Thi	rd Quarter		<u>36 882</u>
Interest income	Fir \$	31,085		ond Quarter 33,127		rd Quarter 34,665	Four	36,882
Interest income		31,085 2,046	Sec	33,127 2,251	Thi	74,665 34,39		36,882 3,662
Interest income		31,085 2,046 29,039	Sec	33,127 2,251 30,876	Thi	34,665 3,139 31,526		36,882 3,662 33,220
Interest income Interest expense Net interest income Provision (recapture) for loan losses		31,085 2,046	Sec	33,127 2,251	Thi	74,665 34,39		36,882 3,662
Interest income Interest expense Net interest income Provision (recapture) for loan losses Net interest income after provision (recapture) for loan		31,085 2,046 29,039 865	Sec	33,127 2,251 30,876 690	Thi	rd Quarter 34,665 3,139 31,526 (1,142)		36,882 3,662 33,220 (2,169)
Interest income Interest expense Net interest income Provision (recapture) for loan losses Net interest income after provision (recapture) for loan losses		31,085 2,046 29,039 865 28,174	Sec	33,127 2,251 30,876 690 30,186	Thi	rd Quarter 34,665 3,139 31,526 (1,142) 32,668		36,882 3,662 33,220 (2,169) 35,389
Interest income Interest expense Net interest income Provision (recapture) for loan losses Net interest income after provision (recapture) for loan losses Noninterest income		31,085 2,046 29,039 865 28,174 3,361	Sec	33,127 2,251 30,876 690 30,186 3,506	Thi	34,665 3,139 31,526 (1,142) 32,668 3,526		36,882 3,662 33,220 (2,169) 35,389 3,859
Interest income Interest expense Net interest income Provision (recapture) for loan losses Net interest income after provision (recapture) for loan losses Noninterest income Noninterest expense		31,085 2,046 29,039 865 28,174 3,361 20,284	Sec	33,127 2,251 30,876 690 30,186 3,506 20,012	Thi	rd Quarter 34,665 3,139 31,526 (1,142) 32,668 3,526 19,964		36,882 3,662 33,220 (2,169) 35,389 3,859 21,756
Interest income Interest expense Net interest income Provision (recapture) for loan losses Net interest income after provision (recapture) for loan losses Noninterest income Noninterest expense Income before income taxes		31,085 2,046 29,039 865 28,174 3,361 20,284 11,251	Sec	33,127 2,251 30,876 690 30,186 3,506 20,012 13,680	Thi	34,665 3,139 31,526 (1,142) 32,668 3,526 19,964 16,230		36,882 3,662 33,220 (2,169) 35,389 3,859 21,756 17,492
Interest income Interest expense Net interest income Provision (recapture) for loan losses Net interest income after provision (recapture) for loan losses Noninterest income Noninterest expense Income before income taxes Income tax expense	\$	31,085 2,046 29,039 865 28,174 3,361 20,284 11,251 2,139	\$	33,127 2,251 30,876 690 30,186 3,506 20,012 13,680 2,638	<u>Thi</u> \$	34,665 3,139 31,526 (1,142) 32,668 3,526 19,964 16,230 3,207	\$	36,882 3,662 33,220 (2,169) 35,389 3,859 21,756 17,492 3,380
Interest income Interest expense Net interest income Provision (recapture) for loan losses Net interest income after provision (recapture) for loan losses Noninterest income Noninterest expense Income before income taxes Income tax expense Net income		31,085 2,046 29,039 865 28,174 3,361 20,284 11,251	Sec	33,127 2,251 30,876 690 30,186 3,506 20,012 13,680	Thi	34,665 3,139 31,526 (1,142) 32,668 3,526 19,964 16,230		36,882 3,662 33,220 (2,169) 35,389 3,859 21,756 17,492
Interest income Interest expense Net interest income Provision (recapture) for loan losses Net interest income after provision (recapture) for loan losses Noninterest income Noninterest expense Income before income taxes Income tax expense Net income Earnings per share:	\$	31,085 2,046 29,039 865 28,174 3,361 20,284 11,251 2,139 9,112	<u>Sect</u> \$	33,127 2,251 30,876 690 30,186 3,506 20,012 13,680 2,638 11,042	<u>Thi</u> \$	34,665 3,139 31,526 (1,142) 32,668 3,526 19,964 16,230 3,207 13,023	\$	36,882 3,662 33,220 (2,169) 35,389 3,859 21,756 17,492 3,380 14,112
Interest income Interest expense Net interest income Provision (recapture) for loan losses Net interest income after provision (recapture) for loan losses Noninterest income Noninterest expense Income before income taxes Income tax expense Net income	\$	31,085 2,046 29,039 865 28,174 3,361 20,284 11,251 2,139	\$	33,127 2,251 30,876 690 30,186 3,506 20,012 13,680 2,638	<u>Thi</u> \$	34,665 3,139 31,526 (1,142) 32,668 3,526 19,964 16,230 3,207	\$	36,882 3,662 33,220 (2,169) 35,389 3,859 21,756 17,492 3,380

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J. PAT PARSONS CBTX, Inc.

JOE PENLAND, SR. Quality Mat Company, Inc.

WAYNE A. REAUD Reaud, Morgan & Quinn, LLP

JOSEPH B. SWINBANK The Sprint Companies

SHEILA UMPHREY The Decorating Depot

JOHN EDDIE WILLIAMS, JR. Williams, Kherkher, Hart & Boundas, LLP

W.E. "BILL" WILSON, JR. Wilson & Company

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JAMES R. BROOKS **Lockton Companies**

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STEVE McREYNOLDS **Groves Equipment**

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SCOTT PARKER Parker's Building Supply

J. PAT PARSONS CommunityBank of Texas

JOE PENLAND, SR. Quality Mat Company, Inc.

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JOSEPH B. SWINBANK The Sprint Companies

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ROBERT T. PIGOTT, JR. Senior Executive Vice President and Chief Financial Officer

JUSTIN M. LONG Senior Executive Vice President and General Counsel

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Chief Executive Officer J. PAT PARSONS

Vice Chairman

ROBERT T. PIGOTT, JR. Senior Executive Vice President and Chief Financial Officer

TAWN VANDENBERG Senior Executive Vice President and Chief Administration Officer

DEBORAH DINSMORE Senior Executive Vice President and Chief Information Officer

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