MBIA INC
Form SC 13G/A
February 13, 2009

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

SCHEDULE 13G/A
Under the Securities Exchange Act of 1934
(Amendment No._)*

M B I A Inc.

(Name of Issuer)

Common Stock

(Title of Class of Securities)

55262C100

(CUSIP Number)

December 31, 2008

(Date of Event Which Requires Filing of this Statement)

Check the appropriate box to designate the rule pursuant to which this Schedule is filed:

[X] Rule 13d-1(b)

[_] Rule 13d-1(c)

[_] Rule 13d-1(d)

*The remainder of this cover page shall be filled out for a reporting person's initialfiling on this form with respect to the subject class of securities, and for any subsequent amendment containing information which would alter the disclosures provided in a prior cover page.

The information required in the remainder of this cover page shall not be deemed to be "filed" for the purpose of Section 18 of the Securities Exchange Act of 1934 ("Act") or otherwise subject to the liabilities of that section of the Act but shall be subject to all other provisions of the Act (however, see the Notes).

Persons who respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB control number.

SEC 1745 (03-06)

CUSIP No. 55262C100 13G

1. Name of Reporting Person
I.R.S. Identification No. of above Person

Davis Selected Advisers, L.P.

2. Check the Appropriate Box if a Member of a Group
(a) [_]
(b) [_]

3. SEC Use Only

4. Citizenship or Place of Organization

Colorado Limited Partnership

Number of Shares Beneficially Owned by Each Reporting Person With:	
	5. Sole Voting Power 4,618,337 shares
	6. Shared Voting Power 0
	7. Sole Dispositive Power 4,933,279 shares
	8. Shared Dispositive Power 0

9. Aggregate Amount Beneficially Owned by Each Reporting Person

4,933,279 shares

10. Check if the Aggregate Amount in Row (9) Excludes Certain Shares

[_]

11. Percent of Class Represented by Amount in Row (9)

1.81%

12. Type of Reporting Person

IA

Item 1(a). Name of Issuer:
M B I A Inc.

Item 1(b). Address of Issuer's Principal Executive Offices:
113 KING ST ARMONK NY 10504

Item 2(a). Name of Persons Filing:
Davis Selected Advisers, L.P.

Item 2(b). Address of Principal Business Office or, if none, Residence:
2949 East Elvira Road, Suite 101
Tucson, Arizona 85756

Item 2(c). Citizenship:
Colorado Limited Partnership

Item 2(d). Title of Class of Securities:
Common Stock

Item 2(e). CUSIP Number:
55262C100

Item 3. If this statement is filed pursuant to Rules 13d-1(b) or 13d-2(b) or (c), check whether the person filing is a :

(a).[_] Broker or dealer registered under Section 15 of the Act (15 U.S.C. 78o).

(b).[_] Bank as defined in Section 3(a)(6) of the Act (15 U.S.C. 78c).

(c).[_] Insurance company as defined in Section 3(a)(19) of the Act (15 U.S.C. 78c).

(d).[X] Investment company registered under Section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8).

(e).[_] An investment adviser in accordance with Rule 13d-1(b)(1)(ii)(E);

(f).[_] An employee benefit plan or endowment fund in accordance with Rule 13d-1(b)(1)(ii)(F);

(g).[_] A parent holding company or control person in accordance with Rule 13d-1(b)(1)(ii)(G);

(h).[_] A savings association as defined in Section 3(b) of the Federal Deposit Insurance Act (12 U.S.C. 1813);

(i).[_] A church plan that is excluded from the definition of an investment company under Section 3(c)(14) of the Investment Company Act of 1940 (15 U.S.C. 80a-3);

(j).[_] Group, in accordance with Rule 13d-1(b)(1)(ii)(J).

Item 4. Ownership.

(a). Amount beneficially owned:
See the response(s) to Item 9 on the attached cover page(s).

(b). Percent of Class:
See the response(s) to Item 11 on the attached cover page(s).

(c). Number of shares as to which such person has:

(i). Sole power to vote or to direct the vote: See the response(s) to Item 5 on the attached cover page(s).

(ii). Shared power to vote or to direct the vote: See the response(s) to Item 6 on the attached cover page(s).

(iii). Sole power to dispose or to direct the disposition of: See the response(s) to Item 7 on the attached cover page(s).

(iv). Shared power to dispose or to direct the disposition of: See the response(s) to Item 8 on the attached cover page(s).

Item 5. Ownership of Five Percent or Less of a Class.
Yes

Item 6. Ownership of More than Five Percent on Behalf of Another Person.

Not Applicable

Item 7. Identification and Classification of the Subsidiary Which Acquired the Security Being Reported on by the Parent Holding Company.

Not Applicable

Item 8. Identification and Classification of Members of the Group.
Not Applicable

Item 9. Notice of Dissolution of Group.
Not Applicable

Item 10. Certification.
By signing below I certify that, to the best of my knowledge and belief, the securities referred to above were acquired and are held in the ordinary course of business and were not acquired and are not held for the purpose of or with the effect of changing or influencing the control of the issuer of the securities and were not acquired and are not held in connection with or as a participant in any transaction having that purpose or effect.

After reasonable inquiry and to the best of my knowledge and belief, I certify that the information set forth in this statement is true, complete and correct.

SIGNATURE

After reasonable inquiry and to the best of my knowledge and belief, I certify that the information set forth in this statement is true, complete and correct.

BY	/s/ Anthony Frazia
PRINT	Anthony Frazia,JD, CRCP Co-Chief Compliance Officer/Director of Institutional Operations, Compliance and Risk Management

DATE February 13, 2009

>

161,811

162,030

3,662

(219)

Investment banking and advisory fees by business line:

Public finance

86,075

90,851

92,308

(4,776)

(1,457)

Capital markets

707

4,621

2,384

(3,914)

2,237

Retail

16,306

14,635

15,258

1,671

(623)

Structured finance

5,675

5,369

5,678

306

(309)

Clearing

1,152

515

48

637

467

Other

5

1

256

4

(255)

109,920

115,992

115,932

(6,072)

60

Other:

Structured finance

66,233

81,352

38,738

(15,119)

42,614

Capital markets

24,878

20,813

17,903

4,065

2,910

Other

1,917

5,798

(108)

(3,881)

5,906

93,028

107,963

56,533

(14,935)

51,430

Total noninterest income

368,421

385,766

334,495

(17,345)

51,271

Net revenue (2)

412,156

416,938

367,466

(4,782)

49,472

Noninterest expense (3):

Compensation and benefits expenses

250,614

252,772

255,629

(2,158)

(2,857)

Other

96,898

124,699

112,103

(27,801)

12,596

Total noninterest expense

347,512

377,471

367,732

(29,959)

9,739

Income before income taxes

$

64,644

$

39,467

$

(266)

$

25,177

$

39,733

(1) Securities commissions and fees includes income of $9.1 million, $3.9 million, and $1.4 million during 2017, 2016, and 2015, respectively, that is eliminated in consolidation.
(2) Net revenue is defined as the sum of total net interest income and total noninterest income.
(3) Noninterest expense includes provision for loan losses associated with the broker-dealer segment within other noninterest expenses.

The broker-dealer segment had net interest income of $43.7 million, $31.2 million and $33.0 million during 2017, 2016 and 2015, respectively. In the broker-dealer segment, interest is earned from securities lending activities, interest charged on customer margin loan balances and interest earned on investment securities used to support sales, underwriting and other customer activities. The increase in net interest income during 2017, compared with 2016, was primarily due to an increase in the net interest earned on mortgage-backed securities and an increase in the average stock borrowing balances offset by an increase in repo interest expense and bank loans due to increased borrowing rates and daily balances. The decrease in net interest income during 2016, compared with 2015 was primarily due to a decrease of 21% in the broker-dealer segment's average stock borrowing balances.

Noninterest income was $368.4 million, $385.8 million and $334.5 million during 2017, 2016 and 2015, respectively. The decrease in noninterest income of $17.3 million during 2017, compared with 2016, was primarily due to a decrease of $14.9 million in other noninterest income and a decrease of $6.1 million in investment banking and advisory fees. The increase in noninterest income of $51.3 million during 2016, compared with 2015, was primarily due to an increase of $51.4 million in other noninterest income.

Securities commissions and fees increased $3.7 million during 2017, compared with 2016. The increase was primarily attributable to fees earned on money market accounts and FDIC insured bank deposits by the clearing and retail businesses resulting from the 61-basis point increase in the federal funds rate during 2017. This increase was partially offset by a reduction in securities commissions and fees earned in the capital markets business on the sale of over-the-counter, municipal and mortgage backed security products. Although securities commissions and fees were relatively flat between 2015 and 2016, the securities commissions and fees earned by our clearing business increased $7.0 million from fees earned on money markets and FDIC insured bank deposits resulting from the 25-basis point increase in the federal funds rate in December 2015, partially offset by a reduction in securities commissions and fees earned in our capital markets and retail businesses of $4.8 million from decreases in municipal bond transactions and insurance product sales.

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Investment banking and advisory fees decreased $6.1 million during 2017, compared with 2016, primarily due to reductions in the number and the aggregate dollar amount of municipal bond transactions and the municipal finance and underwriting fees associated with those and other taxable transactions. Although public finance revenues decreased in 2017 compared to 2016, national municipal issuances surged in the fourth quarter of 2017, due to the anticipated effects of the Tax Legislation. A number of national municipal issuers elected to accelerate certain capital raising initiatives before these changes were enacted. As a result, we anticipate lower municipal issuance volume in 2018. Investment banking and advisory fees were relatively flat between 2015 and 2016.

The decrease in other noninterest income during 2017, compared with 2016, was primarily due to a decrease of $15.1 million in income earned from trading gains associated with the structured finance business and a decrease of $4.5 million in the value of broker-dealer segment investments held at corporate, partially offset by increases of $4.1 million in income earned from trading gains associated with the capital markets business from the sale of municipal bonds and $0.7 million in the value of investments held in the broker-dealer segment's deferred compensation plan. The increase in other noninterest income during 2016, compared with 2015, was primarily due to an increase of $45.5 million in income earned from trading gains associated with the structured finance and capital markets businesses and a $4.1 million increase in other noninterest income due to a non-recurring reversal of a contingent liability associated with an investment.

Noninterest expenses were $347.5 million, $377.5 million and $367.8 million during 2017, 2016 and 2015, respectively. The decrease in noninterest expenses of $30.0 million during 2017, compared with 2016, was primarily due to a decrease of $24.4 million in legal expenses associated with settled litigation, a decrease in pre-tax integration-related professional costs of $2.9 million and a decrease of $2.2 million in compensation and benefits expenses, which was in part a product of the integration and merger of FSC and Hilltop Securities and in part due to the decrease in the variable compensation and benefits expense components that are based on each business lines' performance. The increase in noninterest expenses of $9.7 million during 2016, compared with 2015, was primarily due to an increase in legal expenses associated with both resolved and ongoing litigation matters, partially offset by a decrease of $2.9 million in compensation and benefits expenses. This decrease in compensation and benefits expense was primarily as a result of a decrease in salaries and benefits, which was in part a product of the integration and merger of FSC and Hilltop Securities, partially offset by an increase in incentive pay given the improvement in year-over-year operating performance. During 2016, the broker-dealer segment incurred pre-tax integration-related costs resulting from employee expenses, professional fees and contractual expenses of $2.9 million, $2.9 million and $0.1 million, respectively, compared with pre-tax transaction costs of $0.8 million, and employee expenses, professional fees, and contractual expenses of $6.9 million, $5.6 million and $1.9 million, respectively, during 2015 directly attributable to the integration of the operations acquired in the SWS Merger.

Effective as of January 22, 2016, we merged FSC and Hilltop Securities into a combined firm operating under the "Hilltop Securities" name. The integration is complete and Hilltop Securities does not expect to incur any additional integration costs in relation to the SWS Merger.

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Selected information concerning the broker-dealer segment follows (dollars in thousands).

	Year Ended December 31,		
	2017	2016	2015
Compensation as a % of net revenue	60.8 %	60.6 %	69.6 %
FDIC insured program balances at PlainsCapital Bank (end of period)	$ 1,301,148	$ 1,000,310	$ 845,569
Other FDIC insured program balances (end of period)	$ 1,093,493	$ 1,517,482	$ 1,380,030
Customer margin balances (end of period)	$ 349,794	$ 332,806	$ 414,013
Customer funds on deposit, including short credits (end of period)	$ 411,989	$ 385,104	$ 474,773
Public finance:			
Number of issues	1,561	1,747	1,655
Aggregate amount of offerings	$ 83,907,144	$ 82,561,809	$ 70,021,094
Capital markets:			
Total volumes	$ 65,559,604	$ 76,482,509	$ 76,737,890
Net inventory (end of period)	$ 491,370	$ 95,925	$ 62,879
Retail:			
Retail employee representatives (end of period)	120	117	118
Independent registered representatives (end of period)	218	224	234
Structured finance:			
Lock production/TBA volume	$ 5,938,788	$ 6,088,319	$ 3,848,214
Clearing:			
Total tickets (1)	1,325,760	1,669,856	2,396,478
Correspondents (end of period)	162	175	205
Securities lending:			
Interest-earning assets - stock borrowed (end of period)	$ 1,386,821	$ 1,436,069	$ 1,307,741
Interest-bearing liabilities - stock loaned (end of period)	$ 1,215,093	$ 1,283,676	$ 1,235,466

(1) Effective May 2016, a single correspondent began compressing multiple executions when delivering trades for processing, resulting in a decrease in year-over-year ticket count for the broker-dealer segment's clearing business line. This modification did not significantly impact the correspondent's clearing revenues.

Mortgage Origination Segment

Income before income taxes in our mortgage origination segment during 2017, 2016 and 2015 was $49.6 million, $77.8 million and $47.5 million, respectively. The year-over-year decrease in income before income taxes during

2017, compared with 2016, was primarily due to a decrease in noninterest income, partially offset by decreases in noninterest expense and net interest expense. The increase in income before income taxes during 2016, compared with 2015, was primarily due to an increase in noninterest income, partially offset by an increase in noninterest expense. Net interest expense of $0.9 million, $11.6 million and $10.4 million during 2017, 2016 and 2015, respectively, was primarily comprised of interest incurred on a warehouse line of credit held with the Bank as well as related intercompany financing costs, partially offset by interest income earned on loans held for sale. The improvement in net interest expense during 2017 compared with 2016 included the effects of increased average hold periods and improved net yields on mortgage loans held for sale.

The mortgage lending business is subject to variables that can impact loan origination volume, including seasonal and interest rate fluctuations. Historically, the mortgage origination segment has typically experienced increased loan origination volume from purchases of homes during the spring and summer, when more people tend to move and buy or sell homes. An increase in mortgage interest rates tends to result in decreased loan origination volume from refinancings, while a decrease in mortgage interest rates tends to result in increased loan origination volume from refinancings. During 2017, PrimeLending’s refinancing volume was $2.5 billion, a decrease from $4.2 billion during 2016. Due to increases in mortgage interest rates since the fourth quarter of 2016, refinancing volume and refinancing volume as a percentage of total loan origination volume decreased to 17.2% in 2017 as compared to 27.1% in 2016. We anticipate the percentage of refinance volume relative to total loan origination volume will decrease slightly in 2018.

The mortgage origination segment primarily originates its mortgage loans through a retail channel, with limited lending through its affiliated business relationships (“ABAs”). For 2017, funded loan volume through ABAs was less than 5% of the mortgage origination segment’s total loan volume. Currently, PrimeLending owns a 51% membership interest in three ABAs. We expect production within the ABA channel to represent approximately 5% of the total loan volume during 2018, a slight increase from 2017.

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The following table provides certain details regarding our mortgage loan originations and sales for the periods indicated below (dollars in thousands).

	Year Ended December 31,					
	2017		2016		2015	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
Mortgage Loan Originations - units	62,058		66,881		59,621	
Mortgage Loan Originations - volume	$ 14,457,913		$ 15,460,213		$ 13,352,119	
Mortgage Loan Originations:						
Conventional	$ 8,666,935	59.95 %	$ 9,897,230	64.02 %	$ 8,394,709	62.87 %
Government	3,440,264	23.80 %	3,595,219	23.25 %	3,395,587	25.43 %
Jumbo	1,415,682	9.79 %	1,312,800	8.49 %	961,598	7.20 %
Other	935,032	6.46 %	654,964	4.24 %	600,225	4.50 %
	$ 14,457,913	100.00 %	$ 15,460,213	100.00 %	$ 13,352,119	100.00 %
Home purchases	$ 11,974,571	82.82 %	$ 11,276,378	72.94 %	$ 9,891,792	74.08 %
Refinancings	2,483,342	17.18 %	4,183,835	27.06 %	3,460,327	25.92 %
	$ 14,457,913	100.00 %	$ 15,460,213	100.00 %	$ 13,352,119	100.00 %
Texas	$ 3,129,008	21.64 %	$ 3,352,469	21.69 %	$ 2,967,740	22.23 %
California	1,846,172	12.77 %	2,235,915	14.46 %	1,965,039	14.72 %
Florida	853,727	5.90 %	797,578	5.16 %	644,090	4.82 %
Ohio	634,142	4.39 %	637,435	4.12 %	555,106	4.16 %
Arizona	554,463	3.84 %	527,055	3.41 %	415,215	3.11 %
South Carolina	472,935	3.27 %	446,221	2.89 %	385,347	2.88 %
Washington	465,501	3.22 %	538,857	3.49 %	451,277	3.38 %
Missouri	448,565	3.10 %	441,125	2.85 %	379,621	2.84 %
North Carolina	440,456	3.05 %	512,087	3.31 %	492,879	3.69 %
Maryland	430,668	2.98 %	521,686	3.37 %	452,280	3.39 %
All other states	5,182,276	35.84 %	5,449,785	35.25 %	4,643,525	34.78 %
	$ 14,457,913	100.00 %	$ 15,460,213	100.00 %	$ 13,352,119	100.00 %
Mortgage Loan Sales - volume	$ 14,454,260		$ 15,155,340		$ 13,129,069	

Refinancing volume decreased to $2.5 billion during 2017 from $4.2 billion during 2016 (representing 17.2% and 27.1%, respectively, of total loan origination volume), while home purchases volume increased 6.2% to $12.0 billion during 2017 from $11.3 billion during 2016. Refinancing volume increased to $4.2 billion from $3.5 billion during 2016, compared with 2015 (representing 27.1% and 25.9%, respectively, of total loan origination volume), while home purchases volume increased 14.0% to $11.3 billion during 2016 from $9.9 billion during 2015.

The mortgage origination segment's total loan origination volume during 2017 decreased 6.5%, compared with 2016, while income before income taxes during 2017 decreased 36.3%, compared with 2016. The decrease in income before income taxes during 2017 was primarily due to a decrease in net gains from sale of loans, in addition to a decrease in the change in net fair value of interest rate lock commitments ("IRLCs") and loans held for sale. These changes were partially offset by decreases in compensation that varies with the volume of mortgage loan originations ("variable compensation"), net interest expense, and lender paid closing costs. The mortgage origination segment's total loan origination volume increased 15.8% between 2016 and 2015, while income before income taxes during 2016 increased 63.8%, compared with 2015. The increase in income before income taxes between 2016 and 2015 was primarily due to an increase in net gains from sale of loans, partially offset by increases in variable compensation and segment operating costs.

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Noninterest income was $632.4 million, $704.1 million and $597.2 million during 2017, 2016 and 2015, respectively, and was comprised of the following (in thousands).

	Year Ended December 31,			Variance	
				2017 vs	2016 vs
	2017	2016	2015	2016	2015
Net gains from sale of loans	$ 536,007	$ 577,003	$ 491,532	$ (40,996)	$ 85,471
Mortgage loan origination fees	94,244	96,267	77,708	(2,023)	18,559
Other mortgage production income:					
Change in net fair value and related derivative activity:					
Interest rate lock commitments and loans held for sale	(14,451)	13,357	13,796	(27,808)	(439)
Mortgage servicing rights asset	(4,132)	(6,277)	(5,424)	2,145	(853)
Servicing fees	20,720	23,776	19,551	(3,056)	4,225
	$ 632,388	$ 704,126	$ 597,163	$ (71,738)	$ 106,963

Net gains from sale of loans and mortgage origination fees decreased 7.1% and 2.1% during 2017, respectively, compared with 2016, while net gains from sale of loans and mortgage origination fees increased 17.4% and 23.9% during 2016, respectively, compared with 2015. The decrease in net gains from sale of loans during 2017, compared with 2016, was primarily the result of a 4.6% decrease in total loan sales volume in addition to a decrease in average loan sales margin during the same periods. The decrease in mortgage loan origination fees was primarily the result of a decrease in total loan origination volume during 2017, compared with 2016, partially offset by an increase in average mortgage loan origination fees during the same periods. The increase in net gains from sale of loans during 2016, compared with 2015, was primarily the result of a 15.4% increase in total loan sales volume as well as a slight increase in average loan sales margin. The increase in mortgage loan origination fees during 2016 was a result of increases in total loan origination volume and average mortgage loan origination fees, compared with 2015.

Noninterest income included a decrease of $14.5 million during 2017, and increases of $13.4 million and $13.8 million during 2016 and 2015, respectively, in the net fair value of the mortgage origination segment's IRLCs and loans held for sale and the related activity associated with forward commitments used by the mortgage origination segment to mitigate interest rate risk associated with its IRLCs and mortgage loans held for sale. The decrease during 2017, compared with 2016, was primarily the result of decreases in the total volume of individual IRLCs and mortgage loans and the average value of individual IRLCs and mortgage loans at the end of these periods. The increase during 2016, compared with 2015, was primarily the result of increases in the volume of IRLCs and mortgage loans held and the average value of individual IRLCs and mortgage loans at the end of these periods.

The mortgage origination segment sells substantially all mortgage loans it originates to various investors in the secondary market, the majority servicing released. During 2017, 2016 and 2015, the mortgage origination segment retained servicing on approximately 11%, 16% and 18% of loans sold, respectively. The mortgage origination segment's determination of whether to retain or release servicing on mortgage loans it sells is impacted by, among

other things, changes in mortgage interest rates and refinancing and market activity. The related mortgage servicing rights ("MSR") asset was valued at $55.8 million on $4.9 billion of serviced loan volume at December 31, 2017, compared with a value of $63.3 million on $5.6 billion of serviced loan volume at December 31, 2016. The mortgage origination segment may, from time to time, manage its MSR asset through different strategies, including varying the percentage of mortgage loans sold servicing released and opportunistically selling MSR assets. The mortgage origination segment has also retained servicing on certain loans sold to the banking segment. Gains and losses associated with such sales to the banking segment and the related MSR asset are eliminated in consolidation. The mortgage origination segment uses derivative financial instruments, including various combinations of interest rate swaps, swaptions, forward commitments to sell mortgage-backed securities, and U.S. Treasury bond futures and options, as a means to mitigate interest rate risk associated with its MSR asset. Changes in the net fair value of the MSR asset and the related derivatives associated with normal customer payments, changes in discount rates, prepayment speed assumptions and customer payoffs resulted in net losses of $4.1 million, $6.3 million and $5.4 million during 2017, 2016 and 2015, respectively. Additionally, net servicing income was $8.6 million, $10.2 million and $8.9 million during 2017, 2016 and 2015, respectively. In March 2017 and May 2016, the mortgage origination segment sold MSR assets of $17.5 million and $7.6 million, respectively, which represented $1.7 billion and $917.4 million, respectively, of its serviced loan volume at the time.

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Noninterest expense was $581.9 million, $614.7 million and $539.3 million during 2017, 2016 and 2015, respectively, and was comprised of the following (in thousands).

	Year Ended December 31,			Variance	
				2017 vs	2016 vs
	2017	2016	2015	2016	2015
Variable compensation	$ 244,333	$ 266,373	$ 228,590	$ (22,040)	$ 37,783
Segment operating costs	299,453	299,733	263,049	(280)	36,684
Lender paid closing costs	26,031	35,061	37,010	(9,030)	(1,949)
Servicing expense	12,082	13,574	10,608	(1,492)	2,966
	$ 581,899	$ 614,741	$ 539,257	$ (32,842)	$ 75,484

Employees' compensation and benefits accounted for the majority of the noninterest expenses incurred during all periods presented. Variable compensation decreased $22.0 million during 2017, compared with 2016, and comprised 59.1% and 61.5% of the total employees' compensation and benefits expenses during 2017 and 2016, respectively. Variable compensation increased $37.8 million during 2016, compared with 2015, and comprised 62.2% of the total employees' compensation and benefits expenses during 2015. Variable compensation, which is primarily driven by loan origination volume, tends to fluctuate to a greater degree than loan origination volume because mortgage loan originator and fulfillment staff incentive compensation plans are structured to pay at increasing rates as higher monthly volume tiers are achieved. However, certain other incentive compensation plans driven by non-mortgage production criteria may alter this trend.

While total loan origination volumes decreased 6.5% during 2017, compared with 2016, the mortgage origination segment's operating costs remained relatively unchanged. The largest fluctuations in segment operating costs during 2017, compared with 2016, were an increase in costs resulting from an increase in the number of mortgage branch locations and decreases in both corporate and loan processing headcount as a result of decreased loan volume. During 2016, operating costs increased 13.9%, compared with 2015, while total loan origination volumes increased 15.8%. The increase in segment operating costs was primarily the result of increases in headcount related to loan processing, loan fulfillment and technology functions. The increases in loan processing and fulfillment headcount levels were initiated during 2015 primarily to address growth in loan origination volume that began in 2014 and to address October 2015 implementation of TILA RESPA Integrated Disclosures ("TRID"). Additional increases in segment operating costs during 2016, compared with 2015, were primarily increases in costs associated with loan servicing, an increase in mortgage branch locations, business development and administrative activities. Historically, segment operating costs tend to fluctuate with, but at a lesser magnitude than, loan origination volume, as these costs are comprised of salaries, benefits, occupancy and administrative costs, which are not normally highly sensitive to changes in loan origination volume.

In exchange for a higher interest rate, customers may opt to have PrimeLending pay certain costs associated with the origination of their mortgage loan ("lender paid closing costs"). Fluctuations in lender paid closing costs are not always aligned with fluctuations in loan origination volume. Other loan pricing conditions, including the mortgage loan interest rate, loan origination fees paid by the customer, and a customer's willingness to pay closing costs, may

influence fluctuations in lender paid closing costs.

Between January 1, 2008 and December 31, 2017, the mortgage origination segment sold mortgage loans totaling $101.5 billion. These loans were sold under sales contracts that generally include provisions that hold the mortgage origination segment responsible for errors or omissions relating to its representations and warranties that loans sold meet certain requirements, including representations as to underwriting standards and the validity of certain borrower representations in connection with the loan. In addition, the sales contracts typically require the refund of purchased servicing rights plus certain investor servicing costs if a loan experiences an early payment default. While the mortgage origination segment sold loans prior to 2008, it does not anticipate experiencing significant losses in the future on loans originated prior to 2008 because of investor claims under these provisions of its sales contracts.

When a claim for indemnification of a loan sold is made by an agency, investor, or other party, the mortgage origination segment evaluates the claim and determines if the claim can be satisfied through additional documentation or other deliverables. If the claim is valid and cannot be satisfied in that manner, the mortgage origination segment negotiates with the claimant to reach a settlement of the claim. Settlements typically result in either the repurchase of a loan or reimbursement to the claimant for losses incurred on the loan.

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Following is a summary of the mortgage origination segment's claims resolution activity relating to loans sold between January 1, 2008 and December 31, 2017 (dollars in thousands).

	Original Loan Balance		Loss Recognized	
	Amount	% of Loans Sold	Amount	% of Loans Sold
Claims resolved with no payment	$ 214,259	0.21%	$ —	0.00%
Claims resolved because of a loan repurchase or payment to an investor for losses incurred (1)	241,529	0.24%	16,332	0.02%
	$ 455,788	0.45%	$ 16,332	0.02%

(1) Losses incurred include refunded purchased servicing rights.

The mortgage origination has established a specific claims indemnification liability reserve for each loan it concludes its obligation to a claimant is both probable and reasonably estimable. An additional indemnification liability reserve has been established for probable agency, investor or other party losses that may have been incurred, but not yet reported to the mortgage origination segment based upon a reasonable estimate of such losses.

At December 31, 2017 and 2016, the mortgage origination segment's total indemnification liability reserve totaled $23.5 million and $18.2 million, respectively. The related provision for indemnification losses was $4.0 million, $4.6 million, and $4.0 million during 2017, 2016 and 2015, respectively.

Insurance Segment

Losses before income taxes in our insurance segment were $4.1 million during 2017, compared with income before income taxes of $21.4 million and $15.7 million during 2016 and 2015, respectively. These year-over-year changes during 2017, compared with 2016 and 2015, were driven primarily by a decline in net insurance premiums earned, loss and LAE effects of Hurricane Harvey, and other non-catastrophic weather-related losses experienced during 2017.

The insurance segment is subject to claims arising out of severe weather, the incidence and severity of which are inherently unpredictable. Generally, the insurance segment's insured risks exhibit higher losses in the second and third calendar quarters due to a seasonal concentration of weather-related events in its primary geographic markets. Although weather-related losses (including hail, high winds, tornadoes and hurricanes) can occur in any calendar quarter, the second calendar quarter, historically, has experienced the highest frequency of losses associated with these

events. Hurricanes, however, are more likely to occur in the third calendar quarter of the year.

The insurance segment periodically reviews the pricing of its primary products in each state of operation utilizing a consulting actuarial firm to supplement normal review processes resulting in filings to adjust rates as deemed necessary. The benefit of these rate actions are not fully realized until all policies under the old rates expire, which typically occurs one year from the date of rate change implementation. Concurrently, business concentrations are reviewed and actions initiated, including cancellation of agents, non-renewal of policies and cessation of new business writing on certain products in problematic geographic areas. The insurance segment has historically utilized rate actions to reduce the rate of premium growth for targeted areas when compared with the patterns exhibited in prior quarters and years and reduce the insurance segment’s exposure to volatile weather in these areas, but competition and customer response to rate increases has negatively impacted customer retention and new business. The insurance segment aims to manage and diversify its business concentrations and products to minimize the effects of future weather-related events.

The noted negative impact on premiums written and earned and the significance of the higher net loss and LAE incurred due to current year weather-related events, including Hurricane Harvey, have had a negative impact on current year operating results. In response, we continue to undertake initiatives to help grow net insurance premiums written and earned, streamline business activities and expenses, mitigate the impact of future significant weather-related events, as well as evaluate product offerings and pricing to improve the insurance segment’s long-term financial condition and operating results. These initiatives, as well as other assumptions and conditions, were reflected in the insurance segment’s annual impairment evaluation of goodwill and other intangible assets as of October 1, 2017, which indicated no impairment of goodwill. This analysis and the resulting estimated fair value of our insurance reporting unit exceeded the carrying value by approximately 12%, which represented a decline in estimated excess fair value over carrying value from

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recent annual goodwill assessments. This decrease in the excess fair value over carrying value from our 2016 assessment to our 2017 assessment was primarily a result of a reduction in projected discounted cash flows driven by the insurance reporting unit's current operating performance being below expectations, which was primarily attributable to catastrophic and sub-catastrophic weather-related events that occurred in 2017. In the event future operating performance is below our forecasted projections, there are negative changes to long-term growth rates or discount rates increase, the fair value of the insurance reporting unit may decline and we may be required to record a goodwill impairment charge.

The changes experienced in operating results between periods were primarily a result of changes in claims loss experience associated with the general severity of non-catastrophic and severe weather-related events, and declines in net insurance premiums written and earned. Based on our estimates of the ultimate losses, claims associated with severe weather-related events during 2017 totaled $38.1 million through December 31, 2017, with a net loss, after reinsurance, of $33.5 million during 2017. During 2016, and based on our estimates of the ultimate losses, claims associated with severe weather-related events during 2016 totaled $44.0 million through December 31, 2016, with a net loss, after reinsurance, of $34.0 million during 2016. During 2015, and based on our estimates of the ultimate losses, claims associated with severe weather-related events totaled $35.3 million through December 31, 2015, with a net loss, after reinsurance, of $26.2 million during 2015.

The insurance segment's operations resulted in a combined ratio of 106.5% during 2017, compared with 90.9% and 94.9% during 2016 and 2015, respectively. The increase in the combined ratio during 2017, compared with 2016, included increases in the loss and LAE ratio and the underwriting expense ratio as previously discussed. The decrease in the combined ratio during 2016, compared with 2015, was primarily due to the benefit of the current reinsurance structure that has limited the insurance segment's retention of claims losses associated with sub-catastrophic weather-related events experienced through December 31, 2016. Additionally, premiums earned decreasing at a lower rate than loss and LAE expense also contributed to the decline in the combined ratio during 2016, compared with 2015. The combined ratio is a measure of overall insurance underwriting profitability, and represents the sum of loss and LAE and underwriting expenses divided by net insurance premiums earned.

Noninterest income of $151.4 million, $164.8 million and $171.2 million during 2017, 2016 and 2015, respectively, included net insurance premiums earned of $142.3 million, $155.5 million and $162.1 million, respectively. The decreases in net insurance premiums earned during 2017 and 2016, compared with 2016 and 2015, respectively, were primarily due to the effect of decreases in net insurance premiums written.

Direct insurance premiums written by major product line are presented in the table below (in thousands).

	Year Ended December 31,			Variance	
				2017 vs	2016 vs
	2017	2016	2015	2016	2015

Direct Insurance Premiums Written:					
Homeowners	$ 54,706	$ 64,816	$ 72,939	$ (10,110)	$ (8,123)
Fire	42,414	46,792	52,167	(4,378)	(5,375)
Mobile Home	36,925	37,953	38,161	(1,028)	(208)
Commercial	2,884	3,225	3,536	(341)	(311)
Other	162	184	222	(22)	(38)
	$ 137,091	$ 152,970	$ 167,025	$ (15,879)	$ (14,055)

The total direct insurance premiums written for our three largest insurance product lines decreased by $15.5 million during 2017, compared with 2016, and $13.7 million during 2016, compared with 2015, due primarily to the effects of competitive pressures in our Texas market.

Net insurance premiums earned by major product line are presented in the table below (in thousands).

	Year Ended December 31,			Variance	
	2017	2016	2015	2017 vs 2016	2016 vs 2015
Net Insurance Premiums Earned:					
Homeowners	$ 56,784	$ 65,907	$ 70,781	$ (9,123)	$ (4,874)
Fire	44,025	47,580	50,623	(3,555)	(3,043)
Mobile Home	38,328	38,592	37,032	(264)	1,560
Commercial	2,993	3,279	3,431	(286)	(152)
Other	168	187	215	(19)	(28)
	$ 142,298	$ 155,545	$ 162,082	$ (13,247)	$ (6,537)

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Net insurance premiums earned during 2017 and 2016 decreased, compared to 2016 and 2015, respectively, primarily due to the decreases in net premiums written noted above.

Noninterest expenses of $158.4 million, $146.6 million and $158.7 million during 2017, 2016 and 2015, respectively, included both loss and LAE expenses and policy acquisition and other underwriting expenses, as well as other noninterest expenses. Loss and LAE are recognized based on formula and case basis estimates for losses reported with respect to direct business, estimates of unreported losses based on past experience and deduction of amounts for reinsurance placed with reinsurers. Loss and LAE during 2017 was $94.7 million, compared to $89.2 million and $99.1 million during 2016 and 2015, respectively, resulting in loss and LAE ratios during 2017, 2016 and 2015 of 66.6%, 57.4% and 61.1%, respectively. The increase in the loss and LAE ratio during 2017, compared with 2016, was primarily driven by a 6.1% increase in loss and LAE expense and a decrease in premiums earned of 8.5%. The increase in the loss and LAE ratio during 2017 was attributable to non-catastrophic weather-related losses as well as Hurricane Harvey. The actual loss related to Hurricanes Harvey and Irma, excluding reinstatement premium, was $4.4 million after reinsurance. The lower claims loss experience during 2016, compared with 2015, was primarily driven by the benefit of the current reinsurance structure previously discussed, the effects of premiums earned decreasing at a lower rate than loss and LAE expense, and the decrease in claims loss reserves associated with prior period adverse development of $6.1 million.

The insurance segment seeks to generate underwriting profitability. Management evaluates NLC's loss and LAE ratio by bifurcating the losses to derive catastrophic and non-catastrophic loss ratios. The non-catastrophic loss ratio excludes Property Claims Services events that exceed $1.0 million of losses to NLC. Catastrophic events, including those that do not exceed our reinsurance retention, affect insurance segment loss ratios. During 2017, catastrophic events that did not exceed reinsurance retention accounted for $33.5 million of the total loss and LAE, as compared to $34.0 million and $26.2 million during 2016 and 2015, respectively. The inclusion of catastrophic events increased insurance segment combined ratios by 23.5%, 21.9% and 16.2% during 2017, 2016 and 2015, respectively.

Policy acquisition and other underwriting expenses encompass all expenses incurred relative to NLC operations, and include elements of multiple categories of expense otherwise reported as noninterest expense in the consolidated statements of operations.

The following table details the calculation of the underwriting expense ratio for the periods presented (dollars in thousands).

	Year Ended December 31,			Variance	
	2017	2016	2015	2017 vs 2016	2016 vs 2015
Amortization of deferred policy acquisition costs	$ 36,549	$ 38,502	$ 40,258	$ (1,953)	$ (1,756)

Other underwriting expenses	23,930	16,998	17,609	6,932	(611)
Total	60,479	55,500	57,867	4,979	(2,367)
Agency expenses	(3,745)	(3,460)	(3,128)	(285)	(332)
Total less agency expenses	$ 56,734	$ 52,040	$ 54,739	$ 4,694	$ (2,699)
Net insurance premiums earned	$ 142,298	$ 155,545	$ 162,082	$ (13,247)	$ (6,537)
Expense ratio	39.9 %	33.5 %	33.8 %	6.4 %	(0.3) %

Corporate

Corporate includes certain activities not allocated to specific business segments. These activities include holding company financing and investing activities, merchant banking investment opportunities, and management and administrative services to support the overall operations of the Company including, but not limited to, certain executive management, corporate relations, legal, finance, and acquisition costs. Hilltop's merchant banking investment activities include the identification of attractive opportunities for capital deployment in companies engaged in non-financial activities through its increasingly active merchant bank subsidiary, PlainsCapital Equity, LLC ("PCE").

As a holding company, Hilltop's primary investment objectives are to support capital deployment for organic growth and to preserve capital to be deployed through acquisitions. Investment and interest income earned was $0.3 million during 2017, and $0.4 million during each of 2016 and 2015, respectively. Investment and interest income during 2016 and 2015 included $0.2 million and $0.3 million, respectively, of intercompany interest earned on notes receivable held with Securities Holdings that were paid off in January 2016 and March 2016, respectively.

As a result of previously disclosed strategic leadership and organizational changes, certain interest expenses, headcount and related noninterest expenses of PCC, which were previously allocated to the banking and mortgage origination segments, are included within corporate effective January 1, 2017.

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Interest expense was $10.4 million, $7.6 million and $5.5 million during 2017, 2016 and 2015, respectively. On April 9, 2015, as previously discussed, Hilltop completed its offering of $150.0 million aggregate principal amount of Senior Notes and used the net proceeds of the offering to redeem all of its outstanding Non-Cumulative Perpetual Preferred Stock, Series B ("Series B Preferred Stock") at an aggregate liquidation value of $114.1 million, plus accrued but unpaid dividends of $0.4 million. Consequently, recurring annual interest expense of $7.5 million is being incurred. In addition, interest expense during 2017 of $3.0 million on junior subordinated debentures of $67.0 million issued by PCC (the "Debentures") was included within corporate as a result of the organizational changes noted above. During 2016, interest expense on the Debentures of $2.7 million was reported within our operating segments.

Noninterest income during 2017 was primarily comprised of the previously mentioned pre-tax net increase to other noninterest income of $11.6 million related to the resolution of the appraisal proceedings from the SWS Merger. Noninterest income during 2016 was nominal, while noninterest income of $81.3 million during 2015 represented the recognition of a bargain purchase gain related to the SWS Merger. Included in the bargain purchase gain was a reversal of a $33.4 million valuation allowance against SWS deferred tax assets. This amount was based on our expected ability to realize these acquired deferred tax assets through our consolidated core earnings, the implementation of certain tax planning strategies and reversal of timing differences. SWS's net operating loss carryforwards are subject to an annual Section 382 limitation on their usage because of the ownership change.

Noninterest expenses of $34.0 million, $29.9 million and $31.9 million during 2017, 2016 and 2015, respectively, were primarily comprised of employees' compensation and benefits and professional fees, including corporate governance, legal and transaction costs. During 2017, compared with 2016, the change in noninterest expenses primarily included increases associated with the organizational changes noted above related to employees' compensation and benefits costs of $3.7 million, professional fees of $4.0 million, and occupancy and equipment expenses of $3.0 million, partially offset by a decrease of $5.3 million in transaction-related costs directly attributable to the SWS Merger. Specifically, during 2017, Hilltop incurred pre-tax transaction costs related to the SWS Merger of $2.1 million, compared with $7.4 million during 2016. During 2016, compared with 2015, noninterest expenses included a year-over-year decrease in transaction and integration-related costs directly attributable to the SWS Merger, partially offset by increases in employees' compensation and benefits costs of $2.3 million associated with increases in headcount and incentive compensation costs, as well as other professional fees. During 2016, Hilltop incurred pre-tax transaction costs related to the SWS Merger of $7.4 million, compared with pre-tax transaction costs related to the SWS merger of $12.9 million and pre-tax integration-related costs associated with professional fees of $0.5 million during 2015.

Financial Condition

The following discussion contains a more detailed analysis of our financial condition at December 31, 2017 as compared to December 31, 2016 and 2015.

Securities Portfolio

At December 31, 2017, investment securities consisted of securities of the U.S. Treasury, U.S. government and its agencies, obligations of municipalities and other political subdivisions, primarily in the State of Texas, mortgage-backed, corporate debt, and equity securities. We may categorize investments as trading, available for sale, and held to maturity.

Trading securities are bought and held principally for the purpose of selling them in the near term and are carried at fair value, marked to market through operations and held at the Bank and the Hilltop Broker-Dealers. Securities that may be sold in response to changes in market interest rates, changes in securities' prepayment risk, increases in loan demand, general liquidity needs and other similar factors are classified as available for sale and are carried at estimated fair value, with unrealized gains and losses recorded in accumulated other comprehensive income (loss). However, with the adoption of Accounting Standards Update 2016-01 in January 2018, the Company will reclassify all equity investments out of trading and available for sale securities, with all subsequent changes in fair value recognized in net income, leaving only debt securities within these categories of investment securities. Securities are classified as held to maturity based on the intent and ability of our management, at the time of purchase, to hold such securities to maturity. These securities are carried at amortized cost.

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The table below summarizes our securities portfolio (in thousands).

	December 31, 2017	2016	2015
Trading securities, at fair value			
U.S. Treasury securities	$ —	$ 5,940	$ 20,481
U.S. government agencies:			
Bonds	52,078	36,303	36,244
Residential mortgage-backed securities	372,817	2,539	12,505
Commercial mortgage-backed securities	6,125	15,171	19,280
Collateralized mortgage obligations	5,122	5,607	264
Corporate debt securities	96,182	60,699	34,735
States and political subdivisions	170,413	89,946	58,588
Unit investment trusts	22,612	41,409	18,400
Private-label securitized product	1,631	4,292	12,324
Other	3,705	3,628	1,325
	730,685	265,534	214,146
Securities available for sale, at fair value			
U.S. Treasury securities	24,669	31,801	44,603
U.S. government agencies:			
Bonds	96,640	122,652	296,636
Residential mortgage-backed securities	243,505	133,138	35,853
Commercial mortgage-backed securities	12,023	8,715	9,207
Collateralized mortgage obligations	233,812	114,702	52,701
Corporate debt securities	68,662	79,129	97,950
States and political subdivisions	65,008	87,515	118,725
Commercial mortgage-backed securities	—	515	531
Equity securities	21,241	19,840	17,500
	765,560	598,007	673,706
Securities held to maturity, at amortized cost			
U.S. Treasury securities	—	—	25,146
U.S. government agencies:			
Bonds	39,015	40,513	69,379
Residential mortgage-backed securities	16,130	19,606	23,735
Commercial mortgage-backed securities	71,373	31,767	18,658
Collateralized mortgage obligations	173,928	217,954	167,541
States and political subdivisions	55,403	41,991	27,563
	355,849	351,831	332,022
Total securities portfolio	$ 1,852,094	$ 1,215,372	$ 1,219,874

We had a net unrealized loss of $2.4 million related to the securities available for sale portfolio at December 31, 2017, compared with a net unrealized loss of $0.2 million, and a net unrealized gain of $3.7 million at December 31, 2016 and 2015, respectively.

Our net unrealized losses associated with the securities held to maturity portfolio were $5.9 million, $6.7 million and $0.6 million at December 31, 2017, 2016 and 2015, respectively.

Banking Segment

The banking segment’s securities portfolio plays a role in the management of our interest rate sensitivity and generates additional interest income. In addition, the securities portfolio is used to meet collateral requirements for public and trust deposits, securities sold under agreements to repurchase and other purposes. The available for sale securities portfolio serves as a source of liquidity. Historically, the Bank’s policy has been to invest primarily in securities of the U.S. government and its agencies, obligations of municipalities in the State of Texas and other high grade fixed income securities to minimize credit risk. At December 31, 2017, the banking segment’s securities portfolio of $993.0 million was comprised of trading securities of $6.5 million, available for sale securities of $630.7 million and held to maturity securities of $355.8 million.

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Broker-Dealer Segment

The broker-dealer segment holds securities to support sales, underwriting and other customer activities. The interest rate risk inherent in holding these securities is managed by setting and monitoring limits on the size and duration of positions and on the length of time the securities can be held. The Hilltop Broker-Dealers are required to carry their securities at fair value and record changes in the fair value of the portfolio in operations. Accordingly, the securities portfolio of the Hilltop Broker-Dealers included trading securities of $724.2 million at December 31, 2017. In addition, the Hilltop Broker-Dealers enter into transactions that represent commitments to purchase and deliver securities at prevailing future market prices to facilitate customer transactions and satisfy such commitments. Accordingly, the Hilltop Broker-Dealers' ultimate obligation may exceed the amount recognized in the financial statements. These securities, which are carried at fair value and reported as securities sold, not yet purchased in the consolidated balance sheet, had a value of $232.8 million at December 31, 2017. The Hilltop Broker-Dealers continue to evaluate market opportunities and from time to time will hold residential mortgage-backed securities in firm inventory which is sold to institutional clients and other counterparties.

Insurance Segment

The insurance segment's primary investment objective is to preserve capital and manage for a total rate of return. NLC's strategy is to purchase securities in sectors that represent the most attractive relative value. Our insurance segment invests the premiums it receives from policyholders until they are needed to pay policyholder claims or other expenses. At December 31, 2017, the insurance segment's securities portfolio was comprised of $134.9 million in available for sale securities and $5.8 million of other investments included in other assets within the consolidated balance sheet.

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The following table sets forth the estimated maturities of our debt securities, excluding trading securities, at December 31, 2017. Contractual maturities may be different (dollars in thousands, yields are tax-equivalent).

	One Year Or Less	One Year to Five Years	Five Years to Ten Years	Greater Than Ten Years	Total
U.S. Treasury securities:					
Amortized cost	$ 16,106	$ 3,597	$ 4,962	$ —	$ 24,665
Fair value	$ 16,049	$ 3,551	$ 5,069	$ —	$ 24,669
Weighted average yield	1.17 %	1.14 %	2.65 %	—	1.47 %
U.S. government agencies:					
Bonds:					
Amortized cost	$ 52,951	$ 30,893	$ 36,349	$ 14,999	$ 135,192
Fair value	$ 52,898	$ 30,577	$ 36,436	$ 14,556	$ 134,467
Weighted average yield	1.20 %	1.97 %	2.49 %	1.99 %	1.81 %
Residential mortgage-backed securities:					
Amortized cost	$ 43	$ 95	$ 677	$ 262,022	$ 262,837
Fair value	$ 43	$ 101	$ 694	$ 258,841	$ 259,679
Weighted average yield	1.85 %	3.61 %	6.40 %	2.22 %	2.23 %
Commercial mortgage-backed securities:					
Amortized cost	$ —	$ 3,393	$ 71,622	$ 8,324	$ 83,339
Fair value	$ —	$ 3,378	$ 71,142	$ 8,382	$ 82,902
Weighted average yield	—	2.39 %	2.22 %	3.14 %	2.31 %
Collateralized mortgage obligations:					
Amortized cost	$ 58	$ 9,268	$ 7,239	$ 395,211	$ 411,776
Fair value	$ 58	$ 9,122	$ 7,128	$ 387,482	$ 403,790
Weighted average yield	2.22 %	2.07 %	1.76 %	1.97 %	1.97 %
Corporate debt securities:					
Amortized cost	$ 5,751	$ 31,512	$ 28,687	$ 918	$ 66,868
Fair value	$ 5,810	$ 32,273	$ 29,573	$ 1,006	$ 68,662
Weighted average yield	5.53 %	3.13 %	3.37 %	6.24 %	3.48 %
States and political subdivisions:					
Amortized cost	$ 1,510	$ 2,595	$ 15,276	$ 100,046	$ 119,427
Fair value	$ 1,509	$ 2,587	$ 15,295	$ 100,698	$ 120,089
Weighted average yield	1.46 %	2.51 %	2.40 %	2.71 %	2.65 %
Total securities portfolio:					
Amortized cost	$ 76,419	$ 81,353	$ 164,812	$ 781,520	$ 1,104,104
Fair value	$ 76,367	$ 81,589	$ 165,337	$ 770,965	$ 1,094,258
Weighted average yield	1.53 %	2.43 %	2.50 %	2.17 %	2.19 %

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Non-Covered Loan Portfolio

Consolidated non-covered loans held for investment are detailed in the table below, classified by portfolio segment and segregated between those considered to be PCI loans and all other originated or acquired loans (in thousands). PCI loans showed evidence of credit deterioration on the date of acquisition that made it probable that all contractually required principal and interest payments would not be collected.

December 31, 2017	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 1,675,106	$ 6,099	$ 1,681,205
Real estate	2,981,984	29,540	3,011,524
Construction and land development	961,167	1,438	962,605
Consumer	40,319	127	40,446
Broker-dealer	577,889	—	577,889
Non-covered loans, gross	6,236,465	37,204	6,273,669
Allowance for loan losses	(58,919)	(2,038)	(60,957)
Non-covered loans, net of allowance	$ 6,177,546	$ 35,166	$ 6,212,712

December 31, 2016	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 1,687,781	$ 8,672	$ 1,696,453
Real estate	2,777,768	38,999	2,816,767
Construction and land development	783,383	3,467	786,850
Consumer	41,058	294	41,352
Broker-dealer	502,077	—	502,077
Non-covered loans, gross	5,792,067	51,432	5,843,499
Allowance for loan losses	(51,089)	(3,097)	(54,186)
Non-covered loans, net of allowance	$ 5,740,978	$ 48,335	$ 5,789,313

December 31, 2015	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 1,539,455	$ 13,350	$ 1,552,805
Real estate	2,260,464	52,775	2,313,239
Construction and land development	700,206	5,150	705,356
Consumer	44,893	779	45,672
Broker-dealer	590,545	—	590,545
Non-covered loans, gross	5,135,563	72,054	5,207,617
Allowance for loan losses	(40,929)	(4,486)	(45,415)
Non-covered loans, net of allowance	$ 5,094,634	$ 67,568	$ 5,162,202

December 31, 2014	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 1,366,984	$ 13,442	$ 1,380,426
Real estate	1,670,684	24,151	1,694,835
Construction and land development	404,465	9,178	413,643
Consumer	51,009	2,138	53,147
Broker-dealer	378,425	—	378,425
Non-covered loans, gross	3,871,567	48,909	3,920,476
Allowance for loan losses	(31,722)	(5,319)	(37,041)
Non-covered loans, net of allowance	$ 3,839,845	$ 43,590	$ 3,883,435

December 31, 2013	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 1,318,737	$ 36,816	$ 1,355,553
Real estate	1,418,003	39,250	1,457,253
Construction and land development	344,734	19,817	364,551
Consumer	51,067	4,509	55,576
Broker-dealer	281,713	—	281,713
Non-covered loans, gross	3,414,254	100,392	3,514,646
Allowance for loan losses	(30,104)	(3,137)	(33,241)
Non-covered loans, net of allowance	$ 3,384,150	$ 97,255	$ 3,481,405

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Banking Segment

The loan portfolio constitutes the major earning asset of the banking segment and typically offers the best alternative for obtaining the maximum interest spread above the banking segment's cost of funds. The overall economic strength of the banking segment generally parallels the quality and yield of its loan portfolio. The banking segment's loan portfolio consists of the non-covered loan portfolio and the covered loan portfolio. The covered loan portfolio consists of loans acquired in the FNB Transaction that are subject to loss-share agreements with the FDIC and is discussed below. The non-covered loan portfolio includes all other loans held by the Bank and is discussed herein.

The banking segment's total non-covered loans, net of the allowance for non-covered loan losses, were $7.2 billion, $6.9 billion and $5.9 billion at December 31, 2017, 2016 and 2015, respectively. The banking segment's non-covered loan portfolio includes a warehouse line of credit extended to PrimeLending, of which $1.5 billion, $1.6 billion and $1.4 billion was drawn at December 31, 2017, 2016 and 2015, respectively. Effective April 1, 2017, this warehouse line of credit was increased to $2.2 billion to address seasonal fluctuations in loan origination volumes. Amounts advanced against the warehouse line of credit are eliminated from net loans on our consolidated balance sheets. The banking segment does not generally participate in syndicated loan transactions and has no foreign loans in its portfolio.

At December 31, 2017, the banking segment had non-covered loan concentrations (loans to borrowers engaged in similar activities) that exceeded 10% of total non-covered loans in its real estate portfolio. The areas of concentration within our non-covered real estate portfolio were non-construction commercial real estate loans, non-construction residential real estate loans, and construction and land development loans, which represented 35.6%, 12.4% and 15.3%, respectively, of the banking segment's total non-covered loans at December 31, 2017. The banking segment's non-covered loan concentrations were within regulatory guidelines at December 31, 2017.

Broker-Dealer Segment

The loan portfolio of the broker-dealer segment consists primarily of margin loans to customers and correspondents. These loans are collateralized by the securities purchased or by other securities owned by the clients and, because of collateral coverage ratios, are believed to present minimal collectability exposure. Additionally, these loans are subject to a number of regulatory requirements as well as the Hilltop Broker-Dealers' internal policies. The broker-dealer segment's total non-covered loans, net of the allowance for non-covered loan losses, were $577.5 million, $501.9 million and $590.3 million at December 31, 2017, 2016 and 2015, respectively. The increase during 2017, compared to 2016, was primarily attributable to increases of $17.0 million in borrowings in margin accounts and $58.1 million in receivables from customers. The decrease during 2016, compared to 2015, was primarily attributable to decreases of $81.2 million in borrowings in margin accounts and $6.3 million in receivables from customers.

Mortgage Origination Segment

The loan portfolio of the mortgage origination segment consists of loans held for sale, primarily single-family residential mortgages funded through PrimeLending, and IRLCs with customers pursuant to which we agree to originate a mortgage loan on a future date at an agreed-upon interest rate. The components of the mortgage origination segment's loans held for sale and IRLCs are as follows (in thousands).

	December 31,		
	2017	2016	2015
Loans held for sale:			
Unpaid principal balance	$ 1,528,834	$ 1,706,383	$ 1,410,445
Fair value adjustment	52,770	42,115	50,390
	$ 1,581,604	$ 1,748,498	$ 1,460,835
IRLCs:			
Unpaid principal balance	$ 850,850	$ 944,550	$ 944,942
Fair value adjustment	18,851	23,269	23,762
	$ 869,701	$ 967,819	$ 968,704

The mortgage origination segment uses forward commitments to mitigate interest rate risk associated with its loans held for sale and IRLCs. The notional amounts of these forward commitments at December 31, 2017, 2016 and 2015 were $2.0 billion, $2.1 billion and $2.0 billion, respectively, while the related estimated fair values were ($0.2) million, $8.5 million and $(1.2) million, respectively.

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Covered Loan Portfolio

Banking Segment

Loans acquired in the FNB Transaction that are subject to loss-share agreements with the FDIC are referred to as "covered loans" and reported separately in our consolidated balance sheets. Under the terms of the loss-share agreements, the FDIC has agreed to reimburse the Bank the following amounts with respect to the covered assets (including covered loans): (i) 80% of net losses on the first $240.4 million of net losses incurred; (ii) 0% of net losses in excess of $240.4 million up to and including $365.7 million of net losses incurred; and (iii) 80% of net losses in excess of $365.7 million of net losses incurred. Net losses are defined as book value losses plus certain defined expenses incurred in the resolution of assets, less subsequent recoveries. Under the loss-share agreement for commercial assets, the amount of subsequent recoveries that are reimbursable to the FDIC for a particular asset is limited to book value losses and expenses actually billed plus any book value charge-offs incurred prior to the Bank Closing Date. There is no limit on the amount of subsequent recoveries reimbursable to the FDIC under the loss-share agreement for single family residential assets. The loss-share agreements for commercial and single family residential assets are in effect for five years and ten years, respectively, and the loss recovery provisions to the FDIC are in effect for eight years and ten years, respectively, from the Bank Closing Date. In accordance with the loss-share agreements, the Bank may be required to make a "true-up" payment to the FDIC approximately ten years following the Bank Closing Date if our actual net realized losses over the life of the loss-share agreements are less than the FDIC's initial estimate of losses on covered assets. The "true-up" payment is calculated using a defined formula set forth in the P&A Agreement. The initial estimate of the FDIC Indemnification Asset at the Bank Closing Date was recorded at the present value of 80% of $240.4 million. As of December 31, 2017, the Bank projects that the sum of actual plus projected covered losses and reimbursable expenses subject to the loss-share agreements will be less than $240.4 million. As a result, the Bank has recorded, and expects that it will continue to record, amortization associated with its FDIC Indemnification Asset. As of December 31, 2017, the Bank had billed $184.7 million of covered net losses to the FDIC, of which 80%, or $147.8 million, were reimbursable under the loss-share agreements. As of December 31, 2017, the Bank had received aggregate reimbursements of $145.8 million from the FDIC. While the ultimate amount of any "true-up" payment is unknown at this time and will vary based upon the amount of future losses or recoveries within our covered loan portfolio, the Bank has recorded a related "true-up" payment accrual of $16.3 million at December 31, 2017 based on the current estimate of aggregate realized losses on covered assets over the life of the loss-share agreements. Additionally, as estimates of realized losses on covered assets change, the value of the FDIC Indemnification Asset will be adjusted and therefore may not be realized. As noted above, if the Bank continues to experience favorable resolutions within its covered assets portfolio and covered losses, the Bank will be required to increase its "true-up" payment accrual and recognize amortization on the FDIC Indemnification Asset.

In connection with the FNB Transaction, the Bank acquired loans both with and without evidence of credit quality deterioration since origination. Based on purchase date valuations, the banking segment's portfolio of acquired covered loans had a fair value of $1.1 billion as of the Bank Closing Date, with no carryover of any allowance for loan losses. Unless the banking segment acquires additional loans subject to loss-share agreements with the FDIC, the covered portfolio will continue to decrease as covered loans are liquidated.

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Covered loans held for investment are detailed in the table below and classified by portfolio segment (in thousands).

December 31, 2017	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 861	$ 194	$ 1,055
Real estate	92,444	86,915	179,359
Construction and land development	1,711	4	1,715
Covered loans, gross	95,016	87,113	182,129
Allowance for loan losses	(32)	(2,697)	(2,729)
Covered loans, net of allowance	$ 94,984	$ 84,416	$ 179,400

December 31, 2016	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 1,185	$ 1,512	$ 2,697
Real estate	117,431	127,038	244,469
Construction and land development	3,757	5,204	8,961
Covered loans, gross	122,373	133,754	256,127
Allowance for loan losses	(69)	(344)	(413)
Covered loans, net of allowance	$ 122,304	$ 133,410	$ 255,714

December 31, 2015	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 1,294	$ 7,507	$ 8,801
Real estate	147,502	193,546	341,048
Construction and land development	9,524	20,921	30,445
Covered loans, gross	158,320	221,974	380,294
Allowance for loan losses	(32)	(1,500)	(1,532)
Covered loans, net of allowance	$ 158,288	$ 220,474	$ 378,762

December 31, 2014	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 10,345	$ 20,435	$ 30,780
Real estate	183,886	368,964	552,850
Construction and land development	13,021	45,989	59,010
Covered loans, gross	207,252	435,388	642,640
Allowance for loan losses	(77)	(4,534)	(4,611)
Covered loans, net of allowance	$ 207,175	$ 430,854	$ 638,029

December 31, 2013	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 28,533	$ 38,410	$ 66,943
Real estate	223,304	564,678	787,982
Construction and land development	25,376	126,068	151,444
Covered loans, gross	277,213	729,156	1,006,369
Allowance for loan losses	(179)	(882)	(1,061)
Covered loans, net of allowance	$ 277,034	$ 728,274	$ 1,005,308

At December 31, 2017, the banking segment had covered loan concentrations (loans to borrowers engaged in similar activities) that exceeded 10% of total covered loans in its real estate portfolio. The areas of concentration within our covered real estate portfolio were non-construction residential real estate loans and non-construction commercial real estate loans, which represented 79.1% and 19.4%, respectively, of the banking segment's total covered loans at December 31, 2017. The banking segment's covered loan concentrations were within regulatory guidelines at December 31, 2017.

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Loan Portfolio Maturities

Banking Segment

The following table provides information regarding the maturities of the banking segment's non-covered and covered commercial and real estate loans held for investment, net of unearned income (in thousands).

	December 31, 2017			
	Due Within One Year	Due From One To Five Years	Due After Five Years	Total
Commercial and industrial	$ 2,714,142	$ 372,710	$ 132,594	$ 3,219,446
Real estate (including construction and land development)	1,087,957	2,269,534	799,467	4,156,958
Total	$ 3,802,099	$ 2,642,244	$ 932,061	$ 7,376,404
Fixed rate loans	$ 2,791,110	$ 2,219,687	$ 801,508	$ 5,812,305
Floating rate loans	1,010,989	422,557	130,553	1,564,099
Total	$ 3,802,099	$ 2,642,244	$ 932,061	$ 7,376,404

In the table above, floating rate loans that have reached their applicable rate floor or ceiling are classified as fixed rate loans rather than floating rate loans. The majority of floating rate loans carry an interest rate tied to The Wall Street Journal Prime Rate, as published in The Wall Street Journal.

Allowance for Loan Losses

The allowance for loan losses is a reserve established through a provision for loan losses charged to expense, which represents management's best estimate of probable losses inherent in our existing non-covered and covered loan portfolios. Management has responsibility for determining the level of the allowance for loan losses, subject to review by the Loan Review Committee of the Bank's board of directors.

It is management's responsibility at the end of each quarter, or more frequently as deemed necessary, to analyze the level of the allowance for loan losses to ensure that it is appropriate for the estimated credit losses in the portfolio. Estimated credit losses are the probable current amount of loans that we will be unable to collect given facts and circumstances as of the evaluation date. When management determines that a loan, or portion thereof, is uncollectible, the loan, or portion thereof, is charged-off against the allowance for loan losses, or for acquired loans accounted for in

pools, charged against the pool discount. Recoveries on charge-offs of loans acquired in the Bank Transactions that occurred prior to their acquisition represent contractual cash flows not expected to be collected and are recorded as accretion income. Recoveries on acquired loans charged-off subsequent to their acquisition are credited to the allowance for loan loss, except for recoveries on loans accounted for in pools, which are credited to the pool discount.

We have developed a methodology that seeks to determine an allowance within the scope of the Receivables and Contingencies Topics of the ASC. Each of the loans that has been determined to be impaired is within the scope of the Receivables Topic. Impaired loans that are equal to or greater than $0.5 million are individually evaluated using one of three impairment measurement methods as of the evaluation date: (1) the present value of expected future discounted cash flows on the loan, (2) the loan's observable market price, or (3) the fair value of the collateral if the loan is collateral dependent. Specific reserves are provided in our estimate of the allowance based on the measurement of impairment under these three methods, except for collateral dependent loans, which require the fair value method. All non-impaired loans are within the scope of the Receivables and Contingencies Topic. Estimates of loss for the Receivables and Contingencies Topic are calculated based on historical loss, adjusted for qualitative or environmental factors. The Bank uses a rolling three year average net loss rate to calculate historical loss factors. The analysis is conducted by call report loan category, and further disaggregates commercial and industrial loans by collateral type. The analysis uses net charge-off experience by considering charge-offs and recoveries in determining the loss rate. The historical loss calculation for the quarter is calculated by dividing the current quarter net charge-offs for each loan category by the quarter ended loan category balance. The Bank utilizes a weighted average loss rate to better represent recent trends.

While historical loss experience provides a reasonable starting point for the analysis, historical losses are not the sole basis upon which we determine the appropriate level for the allowance for loan losses. Management considers recent

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qualitative or environmental factors that are likely to cause estimated credit losses associated with the existing portfolio to differ from historical loss experience, including but not limited to:

- changes in the volume and severity of past due, non-accrual and classified loans;
- changes in the nature, volume and terms of loans in the portfolio;
- changes in lending policies and procedures;
- changes in economic and business conditions and developments that affect the collectability of the portfolio;
- changes in lending management and staff;
- changes in the loan review system and the degree of oversight by the Bank's board of directors; and
- any concentrations of credit and changes in the level of such concentrations.

Changes in the volume and severity of past due, non-accrual and classified loans, as well as changes in the nature, volume and terms of loans in the portfolio are key indicators of changes that could indicate a necessary adjustment to the historical loss factors. The magnitude of the impact of these factors on our qualitative assessment of the allowance for loan loss changes from quarter to quarter.

The loan review program is designed to identify and monitor problem loans by maintaining a credit grading process, requiring that timely and appropriate changes are made to reviewed loans and coordinating the delivery of the information necessary to assess the appropriateness of the allowance for loan losses. Loans are evaluated for impaired status when: (i) payments on the loan are delayed, typically by 90 days or more (unless the loan is both well secured and in the process of collection), (ii) the loan becomes classified, (iii) the loan is being reviewed in the normal course of the loan review scope, or (iv) the loan is identified by the servicing officer as a problem. We review on an individual basis all loan relationships equal to or greater than $0.5 million that exhibit probable or observed credit weaknesses, the top 25 loan relationships by dollar amount in each market we serve, and additional relationships necessary to achieve adequate coverage of our various lending markets.

In connection with the Bank Transactions, we acquired loans both with and without evidence of credit quality deterioration since origination. PCI loans acquired in the PlainsCapital Merger are accounted for on an individual loan basis, while PCI loans acquired in each of the FNB Transaction and the SWS Merger are accounted for in pools as well as on an individual loan basis. We have established under our PCI accounting policy a framework to aggregate certain acquired loans into various loan pools based on a minimum of two layers of similar risk characteristics for the purpose of determining their respective fair values as of their acquisition dates, and for applying the subsequent recognition and measurement provisions for income accretion and impairment testing. The similar risk characteristics used for the pooling of the FNB and SWS PCI loans are risk grade and loan collateral type. The loans acquired in the Bank Transactions were initially recorded at fair value with no carryover of any allowance for loan losses.

An allowance for loan losses on PCI loans is calculated using the quarterly recast of cash flows expected to be collected for each loan or pool. These evaluations require the continued use and updating of key assumptions and estimates such as default rates, loss severity given default and prepayment speed assumptions (similar to those used for the initial fair value estimate). Management judgment must be applied in developing these assumptions. If

expected cash flows for a loan or pool decreases, an increase in the allowance for loan losses is made through a charge to the provision for loan losses. If expected cash flows for a loan or pool increase, any previously established allowance for loan losses is reversed and any remaining difference increases the accretable yield. This increase in accretable yield is taken into income over the remaining life of the loan.

Loans without evidence of credit impairment at acquisition are subsequently evaluated for any required allowance at each reporting date. An allowance for loan losses is calculated using a methodology similar to that described above for originated loans. The allowance as determined for each loan collateral type is compared to the remaining fair value discount for that loan collateral type. If greater, the excess is recognized as an addition to the allowance through a provision for loan losses. If less than the discount, no additional allowance is recorded. Charge-offs and losses first reduce any remaining fair value discount for the loan and once the discount is depleted, losses are applied against the allowance established for that loan.

Provisions for loan losses are charged to operations to record the total allowance for loan losses at a level deemed appropriate by the banking segment's management based on such factors as the volume and type of lending it conducted, the amount of non-performing loans and related collateral security, the present level of the allowance for loan losses, the results of recent regulatory examinations, generally accepted accounting principles, general economic conditions and

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other factors related to the ability to collect loans in its portfolio. The provision for loan losses, primarily in the banking segment, was $14.3 million, $40.6 million and $12.7 million during 2017, 2016 and 2015, respectively. The significant changes in the provision for loan losses during 2017, compared with 2016, and during 2016, compared with 2015, were primarily the result of the previously mentioned $24.5 million charge-off of a single large loan by the Bank during the second quarter of 2016.

The allowance for loan losses is subject to regulatory examination, which may take into account such factors as the methodology used to calculate the allowance and the size of the allowance. While we believe we have an appropriate allowance for our existing non-covered and covered portfolios at December 31, 2017, additional provisions for losses on existing loans may be necessary in the future.

The following tables present the activity in our allowance for loan losses within our non-covered and covered loan portfolios for the periods presented (in thousands). Substantially all of the activity shown below occurred within the banking segment. With respect to the covered portfolio, the year ended December 31, 2013 below refers to the period from September 14, 2013 through December 31, 2013.

	Year Ended December 31,				
Non-Covered Portfolio	2017	2016	2015	2014	2013
Balance, beginning of year	$ 54,186	$ 45,415	$ 37,041	$ 33,241	$ 3,409
Provisions charged to operations	11,406	41,741	12,173	7,747	36,093
Recoveries of non-covered loans previously charged off:					
Commercial and industrial	1,833	1,931	3,558	2,943	3,439
Real estate	225	395	520	218	282
Construction and land development	7	—	—	185	265
Consumer	79	123	127	105	61
Broker-dealer	—	—	123	1	—
Total recoveries	2,144	2,449	4,328	3,452	4,047
Non-covered loans charged off:					
Commercial and industrial	6,253	33,776	7,144	6,926	9,359
Real estate	305	1,439	605	114	209
Construction and land development	13	—	—	—	524
Consumer	208	203	378	359	216
Broker-dealer	—	1	—	—	—
Total charge-offs	6,779	35,419	8,127	7,399	10,308
Net charge-offs	(4,635)	(32,970)	(3,799)	(3,947)	(6,261)
Balance, end of year	$ 60,957	$ 54,186	$ 45,415	$ 37,041	$ 33,241
Non-covered allowance for loan losses as a percentage of gross non-covered loans	0.97 %	0.93 %	0.87 %	0.94 %	0.95 %

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Covered Portfolio	Year Ended December 31, 2017		2016		2015		2014		2013	
Balance, beginning of period	$ 413		$ 1,532		$ 4,611		$ 1,061		$ —	
Provisions charged to (recapture from) operations	2,865		(1,121)		542		9,186		1,065	
Recoveries of covered loans previously charged off:										
Commercial and industrial	6		—		222		—		—	
Real estate	6		17		120		—		—	
Construction and land development	10		104		—		—		—	
Total recoveries	22		121		342		—		—	
Covered loans charged off:										
Commercial and industrial	49		6		915		90		4	
Real estate	522		62		2,869		5,399		—	
Construction and land development	—		51		179		147		—	
Total charge-offs	571		119		3,963		5,636		4	
Net recoveries (charge-offs)	(549)		2		(3,621)		(5,636)		(4)	
Balance, end of period	$ 2,729		$ 413		$ 1,532		$ 4,611		$ 1,061	
Covered allowance for loan losses as a percentage of gross covered loans	1.50	%	0.16	%	0.40	%	0.72	%	0.11	%

The distribution of the allowance for loan losses among loan types and the percentage of the loans for that type to gross loans, excluding unearned income, within our non-covered and covered loan portfolios are presented in the tables below (dollars in thousands).

	December 31, 2017			2016			2015			2014			2013	
ed Portfolio	Reserve	% of Gross Non-Covered Loans		Reserve	% of Gross Non-Covered Loans		Reserve	% of Gross Non-Covered Loans		Reserve	% of Gross Non-Covered Loans		Reserve	% of Gross Non-Covere Loans
ercial and ial	$ 23,674	26.80	%	$ 21,369	29.03	%	$ 19,845	29.82	%	$ 18,833	35.21	%	$ 16,717	38.57
tate ing uction and evelopment)	36,619	63.35	%	32,238	61.67	%	25,047	57.96	%	17,581	53.78	%	16,288	51.84
mer	311	0.64	%	424	0.71	%	314	0.88	%	461	1.36	%	88	1.58
-dealer	353	9.21	%	155	8.59	%	209	11.34	%	166	9.65	%	148	8.01
	$ 60,957	100.00	%	$ 54,186	100.00	%	$ 45,415	100.00	%	$ 37,041	100.00	%	$ 33,241	100.00

	December 31,											
	2017			2016			2015			2014		
Covered Portfolio	Reserve	% of Gross Covered loans		Reserve	% of Gross Covered Loans		Reserve	% of Gross Covered Loans		Reserve	% of Gross Covered Loans	
Commercial and industrial	$ 24	0.58	%	$ 35	1.05	%	$ 758	2.31	%	$ 1,193	4.79	
Real estate (including construction and land development)	2,705	99.42	%	378	98.95	%	774	97.69	%	3,418	95.21	
Total	$ 2,729	100.00	%	$ 413	100.00	%	$ 1,532	100.00	%	$ 4,611	100.00	

Potential Problem Loans

Potential problem loans consist of loans that are performing in accordance with contractual terms but for which management has concerns about the ability of an obligor to continue to comply with repayment terms because of the obligor’s potential operating or financial difficulties. Management monitors these loans and reviews their performance on a regular basis. Potential problem loans contain potential weaknesses that could improve, persist or further deteriorate. If such potential weaknesses persist without improving, the loan is subject to downgrade, typically to substandard, in three to six months. Potential problem loans are assigned a grade of special mention within our risk grading matrix. Potential problem loans do not include PCI loans because PCI loans exhibited evidence of credit deterioration at acquisition that made it probable that all contractually required principal payments would not be collected. Within our non-covered loan portfolio, we had five credit relationships totaling $27.3 million of potential problem loans at December 31, 2017,

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compared with four credit relationships totaling $3.8 million of potential problem loans at December 31, 2016 and two credit relationships totaling $1.6 million of potential problem loans at December 31, 2015. Within our covered loan portfolio, we had one credit relationship totaling $0.4 million of potential problem loans at December 31, 2017, compared with one credit relationship totaling $0.5 million with potential problem loans at December 31, 2016 and December 31, 2015.

Non-Performing Assets

The following table presents components of our non-covered non-performing assets (dollars in thousands).

	December 31,				
	2017	2016	2015	2014	2013
Non-covered loans accounted for on a non-accrual basis:					
Commercial and industrial	$ 20,878	$ 9,515	$ 17,764	$ 16,648	$ 16,730
Real estate	18,978	13,932	7,160	4,707	6,511
Construction and land development	611	755	114	703	112
Consumer	56	244	7	—	—
Broker-dealer	—	—	—	—	—
	$ 40,523	$ 24,446	$ 25,045	$ 22,058	$ 23,353
Non-covered non-performing loans as a percentage of total non-covered loans	0.51 %	0.32 %	0.37 %	0.42 %	0.51 %
Non-covered other real estate owned	$ 3,883	$ 4,507	$ 394	$ 808	$ 4,805
Other repossessed assets	$ 323	$ 1,117	$ —	$ 361	$ 13
Non-covered non-performing assets	$ 44,729	$ 30,070	$ 25,439	$ 23,227	$ 28,171
Non-covered non-performing assets as a percentage of total assets	0.33 %	0.24 %	0.21 %	0.25 %	0.32 %
Non-covered loans past due 90 days or more and still accruing	$ 85,113	$ 47,486	$ 50,776	$ 19,237	$ 7,301
Troubled debt restructurings included in accruing non-covered loans	$ 1,150	$ 1,196	$ 1,418	$ 2,901	$ 1,055

At December 31, 2017, total non-covered non-performing assets increased $14.7 million to $44.7 million, compared with $30.1 million at December 31, 2016. Total non-covered non-performing assets increased $4.7 million to $30.1

million, compared with $25.4 million at December 31, 2015. Non-covered non-performing loans totaled $40.5 million, $24.4 million and $25.0 million at December 31, 2017, 2016 and 2015, respectively. At December 31, 2017, non-covered non-accrual loans included 19 commercial and industrial relationships with loans of $20.9 million secured by accounts receivable, life insurance, oil and gas, livestock, and equipment. Non-covered non-accrual loans at December 31, 2017 also included $19.0 million characterized as real estate loans, including eight commercial real estate loan relationships totaling $14.6 million and $4.4 million in loans secured by residential real estate, $2.7 million of which were classified as loans held for sale, as well as construction and land development loans of $0.6 million. At December 31, 2016, non-covered non-accrual loans included 19 commercial and industrial relationships with loans of $9.5 million secured by accounts receivable, life insurance, livestock, oil and gas, and equipment. Non-covered non-accrual loans at December 31, 2016 also included $13.9 million characterized as real estate loans, including five commercial real estate loan relationships of $11.0 million and loans secured by residential real estate of $2.9 million, $1.7 million of which were classified as loans held for sale, as well as construction and land development loans of $0.8 million. The $16.1 million increase in non-covered non-accrual loans from December 31, 2016 to December 31, 2017 was primarily due to $15.4 million in loans at the Bank (two commercial and industrial relationships and one real estate relationship) being moved to non-accrual during 2017. At December 31, 2015, non-covered non-accrual loans included 20 commercial and industrial relationships with loans of $17.4 million secured by accounts receivable, inventory, life insurance, livestock, ad oil and gas, and a total of $0.3 million in lease financing receivables. Non-covered non-accrual loans at December 31, 2015 also included $7.2 million characterized as real estate loans, including four commercial real estate loan relationships of $4.6

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million and loans secured by residential real estate of $2.6 million, $1.6 million of which were classified as loans held for sale, as well as construction and land development loans of $0.1 million.

Non-covered OREO decreased $0.6 million to $3.9 million at December 31, 2017, compared with $4.5 million at December 31, 2016. Changes in non-covered OREO included the addition of six properties totaling $2.2 million, the disposal of eight properties totaling $2.0 million and downward valuation adjustments of $0.8 million. At December 31, 2017, non-covered OREO included commercial properties of $3.6 million and other real estate properties of $0.3 million. At December 31, 2016, non-covered OREO included commercial properties of $4.2 million and other real estate properties of $0.3 million.

Non-covered non-PCI loans past due 90 days or more and still accruing were $85.1 million, $47.5 million and $50.8 million at December 31, 2017, 2016 and 2015, respectively, substantially all of which were loans held for sale and guaranteed by U.S. Government agencies, including loans that are subject to repurchase, or have been repurchased, by PrimeLending. The increase in non-covered loans past due 90 days or more and still accruing from December 31, 2016 to December 31, 2017 was primarily due to an increase in Government National Mortgage Association related loans subject to repurchase within our mortgage origination segment. This increase in loans subject to repurchase was partially due to increased delinquencies resulting from the granting of forbearance by loan servicers to provide flexibility to borrowers impacted by natural disasters during 2017.

At December 31, 2017, troubled debt restructurings ("TDRs") on non-covered loans totaled $10.7 million. These TDRs were comprised of $1.2 million of non-covered loans that were considered to be performing and non-covered non-performing loans of $9.6 million reported in non-accrual loans. At December 31, 2016, TDRs on non-covered loans totaled $6.4 million, consisting of $1.2 million related to non-covered loans that were considered to be performing and non-covered non-performing loans of $5.2 million reported in non-accrual loans. At December 31, 2015, TDRs on non-covered loans totaled $9.3 million, consisting of $1.4 million related to non-covered loans that were considered to be performing and non-covered non-performing loans of $7.9 million reported in non-accrual loans.

The following table presents components of our covered non-performing assets (dollars in thousands).

	December 31,				
	2017	2016	2015	2014	2013
Covered loans accounted for on a non-accrual basis:					
Commercial and industrial	$ —	$ 52	$ 68	$ 1,325	$ 973
Real estate	5,087	3,765	2,958	31,869	249
Construction and land development	17	19	5,952	1,029	575
	$ 5,104	$ 3,836	$ 8,978	$ 34,223	$ 1,797

Covered non-performing loans as a percentage of total covered loans	2.80 %	1.50 %	2.36 %	5.33 %	0.18 %
Covered other real estate owned:					
Real estate - residential	$ 2,433	$ 7,396	$ 17,718	$ 15,711	$ 11,634
Real estate - commercial	6,933	9,558	33,425	40,889	51,897
Construction and land development - residential	4,667	7,926	9,190	21,719	36,866
Construction and land development - commercial	22,711	26,762	38,757	58,626	42,436
	$ 36,744	$ 51,642	$ 99,090	$ 136,945	$ 142,833
Other repossessed assets	$ —	$ —	$ —	$ —	$ —
Covered non-performing assets	$ 41,848	$ 55,478	$ 108,068	$ 171,168	$ 144,630
Covered non-performing assets as a percentage of total assets	0.31 %	0.44 %	0.91 %	1.85 %	1.62 %
Covered loans past due 90 days or more and still accruing	$ 283	$ 173	$ —	$ 67	$ —
Troubled debt restructurings included in accruing covered loans	$ 283	$ 503	$ 515	$ 326	$ —

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At December 31, 2017, covered non-performing assets decreased by $13.6 million to $41.8 million, compared with $55.5 million at December 31, 2016, due to a decrease in covered other real estate owned of $14.9 million, partially offset by an increase in covered non-accrual loans of $1.3 million. At December 31, 2016, covered non-performing assets decreased by $52.6 million to $55.5 million, compared with $108.1 million at December 31, 2015, due to decreases in covered non-accrual loans of $5.1 million and covered other real estate owned of $47.4 million. Covered non-performing loans totaled $5.1 million, $3.8 million and $9.0 million at December 31, 2017, 2016 and 2015, respectively. At December 31, 2017, covered non-performing loans included 53 residential real estate loan relationships of $5.1 million. At December 31, 2016, covered non-performing loans included one commercial and industrial relationship with loans of $0.1 million, three commercial real estate loan relationships of $0.7 million and 31 residential real estate loan relationships of $3.0 million. At December 31, 2015, covered non-performing loans included four commercial and industrial relationships with loans of $0.1 million secured by accounts receivable and inventory, two commercial real estate loan relationships of $0.4 million, 25 residential real estate loan relationships of $2.5 million, as well as construction and land development loans of $6.0 million.

OREO acquired in the FNB Transaction that is subject to the FDIC loss-share agreements is referred to as “covered OREO” and reported separately in our consolidated balance sheets. Covered OREO decreased $14.9 million to $36.7 million at December 31, 2017, compared with $51.6 million at December 31, 2016. The decrease was primarily due to the disposal of 163 properties totaling $17.7 million and fair value valuation decreases of $3.7 million, partially offset by the addition of 48 properties totaling $6.5 million. Covered OREO decreased $47.5 million to $51.6 million at December 31, 2016, compared with $99.1 million at December 31, 2015. The decrease was primarily due to the disposal of 212 properties totaling $42.9 million and fair value valuation decreases of $18.5 million, partially offset by the addition of 124 properties totaling $13.9 million.

Covered non-PCI loans past due 90 days or more and still accruing totaled $0.3 million at December 31, 2017 and included four residential real estate loans. Covered non-PCI loans past due 90 days or more and still accruing totaled $0.2 million at December 31, 2016 and included one residential real estate loan and one commercial and industrial loan. There were no covered non-PCI loans past due 90 days or more and still accruing at December 31, 2015.

At December 31, 2017, 2016 and 2015, TDRs on covered loans totaled $1.2 million, $1.4 million, and $1.5 million, respectively. At December 31, 2017, TDRs on covered loans consisted of $0.3 million related to covered loans that were considered to be performing and covered non-performing loans of $0.9 million included in non-accrual loans. At December 31, 2016, TDRs on covered loans consisted of $0.5 million related to covered loans that were considered to be performing and covered non-performing loans of $0.9 million included in non-accrual loans. At December 31, 2015, TDRs on covered loans consisted of $0.5 million related to covered loans that were considered to be performing and covered non-performing loans of $1.0 million included in non-accrual loans.

Insurance Losses and Loss Adjustment Expenses

At December 31, 2017, 2016 and 2015, our gross reserve for unpaid losses and LAE was $30.2 million, $35.8 million, and $44.4 million, respectively, including estimated recoveries from reinsurance of $11.5 million, $9.4 million, and $13.5 million, respectively. The liability for insurance losses and LAE represents estimates of the ultimate unpaid cost of all losses incurred, including losses for claims that have not yet been reported, less a reduction for reinsurance recoverables related to those liabilities. Separately for each of NLIC and ASIC and each line of business, our actuaries estimate the liability for unpaid losses and LAE by first estimating ultimate losses and LAE amounts for each year, prior to recognizing the impact of reinsurance. The amount of liabilities for reported claims is based primarily on a claim-by-claim evaluation of coverage, liability, injury severity or scope of property damage, and any other information considered relevant to estimating exposure presented by the claim.

The methods that our actuaries utilize to estimate ultimate loss and LAE amounts are the paid and reported loss development method and the paid and reported Bornhuetter-Ferguson method (the “BF method”). Significant periods of time can elapse between the occurrence of an insured loss, the reporting of the loss to the insurer and the insurer’s payment of that loss. NLC’s liabilities for unpaid losses represent the best estimate at a given point in time of what it expects to pay claimants, based on facts, circumstances and historical trends then known. During the loss settlement period, additional facts regarding individual claims may become known and, consequently, it often becomes necessary to refine and adjust the estimates of liability. This process is commonly referred to as loss development. To project ultimate losses and LAE, our actuaries examine the paid and reported losses and LAE for each accident year and multiply these values by a loss development factor. The selected loss development factors are based upon a review of the loss development patterns indicated in the companies’ historical loss triangles (which utilize historical trends, adjusted for

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changes in loss costs, underwriting standards, policy provisions, product mix and other factors) and applicable insurance industry loss development factors. Estimating the liability for unpaid losses and LAE is inherently judgmental and is influenced by factors that are subject to significant variation. Liabilities for LAE are intended to cover the ultimate cost of settling claims, including investigation and defense of lawsuits resulting from such claims.

The BF method is a procedure that weights an expected ultimate loss and LAE amount, and the result of the loss development method. This method is useful when loss data is immature or sparse because it is not as sensitive as the loss development method to unusual variations in the paid or reported amounts. The BF method requires an initial estimate of expected ultimate losses and LAE. For each year, the expected ultimate losses and LAE is based on a review of the ultimate loss ratios indicated in the companies' historical data and applicable insurance industry ultimate loss ratios. Each loss development factor, paid or reported, implies a certain percent of the ultimate losses and LAE is still unpaid or unreported. The amounts of unpaid or unreported losses and LAE by year are estimated as the percentage unpaid or unreported, times the expected ultimate loss and LAE amounts. To project ultimate losses and LAE, the actual paid or reported losses and LAE to date are added to the estimated unpaid or unreported amounts. The results of each actuarial method performed by year are reviewed to select an ultimate loss and LAE amount for each accident year. In general, more weight is given to the loss development projections for more mature accident periods and more weight is given to the BF methods for less mature accident periods.

The reserve analysis performed by our actuaries provides preliminary central estimates of the unpaid losses and LAE. At each quarter-end, the results of the reserve analysis are summarized and discussed with our senior management. The senior management group considers many factors in determining the amount of reserves to record for financial statement purposes. These factors include the extent and timing of any recent catastrophic events, historical pattern and volatility of the actuarial indications, the sensitivity of the actuarial indications to changes in paid and reported loss patterns, the consistency of claims handling processes, the consistency of case reserving practices, changes in our pricing and underwriting, and overall pricing and underwriting trends in the insurance market. We would consider reasonably likely changes in the key assumptions to have an impact on our best estimate by plus or minus 10%. At December 31, 2017, this equates to approximately plus or minus $1.9 million, or 1.6% of insurance segment equity, and 2.0% of calendar year 2017 insurance losses.

Deposits

The banking segment's major source of funds and liquidity is its deposit base. Deposits provide funding for its investments in loans and securities. Interest paid for deposits must be managed carefully to control the level of interest expense and overall net interest margin. The composition of the deposit base (time deposits versus interest-bearing demand deposits and savings), as discussed in more detail within the section entitled "Liquidity and Capital Resources — Banking Segment" below, is constantly changing due to the banking segment's needs and market conditions. Average deposits totaled $7.5 billion during 2017 and were higher than average deposits of $7.1 billion during 2016 and $7.0 billion during 2015. For the periods presented in the table below, the average rates paid associated with time deposits include the effects of amortization of the deposit premiums booked as a part of the Bank Transactions.

The table below presents the average balance of, and rate paid on, consolidated deposits (dollars in thousands).

	Year Ended December 31,					
	2017		2016		2015	
	Average Balance	Average Rate Paid	Average Balance	Average Rate Paid	Average Balance	Average Rate Paid
Noninterest-bearing demand deposits	$ 2,309,776	0.00 %	$ 2,241,561	0.00 %	$ 2,187,336	0.00 %
Interest-bearing demand deposits	3,671,521	0.29 %	3,185,006	0.14 %	3,011,647	0.13 %
Savings deposits	234,420	0.10 %	301,877	0.15 %	297,857	0.15 %
Time deposits	1,314,418	1.05 %	1,337,491	0.81 %	1,494,573	0.74 %
	$ 7,530,135	0.33 %	$ 7,065,935	0.22 %	$ 6,991,413	0.22 %

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The maturity of consolidated interest-bearing time deposits of $100,000 or more at December 31, 2017 is set forth in the table below (in thousands).

Months to maturity:	
3 months or less	$ 200,474
3 months to 6 months	178,623
6 months to 12 months	212,491
Over 12 months	498,772
	$ 1,090,360

The banking segment experienced an increase of $192.6 million in interest-bearing time deposits of $100,000 or more at December 31, 2017, compared to December 31, 2016. This is compared to an increase of $125.8 million in interest-bearing time deposits of $100,000 or more at December 31, 2016, compared to December 31, 2015. The increases during both periods were primarily due to our strategic decision to offer more aggressive time deposit rate options. At December 31, 2017, there were $791.7 million in interest-bearing time deposits scheduled to mature within one year.

Borrowings

Our borrowings are shown in the table below (dollars in thousands).

	December 31, 2017		2016		2015	
	Balance	Average Rate Paid	Balance	Average Rate Paid	Balance	Average Rate Paid
Short-term borrowings	$ 1,206,424	1.20 %	$ 1,417,289	0.65 %	$ 947,373	0.56 %
Notes payable	208,809	3.65 %	317,912	3.89 %	238,716	3.93 %
Junior subordinated debentures	67,012	4.50 %	67,012	3.99 %	67,012	3.58 %
	$ 1,482,245	1.84 %	$ 1,802,213	1.57 %	$ 1,253,101	1.38 %

Short-term borrowings consisted of federal funds purchased, securities sold under agreements to repurchase, borrowings at the Federal Home Loan Bank ("FHLB") and short-term bank loans. The $210.9 million decrease in short-term borrowings at December 31, 2017 compared with December 31, 2016 included a net decrease of $735.4 million in our banking segment primarily associated with a decrease in FHLB notes, partially offset by an increase of

$549.6 million in short-term bank loans and securities sold under agreements to repurchase used by the Hilltop Broker-Dealers to finance their activities. The $469.9 million increase in short-term borrowings at December 31, 2016 compared with December 31, 2015 included an increase in borrowings of $428.2 million in our banking segment primarily associated with an increase in borrowings under the mortgage origination segment's warehouse line of credit with the Bank and a net increase of $34.5 million in short-term bank loans and securities sold under agreements to repurchase used by the Hilltop Broker-Dealers to finance their activities. Notes payable at December 31, 2017 of $208.8 million was comprised of $148.4 million related to Senior Notes, net of loan origination fees, FHLB borrowings with an original maturity greater than one within our banking segment of $19.4 million, insurance segment term notes of $28.5 million, and mortgage origination segment borrowings of $12.5 million. Notes payable at December 31, 2016 of $317.9 million was comprised of $148.3 million related to Senior Notes, net of loan origination fees, associated with our debt offering in April 2015, FHLB borrowings with an original maturity greater than one year held by the former SWS FSB within the banking segment of $102.6 million, insurance segment term notes of $50.5 million, and mortgage origination segment borrowings of $16.5 million. The decrease in notes payable at December 31, 2017 compared to December 31, 2016 included the payoff by NLC of its $20.0 million insurance company note payable due March 2035. Notes payable at December 31, 2015 of $238.7 million was comprised of $148.2 million related to Senior Notes, net of loan origination fees, insurance segment term notes of $54.5 million, and FHLB borrowings with an original maturity greater than one year held by the former SWS FSB within the banking segment of $36.0 million. The average rate paid associated with notes payable includes the effect of amortization of the premiums on FHLB borrowings booked as a part of the SWS Merger.

Liquidity and Capital Resources

Hilltop is a financial holding company whose assets primarily consist of the stock of its subsidiaries and invested assets. Hilltop's primary investment objectives, as a holding company, are to support capital deployment for organic growth and to preserve capital to be deployed through acquisitions. At December 31, 2017, Hilltop had $96.8 million in freely available cash and cash equivalents, a decrease of $7.1 million from $103.9 million at December 31, 2016. This decrease

in available cash was primarily due to the net effects of Hilltop's payment of $55.0 million related to the resolution of the SWS appraisal proceeding, $27.4 million associated with our stock repurchase program, $23.1 million in cash dividends declared and paid, a $10.0 million capital contribution to PCE and other general corporate expenses, partially offset by Hilltop's receipt of $94.5 million in dividends from its subsidiaries and receipt of $20.6 million from PCC due to organizational changes. If necessary or appropriate, we may also finance acquisitions with the proceeds from equity or debt issuances. Subject to regulatory restrictions, Hilltop has received, and may also continue to receive, dividends from its subsidiaries. We believe that Hilltop's liquidity is sufficient for the foreseeable future, with current short-term liquidity needs including operating expenses, interest on debt obligations, dividend payments to stockholders and potential stock repurchases.

Dividend Program and Declaration

In October 2016, we announced that our board of directors authorized a dividend program under which we intend pay quarterly dividends on our common stock, subject to quarterly declarations by our board of directors. During 2017, we declared and paid cash dividends of $0.24 per common share, or $23.1 million.

On January 25, 2018, our board of directors declared a quarterly cash dividend of $0.07 per common share, payable on February 28, 2018 to all common stockholders of record as of the close of business on February 15, 2018.

Future dividends on our common stock are subject to the determination by the board of directors based on an evaluation of our earnings and financial condition, liquidity and capital resources, the general economic and regulatory climate, our ability to service any equity or debt obligations senior to our common stock and other factors.

Pending Acquisition

On February 13, 2018, we entered into a definitive agreement to acquire privately-held, Houston-based The Bank of River Oaks ("BORO") in an all-cash transaction. Under the terms of the definitive agreement, we have agreed to pay cash in the aggregate amount of $85 million to the shareholders and option holders of BORO. As of December 31, 2017, BORO had unaudited total assets, gross loans and deposits of approximately $454 million, $344 million and $406 million, respectively. The transaction is subject to customary closing conditions, including regulatory approvals and approval by shareholders of BORO, and is expected to close during the third quarter of 2018.

Senior Notes due 2025

On April 9, 2015, we completed an offering of $150.0 million aggregate principal amount of our 5% senior notes due 2025 ("Senior Unregistered Notes") in a private offering that was exempt from the registration requirements of the Securities Act. The Senior Unregistered Notes were offered within the United States only to qualified institutional buyers pursuant to Rule 144A under the Securities Act, and to persons outside of the United States under Regulation S under the Securities Act. The Senior Unregistered Notes were issued pursuant to an indenture, dated as of April 9, 2015 (the "indenture"), by and between Hilltop and U.S. Bank National Association, as trustee. The net proceeds from the offering, after deducting estimated fees and expenses and the initial purchasers' discounts, were approximately $148 million. We used the net proceeds of the offering to redeem all of our outstanding Series B Preferred Stock at an aggregate liquidation value of $114.1 million, plus accrued but unpaid dividends of $0.4 million, and Hilltop utilized the remainder for general corporate purposes.

In connection with the issuance of the Senior Unregistered Notes, on April 9, 2015, we entered into a registration rights agreement with the initial purchasers of the Senior Unregistered Notes. Under the terms of the registration rights agreement, we agreed to offer to exchange the Senior Unregistered Notes for notes registered under the Securities Act (the "Senior Registered Notes"). The terms of the Senior Registered Notes are substantially identical to the Senior Unregistered Notes for which they were exchanged (including principal amount, interest rate, maturity and redemption rights), except that the Senior Registered Notes generally are not subject to transfer restrictions. On May 22, 2015, and subject to the terms and conditions set forth in the Senior Registered Notes prospectus, we commenced an offer to exchange the outstanding Senior Unregistered Notes for Senior Registered Notes. Substantially all of the Senior Unregistered Notes were tendered for exchange, and on June 22, 2015, we fulfilled all of the requirements of the registration rights agreement for the Senior Unregistered Notes by issuing Senior Registered Notes in exchange for the tendered Senior Unregistered Notes. We refer to the Senior Registered Notes and the Senior Unregistered Notes that remain outstanding collectively as the "Senior Notes."

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The Senior Notes bear interest at a rate of 5% per year, payable semi-annually in arrears in cash on April 15 and October 15 of each year, commencing on October 15, 2015. The Senior Notes will mature on April 15, 2025, unless we redeem the Senior Notes, in whole at any time or in part from time to time, on or after January 15, 2025 (three months prior to the maturity date of the Senior Notes) at our election at a redemption price equal to 100% of the principal amount of the Senior Notes to be redeemed plus accrued and unpaid interest to, but excluding, the redemption date. At December 31, 2017, $150.0 million of our Senior Notes was outstanding.

The indenture contains covenants that limit our ability to, among other things and subject to certain significant exceptions: (i) dispose of or issue voting stock of certain of our bank subsidiaries or subsidiaries that own voting stock of our bank subsidiaries, (ii) incur or permit to exist any mortgage, pledge, encumbrance or lien or charge on the capital stock of certain of our bank subsidiaries or subsidiaries that own capital stock of our bank subsidiaries and (iii) sell all or substantially all of our assets or merge or consolidate with or into other companies. The indenture also provides for certain events of default, which, if any of them occurs, would permit or require the principal amount, premium, if any, and accrued and unpaid interest on the then outstanding Senior Notes to be declared immediately due and payable.

Stock Repurchase Program

In January 2017, our board of directors reauthorized the stock repurchase program originally approved during the second quarter of 2016 through January 2018. In January 2018, our board of directors authorized a stock repurchase program through January 2019. Pursuant to the stock repurchase program, we are authorized to repurchase, in the aggregate, up to $50.0 million of our outstanding common stock. Under the stock repurchase program authorized, we may repurchase shares in open-market purchases or through privately negotiated transactions as permitted under Rule 10b-18 promulgated under the Exchange Act. The extent to which we repurchase our shares and the timing of such repurchases depends upon market conditions and other corporate considerations, as determined by Hilltop's management team. Repurchased shares will be returned to our pool of authorized but unissued shares of common stock. During 2017, the Company paid $27.4 million to repurchase an aggregate of 1,057,656 shares of common stock at an average price of $25.87 per share. The purchases were funded from available cash balances.

Loss-Share Agreements

In connection with the FNB Transaction, the Bank entered into two loss-share agreements with the FDIC that collectively cover $1.2 billion of loans and OREO acquired in the FNB Transaction, which we refer to as "covered assets". Pursuant to the loss-share agreements, the FDIC has agreed to reimburse the Bank the following amounts with respect to the covered assets: (i) 80% of net losses on the first $240.4 million of net losses incurred; (ii) 0% of net losses in excess of $240.4 million up to and including $365.7 million of net losses incurred; and (iii) 80% of net losses in excess of $365.7 million of net losses incurred. Net losses are defined as book value losses plus certain defined expenses incurred in the resolution of assets, less subsequent recoveries. Under the loss-share agreement for commercial assets, the amount of subsequent recoveries that are reimbursable to the FDIC for a particular asset is

limited to book value losses and expenses actually billed plus any book value charge-offs incurred prior to the Bank Closing Date. There is no limit on the amount of subsequent recoveries reimbursable to the FDIC under the loss-share agreement for single family assets. The loss-share agreements for commercial and single family residential loans are in effect for five years and ten years, respectively, from the Bank Closing Date and the loss recovery provisions to the FDIC are in effect for eight years and ten years, respectively, from the Bank Closing Date. In accordance with the loss-share agreements, the Bank may be required to make a “true-up” payment to the FDIC approximately ten years following the Bank Closing Date if our actual net realized losses over the life of the loss-share agreements are less than the FDIC’s initial estimate of losses on covered assets. The “true-up” payment is calculated using a defined formula set forth in the P&A Agreement. While the ultimate amount of any “true-up” payment is unknown at this time and will vary based upon the amount of future losses or recoveries within our covered loan portfolio, the Bank has recorded a related “true-up” payment accrual of $16.3 million at December 31, 2017 based on the current estimate of aggregate realized losses on covered assets over the life of the loss-share agreements.

Regulatory Capital

We are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements may prompt certain actions by regulators that, if undertaken, could have a direct material adverse effect on our financial condition and results of operations. Under capital adequacy and regulatory requirements, we must meet specific capital guidelines that involve quantitative measures of our assets, liabilities, and certain off-

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balance sheet items as calculated under regulatory accounting practices. Our capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

In January 2015, the comprehensive capital framework ("Basel III") for U.S. banking organizations became effective for PlainsCapital and Hilltop for reporting periods beginning after January 1, 2015 (subject to a phase-in period through January 2019). Under Basel III, total capital consists of two tiers of capital, Tier 1 and Tier 2. Tier 1 capital is further composed of common equity Tier 1 capital and additional Tier 1 capital. Total capital is the sum of Tier 1 capital and Tier 2 capital. We perform reviews of the classification and calculation of risk-weighted assets to ensure accuracy and compliance with the Basel III regulatory capital requirements. Our capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

In order to avoid limitations on capital distributions, including dividend payments, stock repurchases and certain discretionary bonus payments to executive officers, Basel III also implemented a capital conservation buffer, which requires a banking organization to hold a buffer above its minimum risk-based capital requirements. This buffer helps to ensure that banking organizations conserve capital when it is most needed, allowing them to better weather periods of economic stress. The buffer is measured relative to risk-weighted assets. The phase-in of the capital conservation buffer requirements began on January 1, 2016 for Hilltop and PlainsCapital. Based on the actual ratios as noted below, Hilltop and PlainsCapital exceed each of the capital conservation buffer requirements in effect as of December 31, 2017, as well as the fully phased-in requirements through 2019.

In addition, under the final rules, bank holding companies with less than $15 billion in assets as of December 31, 2009 are allowed to continue to include junior subordinated debentures in Tier 1 capital, subject to certain restrictions. However, if an institution grows to above $15 billion in assets as a result of an acquisition, or organically grows to above $15 billion in assets and then makes an acquisition, the combined trust preferred issuances must be phased out of Tier 1 and into Tier 2 capital. All of the debentures issued to the PCC Statutory Trusts I, II, III and IV (the "Trusts"), less the common stock of the Trusts, qualified as Tier 1 capital as of December 31, 2017, under guidance issued by the Board of Governors of the Federal Reserve System.

At December 31, 2017, Hilltop had a total capital to risk weighted assets ratio of 18.78%, Tier 1 capital to risk weighted assets ratio of 18.24%, common equity Tier 1 capital to risk weighted assets ratio of 17.71% and a Tier 1 capital to average assets, or leverage, ratio of 12.94%. Accordingly, Hilltop's actual capital amounts and ratios in accordance with Basel III exceeded the regulatory capital requirements including conservation buffer in effect at the end of the period and on a fully phased-in basis as if such requirements were currently in effect.

At December 31, 2017, PlainsCapital had a total capital to risk weighted assets ratio of 15.29%, Tier 1 capital to risk weighted assets ratio of 14.47%, common equity Tier 1 capital to risk weighted assets ratio of 14.47%, and a Tier 1 capital to average assets, or leverage, ratio of 12.32%. Accordingly, PlainsCapital's actual capital amounts and ratios in accordance with Basel III resulted in it being considered "well-capitalized" and exceeded the regulatory capital requirements including conservation buffer in effect at the end of the period and on a fully phased-in basis as if such

requirements were currently in effect.

We discuss regulatory capital requirements in more detail in Note 21 to our consolidated financial statements, as well as under the caption “Government Supervision and Regulation — Corporate — Capital Adequacy Requirements and BASEL III” set forth in Part I, Item I. of our Annual Report on Form 10-K.

Banking Segment

Within our banking segment, our primary uses of cash are for customer withdrawals and extensions of credit as well as our borrowing costs and other operating expenses. Our asset and liability group is responsible for continuously monitoring our liquidity position to ensure that our assets and liabilities are managed in a manner that will meet our short-term and long-term cash requirements. Our goal is to manage our liquidity position in a manner such that we can meet our customers’ short-term and long-term deposit withdrawals and anticipated and unanticipated increases in loan demand without penalizing earnings. Funds invested in short-term marketable instruments, the continuous maturing of other interest-earning assets, cash flows from self-liquidating investments such as mortgage-backed securities and collateralized mortgage obligations, the possible sale of available for sale securities, and the ability to securitize certain types of loans provide sources of liquidity from an asset perspective. The liability base provides sources of liquidity through deposits and the maturity structure of short-term borrowed funds. For short-term liquidity needs, we utilize federal fund lines of

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credit with correspondent banks, securities sold under agreements to repurchase, borrowings from the Federal Reserve and borrowings under lines of credit with other financial institutions. For intermediate liquidity needs, we utilize advances from the FHLB. To supply liquidity over the longer term, we have access to brokered time deposits, term loans at the FHLB and borrowings under lines of credit with other financial institutions.

We had deposits of $8.0 billion at December 31, 2017, an increase of $914.3 million from $7.1 billion at December 31, 2016. Deposit flows are affected by the level of market interest rates, the interest rates and products offered by competitors, the volatility of equity markets and other factors. The Bank regularly evaluates its deposit products and pricing structures relative to the market to maintain competitiveness over time. At December 31, 2017, money market deposits, including brokered deposits, were $2.3 billion; time deposits, including brokered deposits, were $1.4 billion; and noninterest bearing demand deposits were $2.4 billion. Money market deposits, including brokered deposits, increased by $572.7 million from $1.8 billion and time deposits, including brokered deposits, increased $213.5 million from $1.2 billion at December 31, 2016.

The Bank's 15 largest depositors, excluding Hilltop and Hilltop Securities, collectively accounted for 8.47% of the Bank's total deposits, and the Bank's five largest depositors, excluding Hilltop and Hilltop Securities, collectively accounted for 4.45% of the Bank's total deposits at December 31, 2017. The loss of one or more of our largest Bank customers, or a significant decline in our deposit balances due to ordinary course fluctuations related to these customers' businesses, could adversely affect our liquidity and might require us to raise deposit rates to attract new deposits, purchase federal funds or borrow funds on a short-term basis to replace such deposits.

Broker-Dealer Segment

The Hilltop Broker-Dealers rely on their equity capital, short-term bank borrowings, interest-bearing and non-interest-bearing client credit balances, correspondent deposits, securities lending arrangements, repurchase agreement financings and other payables to finance their assets and operations, subject to their respective compliance with broker-dealer net capital and customer protection rules. At December 31, 2017, Hilltop Securities had credit arrangements with five unaffiliated banks of up to $725.0 million. These credit arrangements are used to finance securities owned, securities held for correspondent accounts, receivables in customer margin accounts and underwriting activities. These credit arrangements are provided on an "as offered" basis and are not committed lines of credit. In addition, Hilltop Securities has a committed revolving credit facility with an unaffiliated bank of up to $50.0 million. At December 31, 2017, Hilltop Securities had borrowed $315.5 million under its credit arrangements and had no borrowings under its credit facility.

Mortgage Origination Segment

PrimeLending funds the mortgage loans it originates through a warehouse line of credit maintained with the Bank. At December 31, 2017, PrimeLending had outstanding borrowings of $1.5 billion against the warehouse line of credit. Effective April 1, 2017, this warehouse line of credit was increased to $2.2 billion to address seasonal fluctuations in loan origination volumes. PrimeLending sells substantially all mortgage loans it originates to various investors in the secondary market, the majority with servicing released. As these mortgage loans are sold in the secondary market, PrimeLending pays down its warehouse line of credit with the Bank. In addition, PrimeLending has an available line of credit with an unaffiliated bank of up to $1.0 million, of which no borrowings were outstanding at December 31, 2017.

PrimeLending owns a 100% membership interest in PrimeLending Ventures Management, LLC ("Ventures Management") which holds an ownership interest in and is the managing member of certain ABAs. At December 31, 2017, these ABAs have combined available lines of credit totaling $70.0 million, $30.0 million of which was with a single unaffiliated bank, while $40.0 million was with the Bank. At December 31, 2017, Ventures Management had outstanding borrowings of $12.5 million with a single unaffiliated bank.

Insurance Segment

Our insurance operating subsidiary's primary investment objectives are to preserve capital and manage for a total rate of return. NLC's strategy is to purchase securities in sectors that represent the most attractive relative value. Bonds, cash and short-term investments of $176.9 million, or 86.8%, equity investments of $21.2 million and other investments of $5.8 million comprised NLC's $203.9 million in total cash and investments at December 31, 2017. NLC does not currently have any significant concentration in both direct and indirect guarantor exposure or any investments in subprime mortgages. NLC has custodial agreements with an unaffiliated bank and an investment management agreement with DTF Holdings, LLC.

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Contractual Obligations

The following table presents information regarding our contractual obligations at December 31, 2017 (in thousands). Our reserve for losses and LAE does not have a contractual maturity date. However, based on historical payment patterns, the amounts presented are management's estimate of the expected timing of these payments. The timing of payments is subject to significant uncertainty. NLC maintains a portfolio of investments with varying maturities to provide adequate cash flows for such payments. Payments related to leases are based on actual payments specified in the underlying contracts. Payments related to short-term borrowings and long-term debt obligations include the estimated contractual interest payments under the respective agreements.

	Payments Due by Period				
	1 year or Less	More than 1 Year but Less than 3 Years	3 Years or More but Less than 5 Years	5 Years or More	Total
Reserve for losses and LAE	$ 18,702	$ 9,064	$ 2,055	$ 392	$ 30,213
Short-term borrowings	1,224,567	—	—	—	1,224,567
Long-term debt obligations	38,591	28,145	25,240	327,040	419,016
Capital lease obligations	1,444	3,019	2,578	4,125	11,166
Operating lease obligations	36,602	54,588	30,735	31,422	153,347
FDIC loss-share obligation (1)	—	—	—	16,325	16,325
Total	$ 1,319,906	$ 94,816	$ 60,608	$ 379,304	$ 1,854,634

(1) In accordance with the loss-share agreements, the Bank may be required to make a "true-up" payment to the FDIC approximately ten years following the Bank Closing Date if our actual net realized losses over the life of the loss-share agreements are less than the FDIC's initial estimate of losses on covered assets. The "true-up" payment is calculated using a defined formula set forth in the P&A Agreement. While the ultimate amount of any "true-up" payment is unknown at this time and will vary based upon the amount of future losses or recoveries within our covered loan portfolio, the Bank has recorded the noted "true-up" payment accrual at December 31, 2017 based on the current estimate of aggregate realized losses on covered assets over the life of the loss-share agreements.

Impact of Inflation and Changing Prices

Our consolidated financial statements included herein have been prepared in accordance with GAAP, which presently require us to measure financial position and operating results primarily in terms of historic dollars. Changes in the

relative value of money due to inflation or recession are generally not considered. The primary effect of inflation on our operations is reflected in increased operating costs. In management's opinion, changes in interest rates affect the financial condition of a financial institution to a far greater degree than changes in the inflation rate. While interest rates are greatly influenced by changes in the inflation rate, they do not necessarily change at the same rate or in the same magnitude as the inflation rate. Interest rates are highly sensitive to many factors that are beyond our control, including changes in the expected rate of inflation, the influence of general and local economic conditions and the monetary and fiscal policies of the U.S. government, its agencies and various other governmental regulatory authorities.

Off-Balance Sheet Arrangements; Commitments; Guarantees

In the normal course of business, we enter into various transactions, which, in accordance with GAAP, are not included in our consolidated balance sheets. We enter into these transactions to meet the financing needs of our customers. These transactions include commitments to extend credit and standby 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.

We enter into contractual loan commitments to extend credit, normally with fixed expiration dates or termination clauses, at specified rates and for specific purposes. Substantially all of our commitments to extend credit are contingent upon customers maintaining specific credit standards until the time of loan funding. We minimize our exposure to loss under these commitments by subjecting them to credit approval and monitoring procedures. We assess the credit risk associated with certain commitments to extend credit and have recorded a liability related to such credit risk in our consolidated financial statements.

Standby letters of credit are written conditional commitments issued by us to guarantee the performance of a customer to a third party. In the event the customer does not perform in accordance with the terms of the agreement with the third party, we would be required to fund the commitment. The maximum potential amount of future payments we could be required to make is represented by the contractual amount of the commitment. If the commitment is funded, we would be

entitled to seek recovery from the customer. Our policies generally require that standby letter of credit arrangements contain security and debt covenants similar to those contained in loan agreements.

In the aggregate, the Bank had outstanding unused commitments to extend credit of $1.9 billion at December 31, 2017 and outstanding financial and performance standby letters of credit of $24.4 million at December 31, 2017.

In the normal course of business, the Hilltop Broker-Dealers execute, settle and finance various securities transactions that may expose the Hilltop Broker-Dealers to off-balance sheet risk in the event that a customer or counterparty does not fulfill its contractual obligations. Examples of such transactions include the sale of securities not yet purchased by customers or for the account of the Hilltop Broker-Dealers, use of derivatives to support certain non-profit housing organization clients, clearing agreements between the Hilltop Broker-Dealers and various clearinghouses and broker-dealers, secured financing arrangements that involve pledged securities, and when-issued underwriting and purchase commitments.

Critical Accounting Policies and Estimates

Our accounting policies are fundamental to understanding our management's discussion and analysis of our results of operations and financial condition. Our significant accounting policies are presented in Note 1 to our consolidated financial statements, which are included in this Annual Report. We have identified certain significant accounting policies which involve a higher degree of judgment and complexity in making certain estimates and assumptions that affect amounts reported in our consolidated financial statements. The significant accounting policies which we believe to be the most critical in preparing our consolidated financial statements relate to allowance for loan losses, FDIC Indemnification Asset, reserve for losses and LAE, goodwill and identifiable intangible assets, mortgage loan indemnification liability, mortgage servicing rights asset and acquisition accounting.

Allowance for Loan Losses

The allowance for loan losses is a valuation allowance for probable losses inherent in the loan portfolio. Loans are charged to the allowance when the loss is confirmed or when a determination is made that a probable loss has occurred on a specific loan. Recoveries are credited to the allowance at the time of recovery. Throughout the year, management estimates the probable level of losses to determine whether the allowance for credit losses is appropriate to absorb losses in the existing portfolio. Based on these estimates, an amount is charged to the provision for loan losses and credited to the allowance for loan losses in order to adjust the allowance to a level determined to be appropriate to absorb losses. Management's judgment regarding the appropriateness of the allowance for loan losses involves the consideration of current economic conditions and their estimated effects on specific borrowers; an evaluation of the existing relationships among loans, potential loan losses and the present level of the allowance; results of examinations of the loan portfolio by regulatory agencies; and management's internal review of the loan

portfolio. In determining the ability to collect certain loans, management also considers the fair value of any underlying collateral. The amount ultimately realized may differ from the carrying value of these assets because of economic, operating or other conditions beyond our control. For additional discussion of allowance for loan losses and provisions for loan losses, see the section entitled "Allowance for Loan Losses" earlier in this Item 7.

FDIC Indemnification Asset

The FDIC Indemnification Asset is initially recorded at fair value, based on the discounted value of expected future cash flows under the loss-share agreements. The difference between the present value and the undiscounted cash flows we expect to collect from the FDIC will be accreted into noninterest income within the consolidated statements of operations over the life of the FDIC Indemnification Asset. The FDIC Indemnification Asset is reviewed quarterly and the accretion rate is adjusted for changes in the timing of cash flows expected to be collected from the FDIC. Cumulative net losses over the life of the loss-share agreements of less than $240.4 million will reduce the value of the FDIC Indemnification Asset. Any amortization of changes in value of the FDIC Indemnification Asset is limited to the contractual terms of the loss-share agreements. Changes to the FDIC Indemnification Asset are recorded as adjustments to other noninterest income or expense, as appropriate, within the consolidated statements of operations over the life of the loss-share agreements.

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Reserve for Losses and Loss Adjustment Expenses

The reserve for losses and LAE represents our best estimate of our ultimate liability for losses and LAE relating to events that occurred prior to the end of any given accounting period but have not been paid, less a reduction for reinsurance recoverables related to those liabilities. Months and potentially years may elapse between the occurrence of a loss covered by one of our insurance policies, the reporting of the loss and the payment of the claim. We record a liability for estimates of losses that will be paid for claims that have been reported, which is referred to as case reserves. As claims are not always reported when they occur, we estimate liabilities for claims that have occurred but have not been reported ("IBNR").

Each of our insurance company subsidiaries establishes a reserve for all of its unpaid losses, including case reserves and IBNR reserves, and estimates for the cost to settle the claims. We estimate our IBNR reserves by estimating our ultimate liability for loss and LAE reserves first, and then reducing that amount by the amount of cumulative paid claims and by the amount of our case reserves. The reserve analysis performed by our actuaries provides preliminary central estimates of the unpaid losses and LAE. At each quarter-end, the results of the reserve analysis are summarized and discussed with our senior management. The senior management group considers many factors in determining the amount of reserves to record for financial statement purposes. These factors include the extent and timing of any recent catastrophic events, historical pattern and volatility of the actuarial indications, the sensitivity of the actuarial indications to changes in paid and reported loss patterns, the consistency of claims handling processes, the consistency of case reserving practices, changes in our pricing and underwriting, and overall pricing and underwriting trends in the insurance market. As experience develops or new information becomes known, we increase or decrease the level of our reserves in the period in which changes to the estimates are determined. Accordingly, the actual losses and LAE may differ materially from the estimates we have recorded. See "Insurance Losses and Loss Adjustment Expenses" earlier in this Item 7 for additional discussion.

Goodwill and Identifiable Intangible Assets

Goodwill and other identifiable intangible assets were initially recorded at their estimated fair values at the date of acquisition. Goodwill and other intangible assets having an indefinite useful life are not amortized for financial statement purposes. In the event that facts and circumstances indicate that the goodwill and other identifiable intangible assets may be impaired, an interim impairment test would be required. Intangible assets with finite lives have been fully amortized over their useful lives. We perform required annual impairment tests of our goodwill and other intangible assets as of October 1st for our reporting units.

As of January 1, 2017, we adopted the provisions of ASU 2017-04 which removes Step 2 from the goodwill impairment test and eliminates the determination of goodwill impairment through calculation of the implied fair value when the carrying amount of a reporting unit exceeds its fair value. The goodwill impairment test requires us to make judgments in determining what assumptions to use in the calculation. The process consists of estimating the fair value of each reporting unit based on valuation techniques, including a discounted cash flow model using revenue and profit

forecasts and recent industry transaction and trading multiples of our peers, and comparing those estimated fair values with the carrying values of the assets and liabilities of the reporting unit, which includes the allocated goodwill. If the estimated fair value is less than the carrying value, we will recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit’s fair value; however, the loss recognized will not exceed the total amount of goodwill allocated to that reporting unit.

Our evaluation includes multiple assumptions, including estimated discounted cash flows and other estimates that may change over time. If future discounted cash flows become less than those projected by us, future impairment charges may become necessary that could have a materially adverse impact on our results of operations and financial condition in the period in which the write-off occurs.

Mortgage Loan Indemnification Liability

The mortgage origination segment may be responsible for errors or omissions relating to its representations and warranties that the mortgage loans sold meet certain requirements, including representations as to underwriting standards and the validity of certain borrower representations in connection with the mortgage loan. If determined to be at fault, the mortgage origination segment either repurchases the mortgage loans from the investors or reimburses the investors’ losses (a “make-whole” payment). The mortgage origination segment has established an indemnification liability for such

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probable losses based upon, among other things, the level of current unresolved repurchase requests, the volume of estimated probable future repurchase requests, our ability to cure the defects identified in the repurchase requests, and the severity of the estimated loss upon repurchase. Although we consider this reserve to be appropriate, there can be no assurance that the reserve will prove to be appropriate over time to cover ultimate losses, due to unanticipated adverse changes in the economy and historical loss patterns, discrete events adversely affecting specific borrowers or industries, and/or actions taken by institutions or investors. The impact of such matters will be considered in the reserving process when known.

Mortgage Servicing Rights Asset

The Company measures its residential mortgage servicing rights asset using the fair value method. Under the fair value method, the retained MSR assets are carried in the balance sheet at fair value and the changes in fair value are reported in earnings within other noninterest income in the period in which the change occurs. Retained MSR assets are measured at fair value as of the date of sale of the related mortgage loan. Subsequent fair value measurements are determined using a discounted cash flow model. In order to determine the fair value of the MSR asset, the present value of expected future cash flows is estimated. Assumptions used include market discount rates, anticipated prepayment speeds, delinquency and foreclosure rates, and ancillary fee income.

The model assumptions and the MSR asset fair value estimates are compared to observable trades of similar portfolios as well as to MSR asset broker valuations and industry surveys, as available. The expected life of the loan can vary from management’s estimates due to prepayments by borrowers, especially when rates fall. Prepayments in excess of management’s estimates would negatively impact the recorded value of the MSR asset. The value of the MSR asset is also dependent upon the discount rate used in the model, which is based on current market rates. Management reviews this rate on an ongoing basis based on current market rates. A significant increase in the discount rate would reduce the value of the MSR asset.

Acquisition Accounting

We account for business combinations using the acquisition method, which requires an allocation of the purchase price of an acquired entity to the assets acquired, including identifiable intangibles, and liabilities assumed based on their estimated fair values at the date of acquisition. Management applies various valuation methodologies to these acquired assets and assumed liabilities which often involve a significant degree of judgment, particularly when liquid markets do not exist for the particular item being valued. Examples of such items include loans, deposits, identifiable intangible assets and certain other assets and liabilities acquired or assumed in business combinations. Management uses significant estimates and assumptions to value such items, including, among others, projected cash flows, prepayment and default assumptions, discount rates, and realizable collateral values. Purchase date valuations, which are subject to change for up to one year after the acquisition date, determine the amount of goodwill or bargain purchase gain recognized in connection with the business combination. Changes to provisional amounts identified during this measurement period are recognized in the reporting period in which the adjustment amounts are

determined. Certain assumptions and estimates must be updated regularly in connection with the ongoing accounting for purchased loans. Valuation assumptions and estimates may also have to be revisited in connection with periodic assessments of possible value impairment, including impairment of goodwill, intangible assets and certain other long-lived assets. The use of different assumptions could produce significantly different valuation results, which could have material positive or negative effects on the Company’s results of operations.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

The primary objective of the following information is to provide forward-looking quantitative and qualitative information about our potential exposure to market risks. Market risk represents the risk of loss that may result from changes in value of a financial instrument as a result of changes in interest rates, market prices and the credit perception of an issuer. The disclosure is not meant to be a precise indicator of expected future losses, but rather an indicator of reasonably possible losses, and therefore our actual results may differ from any of the following projections. This forward-looking information provides an indicator of how we view and manage our ongoing market risk exposures.

At December 31, 2017, total debt obligations on our consolidated balance sheet, excluding short-term borrowings and unamortized debt issuance costs and premiums, were $276.9 million, and were comprised of $169.0 million in debt obligations subject to fixed interest rates, with the remainder of indebtedness subject to variable interest rates. If LIBOR

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and the prime rate were to increase by one eighth of one percent (0.125%), the increase in interest expense on the variable rate debt would not have a significant impact on our future consolidated earnings or cash flows.

Banking Segment

The banking segment is engaged primarily in the business of investing funds obtained from deposits and borrowings in interest-earning loans and investments, and our primary component of market risk is sensitivity to changes in interest rates. Consequently, our earnings depend to a significant extent on our net interest income, which is the difference between interest income on loans and investments and our interest expense on deposits and borrowings. To the extent that our interest-bearing liabilities do not reprice or mature at the same time as our interest-bearing assets, we are subject to interest rate risk and corresponding fluctuations in net interest income.

There are several common sources of interest rate risk that must be effectively managed if there is to be minimal impact on our earnings and capital. Repricing risk arises largely from timing differences in the pricing of assets and liabilities. Reinvestment risk refers to the reinvestment of cash flows from interest payments and maturing assets at lower or higher rates. Basis risk exists when different yield curves or pricing indices do not change at precisely the same time or in the same magnitude such that assets and liabilities with the same maturity are not all affected equally. Yield curve risk refers to unequal movements in interest rates across a full range of maturities.

We have employed asset/liability management policies that attempt to manage our interest-earning assets and interest-bearing liabilities, thereby attempting to control the volatility of net interest income, without having to incur unacceptable levels of risk. We employ procedures which include interest rate shock analysis, repricing gap analysis and balance sheet decomposition techniques to help mitigate interest rate risk in the ordinary course of business. In addition, the asset/liability management policies permit the use of various derivative instruments to manage interest rate risk or hedge specified assets and liabilities.

An interest rate sensitive asset or liability is one that, within a defined time period, either matures or experiences an interest rate change in line with general market interest rates. The management of interest rate risk is performed by analyzing the maturity and repricing relationships between interest-earning assets and interest-bearing liabilities at specific points in time ("GAP") and by analyzing the effects of interest rate changes on net interest income over specific periods of time by projecting the performance of the mix of assets and liabilities in varied interest rate environments. Interest rate sensitivity reflects the potential effect on net interest income resulting from a movement in interest rates. A company is considered to be asset sensitive, or have a positive GAP, when the amount of its interest-earning assets maturing or repricing within a given period exceeds the amount of its interest-bearing liabilities also maturing or repricing within that time period. Conversely, a company is considered to be liability sensitive, or have a negative GAP, when the amount of its interest-bearing liabilities maturing or repricing within a given period exceeds the amount of its interest-earning assets also maturing or repricing within that time period. During a period of rising interest rates, a negative GAP would tend to affect net interest income adversely, while a positive GAP would tend to result in an increase in net interest income. During a period of falling interest rates, a negative GAP would tend to

result in an increase in net interest income, while a positive GAP would tend to affect net interest income adversely. However, it is our intent to remain relatively balanced so that changes in rates do not have a significant impact on earnings.

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As illustrated in the table below, the banking segment is asset sensitive overall. Loans that adjust daily or monthly to the Wall Street Journal Prime rate comprise a large percentage of interest sensitive assets and are the primary cause of the banking segment's asset sensitivity. To help neutralize interest rate sensitivity, the banking segment has kept the terms of most of its borrowings under one year as shown in the following table (dollars in thousands).

	December 31, 2017					
	3 Months or Less	> 3 Months to 1 Year	> 1 Year to 3 Years	> 3 Years to 5 Years	> 5 Years	Total
Interest sensitive assets:						
Loans	$ 4,405,211	$ 1,067,238	$ 1,421,347	$ 330,929	$ 192,123	$ 7,416,848
Securities	118,943	139,268	227,719	106,494	403,055	995,479
Federal funds sold and securities purchased under agreements to resell	405	—	—	—	—	405
Other interest sensitive assets	265,294	—	—	—	29,160	294,454
Total interest sensitive assets	4,789,853	1,206,506	1,649,066	437,423	624,338	8,707,186
Interest sensitive liabilities:						
Interest bearing checking	$ 3,614,991	$ —	$ —	$ —	$ —	$ 3,614,991
Savings	218,812	—	—	—	—	218,812
Time deposits	311,800	510,904	562,597	13,657	9,797	1,408,755
Notes payable and other borrowings	483,756	11,992	4,955	1,271	6,115	508,089
Total interest sensitive	4,629,359	522,896	567,552	14,928	15,912	5,750,647

liabilities						
Interest sensitivity gap	$ 160,494	$ 683,610	$ 1,081,514	$ 422,495	$ 608,426	$ 2,956,539
Cumulative interest sensitivity gap	$ 160,494	$ 844,104	$ 1,925,618	$ 2,348,113	$ 2,956,539	
Percentage of cumulative gap to total interest sensitive assets	1.84 %	9.69 %	22.12 %	26.97 %	33.96 %	

The positive GAP in the interest rate analysis indicates that banking segment net interest income would generally rise if rates increase. Because of inherent limitations in interest rate GAP analysis, the banking segment uses multiple interest rate risk measurement techniques. Simulation analysis is used to subject the current repricing conditions to rising and falling interest rates in increments and decrements of 1%, 2% and 3% to determine the effect on net interest income changes for the next twelve months. The banking segment also measures the effects of changes in interest rates on economic value of equity by discounting projected cash flows of deposits and loans. Economic value changes in the investment portfolio are estimated by discounting future cash flows and using duration analysis. Investment security prepayments are estimated using current market information. We believe the simulation analysis presents a more accurate picture than the GAP analysis. Simulation analysis recognizes that deposit products may not react to changes in interest rates as quickly or with the same magnitude as earning assets contractually tied to a market rate index. The sensitivity to changes in market rates varies across deposit products. Also, unlike GAP analysis, simulation analysis takes into account the effect of embedded options in the securities and loan portfolios as well as any off-balance-sheet derivatives.

The table below shows the estimated impact of increases of 1%, 2% and 3% and a decrease of 0.5% in interest rates on net interest income and on economic value of equity for the banking segment at December 31, 2017 (dollars in thousands).

Change in Interest Rates	Changes in Net Interest Income		Changes in Economic Value of Equity	
(basis points)	Amount	Percent	Amount	Percent
+300	$ 64,266	20.34 %	$ 275,309	14.92 %
+200	$ 42,744	13.53 %	$ 192,592	10.44 %
+100	$ 10,365	6.86 %	$ 98,511	5.34 %
-50	$ (4,260)	(1.35) %	$ (48,774)	(2.64) %

The projected changes in net interest income and economic value of equity to changes in interest rates at December 31, 2017 were in compliance with established internal policy guidelines. These projected changes are based on numerous assumptions of growth and changes in the mix of assets or liabilities.

The historically low level of interest rates, combined with the existence of rate floors that are in effect for a portion of the loan portfolio, are projected to cause yields on our earning assets to rise more slowly than increases in market interest rates. As a result, in a rising interest rate environment, our interest rate margins are projected to compress until contractual rate resets allow our entire loan portfolio to reprice above applicable rate floors.

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Broker-Dealer Segment

Our broker-dealer segment is exposed to market risk primarily due to its role as a financial intermediary in customer transactions, which may include purchases and sales of securities, use of derivatives and securities lending activities, and in our trading activities, which are used to support sales, underwriting and other customer activities. We are subject to the risk of loss that may result from the potential change in value of a financial instrument as a result of fluctuations in interest rates, market prices, investor expectations and changes in credit ratings of the issuer.

Our broker-dealer segment is exposed to interest rate risk as a result of maintaining inventories of interest rate sensitive financial instruments and other interest earning assets including customer and correspondent margin loans and securities borrowing activities. Our exposure to interest rate risk is also from our funding sources including customer and correspondent cash balances, bank borrowings, repurchase agreements and securities lending activities. Interest rates on customer and correspondent balances and securities produce a positive spread with rates generally fluctuating in parallel.

With respect to securities held, our interest rate risk is managed by setting and monitoring limits on the size and duration of positions and on the length of time securities can be held. Much of the interest rates on customer and correspondent margin loans are indexed and can vary daily. Our funding sources are generally short term with interest rates that can vary daily.

The following table categorizes the broker-dealer segment's net trading securities which are subject to interest rate and market price risk (dollars in thousands):

	December 31, 2017				
	1 Year or Less	> 1 Year to 5 Years	> 5 Years to 10 Years	> 10 Years	Total
Trading securities, at fair value					
Municipal obligations	$ 532	$ 10,264	$ 9,435	$ 150,182	$ 170,413
U.S. government and government agency obligations	3,092	(28,224)	(60,684)	356,624	270,808
Corporate obligations	(4,138)	(1,631)	10,409	28,139	32,779
Total debt securities	(514)	(19,591)	(40,840)	534,945	474,000
Corporate equity securities	(8,945)	-	-	-	(8,945)
Other	26,315	-	-	-	26,315
	$ 16,856	$ (19,591)	$ (40,840)	$ 534,945	$ 491,370
Weighted average yield					
Municipal obligations	1.46 %	2.25 %	2.51 %	3.36 %	3.24 %

U.S. government and government agency obligations	1.69 %	1.96 %	2.43 %	3.95 %	3.36 %
Corporate obligations	2.35 %	3.45 %	4.22 %	5.26 %	4.02 %

Derivatives are used to support certain customer programs and hedge our related exposure to interest rate risks.

Our broker-dealer segment is engaged in various brokerage and trading activities that expose us to credit risk arising from potential non-performance from counterparties, customers or issuers of securities. This risk is managed by setting and monitoring position limits for each counterparty, conducting periodic credit reviews of counterparties, reviewing concentrations of securities and conducting business through central clearing organizations.

Collateral underlying margin loans to customers and correspondents and with respect to securities lending activities is marked to market daily and additional collateral is required as necessary.

Mortgage Origination Segment

Within our mortgage origination segment, our principal market exposure is to interest rate risk due to the impact on our mortgage-related assets and commitments, including mortgage loans held for sale, IRLCs and MSR. Changes in interest rates could also materially and adversely affect our volume of mortgage loan originations.

IRLCs represent an agreement to extend credit to a mortgage loan applicant, whereby the interest rate on the loan is set prior to funding. Our mortgage loans held for sale, which we hold in inventory while awaiting sale into the secondary market, and our IRLCs are subject to the effects of changes in mortgage interest rates from the date of the commitment through the sale of the loan into the secondary market. As a result, we are exposed to interest rate risk and related price risk during the period from the date of the lock commitment until (i) the lock commitment cancellation or expiration date or (ii) the date of sale into the secondary mortgage market. Loan commitments generally range from 20 to 60 days, and

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our average holding period of the mortgage loan from funding to sale is approximately 30 days. An integral component of our interest rate risk management strategy is our execution of forward commitments to sell MBSs to minimize the impact on earnings resulting from significant fluctuations in the fair value of mortgage loans held for sale and IRLCs caused by changes in interest rates.

We have expanded, and may continue to expand, our residential mortgage servicing operations within our mortgage origination segment. As a result of our mortgage servicing business, we have a portfolio of retained MSR. One of the principal risks associated with MSR is that in a declining interest rate environment, they will likely lose a substantial portion of their value as a result of higher than anticipated prepayments. Moreover, if prepayments are greater than expected, the cash we receive over the life of the mortgage loans would be reduced. The mortgage origination segment uses derivative financial instruments, including interest rate swaps and swaptions, U.S. Treasury bond futures and options, and forward MBS commitments, as a means to mitigate market risk associated with MSR assets. No hedging strategy can protect us completely, and hedging strategies may fail because they are improperly designed, improperly executed and documented or based on inaccurate assumptions and, as a result, could actually increase our risks and losses. The increasing size of our MSR portfolio may increase our interest rate risk and, correspondingly, the volatility of our earnings, especially if we cannot adequately hedge the interest rate risk relating to our MSR.

The goal of our interest rate risk management strategy within our mortgage origination segment is not to eliminate interest rate risk, but to manage it within appropriate limits. To mitigate the risk of loss, we have established policies and procedures, which include guidelines on the amount of exposure to interest rate changes we are willing to accept.

Insurance Segment

Within our insurance segment, our exposures to market risk relate primarily to our investment portfolio, which is exposed primarily to interest rate risk and credit risk. The fair value of our investment portfolio is directly impacted by changes in market interest rates; generally, the fair value of fixed-income investments moves inversely with movements in market interest rates. Our fixed maturity portfolio is comprised of substantially all fixed rate investments with primarily short-term and intermediate-term maturities. This portfolio composition allows flexibility in reacting to fluctuations of interest rates. The portfolios of our insurance company subsidiaries are managed to achieve an adequate risk-adjusted return while maintaining sufficient liquidity to meet policyholder obligations. Additionally, the fair values of interest rate sensitive instruments may be affected by the creditworthiness of the issuer, prepayment options, relative values of alternative investments, the liquidity of the instrument and other general market conditions.

Item 8. Financial Statements and Supplementary Data.

Our financial statements required by this item are submitted as a separate section of this Annual Report. See “Financial Statements,” commencing on page F-1 hereof.

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

None.

Item 9A. Controls and Procedures.

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

Our management, with the supervision and participation of our Co-Principal Executive Officers and Principal Financial Officer, has evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this Annual Report.

Based upon that evaluation, our Co-Principal Executive Officers and Principal Financial Officer concluded that, as of the end of such period, our disclosure controls and procedures were effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports that we file or submit under the Exchange Act and are effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to the Company’s management, including our Co-Principal Executive Officers and Principal Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

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Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting during the fiscal quarter ended December 31, 2017 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Management's Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act, as a process designed by, or under the supervision of, our Co-Principal Executive Officers and Principal Financial Officer and effected by our board of directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of our assets;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorization of our management and directors; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

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

Management assessed the effectiveness of our internal control over financial reporting at December 31, 2017. In making this assessment, management used the criteria set forth in Internal Control—Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission, or COSO. Based on our assessment, management concluded that, at December 31, 2017, our internal control over financial reporting is effective.

The effectiveness of our internal control over financial reporting as of December 31, 2017, has been audited by PricewaterhouseCoopers LLP, our independent registered public accounting firm, as stated in its report below, which expressed an unqualified opinion on the effectiveness of our internal control over financial reporting as of December 31, 2017.

Item 9B. Other Information.

None.

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PART III

Item 10. Directors, Executive Officers and Corporate Governance.

The information called for by this Item is contained in our definitive Proxy Statement for our 2018 Annual Meeting of Stockholders, and is incorporated herein by reference.

Item 11. Executive Compensation.

The information called for by this Item is contained in our definitive Proxy Statement for our 2018 Annual Meeting of Stockholders, and is incorporated herein by reference.

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

The information called for by this Item is contained in our definitive Proxy Statement for our 2018 Annual Meeting of Stockholders, and is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions, and Director Independence.

The information called for by this Item is contained in our definitive Proxy Statement for our 2018 Annual Meeting of Stockholders, and is incorporated herein by reference.

Item 14. Principal Accounting Fees and Services.

The information called for by this Item is contained in our definitive Proxy Statement for our 2018 Annual Meeting of Stockholders, and is incorporated herein by reference.

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PART IV

Item 15. Exhibits, Financial Statement Schedules.

(a)The following documents are filed herewith as part of this Form 10-K.

		Page
1.	Financial Statements.	
	Hilltop Holdings Inc.	
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All other financial statement schedules have been omitted because they are not required, not applicable or the information has been included in our consolidated financial statements.

3. Exhibits. See the Exhibit Index preceding the signature page hereto.

Item 16. Form 10-K Summary.

None.

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Exhibit Number	Description of Exhibit
2.1	Purchase and Assumption Agreement — Whole Bank, All Deposits, dated as of September 13, 2013, by and among the Federal Deposit Insurance Corporation, receiver of First National Bank, Edinburg, Texas, PlainsCapital Bank and the Federal Deposit Insurance Corporation (filed as Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed on September 19, 2013 (File No. 001-31987) and incorporated herein by reference).
2.2	Agreement and Plan of Merger by and among SWS Group, Inc., Hilltop Holdings Inc. and Peruna LLC, dated as of March 31, 2014 (filed as Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed on April 1, 2014 (File No. 001-31987) and incorporated herein by reference).
3.1	Articles of Amendment and Restatement of Affordable Residential Communities Inc., dated February 16, 2004, as amended or supplemented by: Articles Supplementary, dated February 16, 2004; Corporate Charter Certificate of Notice, dated June 6, 2005; Articles of Amendment, dated January 23, 2007; Articles of Amendment, dated July 31, 2007; Corporate Charter Certificate of Notice, dated September 23, 2008; Articles Supplementary, dated December 15, 2010; Articles Supplementary, dated as of November 29, 2012 relating to Subtitle 8 election; Articles Supplementary, dated November 29, 2012 relating to Non-Cumulative Perpetual Preferred Stock, Series B, of Hilltop Holdings Inc.; and Articles of Amendment and Restatement, dated March 31, 2014 (filed as Exhibit 3.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2014 (File No. 001-31987) and incorporated herein by reference).
3.2	Third Amended and Restated Bylaws of Hilltop Holdings Inc. (filed as Exhibit 3.2 to the Registrant's Current Report on Form 8-K filed on January 31, 2018 (File No. 001-31987) and incorporated herein by reference).
4.1	Form of Certificate of Common Stock of Hilltop Holdings Inc. (filed as Exhibit 4.1 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2007 (File No. 001-31987) and incorporated herein by reference).
4.2	Corporate Charter Certificate of Notice, dated June 6, 2005 (filed as Exhibit 3.2 to the Registrant's Registration Statement on Form S-3 (File No. 333-125854) and incorporated herein by reference).
4.3.1	Amended and Restated Declaration of Trust, dated as of July 31, 2001, by and among U.S. Bank National Association (successor in interest to State Street Bank and Trust Company of Connecticut, National Association), as Institutional Trustee, PlainsCapital Corporation, and the Administrators party thereto from time to time (filed as Exhibit 4.2 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).
4.3.2	First Amendment to Amended and Restated Declaration of Trust, dated as of August 7, 2006, by and between PlainsCapital Corporation and U.S. Bank National Association, as Institutional Trustee (filed as Exhibit 4.3 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).
4.3.3	Indenture, dated as of July 31, 2001, by and between PlainsCapital Corporation and U.S. Bank National Association (successor in interest to State Street Bank and Trust Company of Connecticut, National

Association), as Trustee (filed as Exhibit 4.4 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.3.4 First Supplemental Indenture, dated as of August 7, 2006, by and between PlainsCapital Corporation and U.S. Bank National Association, as Trustee (filed as Exhibit 4.5 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

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4.3.5 Second Supplemental Indenture, dated as of November 30, 2012, by and among U.S. Bank National Association, as Trustee, PlainsCapital Corporation (f/k/a Meadow Corporation) and PlainsCapital Corporation (filed as Exhibit 4.5.5 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2012 filed on March 15, 2013 (File No. 001-31987) and incorporated herein by reference).

4.3.6 Amended and Restated Floating Rate Junior Subordinated Deferrable Interest Debenture of Plains Capital Corporation, dated as of August 7, 2006, by PlainsCapital Corporation in favor of U.S. Bank National Association, as Institutional Trustee for PCC Statutory Trust I (filed as Exhibit 4.6 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.3.7 Guarantee Agreement, dated as of July 31, 2001, by and between PlainsCapital and U.S. Bank National Association (successor in interest to State Street Bank and Trust Company of Connecticut, National Association), as Trustee (filed as Exhibit 4.7 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.3.8 First Amendment to Guarantee Agreement, dated as of August 7, 2006, by and between PlainsCapital Corporation and U.S. Bank National Association, as Guarantee Trustee (filed as Exhibit 4.8 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.4.1 Amended and Restated Declaration of Trust, dated as of March 26, 2003, by and among U.S. Bank National Association, as Institutional Trustee, PlainsCapital Corporation, and the Administrators party thereto from time to time (filed as Exhibit 4.9 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.4.2 Indenture, dated as of March 26, 2003, by and between PlainsCapital Corporation and U.S. Bank National Association, as Trustee (filed as Exhibit 4.10 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.4.3 First Supplemental Indenture, dated as of November 30, 2012, by and among U.S. Bank National Association, as Trustee, PlainsCapital Corporation (f/k/a Meadow Corporation) and PlainsCapital Corporation (filed as Exhibit 4.6.3 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2012 filed on March 15, 2013 (File No. 001-31987) and incorporated herein by reference).

4.4.4 Floating Rate Junior Subordinated Deferrable Interest Debenture of Plains Capital Corporation, dated as of March 26, 2003, by PlainsCapital Corporation in favor of U.S. Bank National Association, as Institutional Trustee for PCC Statutory Trust II (filed as Exhibit 4.11 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.4.5 Guarantee Agreement, dated as of March 26, 2003, by and between PlainsCapital Corporation and U.S. Bank National Association, as Guarantee Trustee (filed as Exhibit 4.12 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.5.1 Amended and Restated Declaration of Trust, dated as of September 17, 2003, by and among U.S. Bank National Association, as Institutional Trustee, PlainsCapital Corporation, and the Administrators party thereto from time to time (filed as Exhibit 4.13 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.5.2 Indenture, dated as of September 17, 2003, by and between PlainsCapital Corporation and U.S. Bank National Association, as Trustee (filed as Exhibit 4.14 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

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4.5.3 First Supplemental Indenture, dated as of November 30, 2012, by and among U.S. Bank National Association, as Trustee, PlainsCapital Corporation (f/k/a Meadow Corporation) and PlainsCapital Corporation. (filed as Exhibit 4.7.3 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2012 filed on March 15, 2013 (File No. 001-31987) and incorporated herein by reference).

4.5.4 Floating Rate Junior Subordinated Deferrable Interest Debenture of Plains Capital Corporation, dated as of September 17, 2003, by PlainsCapital Corporation in favor of U.S. Bank National Association, as Institutional Trustee for PCC Statutory Trust III (filed as Exhibit 4.15 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.5.5 Guarantee Agreement, dated as of September 17, 2003, by and between PlainsCapital Corporation and U.S. Bank National Association, as Guarantee Trustee (filed as Exhibit 4.16 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.6.1 Amended and Restated Trust Agreement, dated as of February 22, 2008, by and among PlainsCapital Corporation, Wells Fargo Bank, N.A., as Property Trustee, Wells Fargo Delaware Trust Company, as Delaware Trustee, and the Administrators party thereto from time to time (filed as Exhibit 4.17 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.6.2 Junior Subordinated Indenture, dated as of February 22, 2008, by and between PlainsCapital Corporation and Wells Fargo Bank, N.A., as Trustee (filed as Exhibit 4.18 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.6.3 First Supplemental Indenture, dated as of November 30, 2012, by and between PlainsCapital Corporation (f/k/a Meadow Corporation) and Wells Fargo Bank, National Association, as Trustee. (filed as Exhibit 4.8.3 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2012 filed on March 15, 2013 (File No. 001-31987) and incorporated herein by reference).

4.6.4 Plains Capital Corporation Floating Rate Junior Subordinated Note due 2038, dated as of February 22, 2008, by PlainsCapital Corporation in favor of Wells Fargo Bank, N.A., as Property Trustee of PCC Statutory Trust IV (filed as Exhibit 4.19 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.6.5 Guarantee Agreement, dated as of February 22, 2008, by and between PlainsCapital Corporation and Wells Fargo Bank, N.A., as Guarantee Trustee (filed as Exhibit 4.20 to the Registration Statement on Form 10 filed by PlainsCapital Corporation on April 17, 2009 (File No. 000-53629) and incorporated herein by reference).

4.7 Indenture, dated as of April 9, 2015, by and between Hilltop Holdings, Inc. and U.S. Bank National Association, as Trustee, including form of notes (filed as Exhibit 4.1 to the Registrant's Current Report on Form 8-K filed on April 9, 2015 (File No. 001-31987) and incorporated herein by reference).

10.1.1† Hilltop Holdings Inc. 2012 Equity Incentive Plan, effective September 20, 2012 (filed as Exhibit 10.18 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2012 filed on March 15, 2013 (File No. 001-31987) and incorporated herein by reference).

10.1.2†

Form of Restricted Stock Award Agreement (filed as Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 filed on May 6, 2013 (File No. 001-31987) and incorporated herein by reference).

10.1.3† Form of Restricted Stock Unit Award Agreement (Time-Based Vesting) (filed as Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed on February 28, 2014 (File No. 001-31987) and incorporated herein by reference).

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10.1.4† Form of Restricted Stock Unit Award Agreement (Performance-Based Vesting) (filed as Exhibit 10.2 to the Registrant's Current Report on Form 8-K filed on February 28, 2014 (File No. 001-31987) and incorporated herein by reference).

10.1.5† Form of Restricted Stock Unit Award Agreement (Performance-Based Vesting) for awards beginning in 2016 (filed as Exhibit 10.1 to the Registrant's Quarterly Report on Form 10-Q filed on April 28, 2016 (File No. 001-31987) and incorporated herein by reference).

10.1.6† Form of Restricted Stock Unit Award Agreement (Time-Based Vesting for Section 16 Officers) for awards beginning in 2016 (filed as Exhibit 10.2 to the Registrant's Quarterly Report on Form 10-Q filed on April 28, 2016 (File No. 001-31987) and incorporated herein by reference).

10.1.7† Form of Restricted Stock Unit Award Agreement (Time-Based Vesting for Non-Section 16 Officers) for awards beginning in 2016 (filed as Exhibit 10.3 to the Registrant's Quarterly Report on Form 10-Q filed on April 28, 2016 (File No. 001-31987) and incorporated herein by reference).

10.1.8†* Form of Restricted Stock Unit Award Agreement (Performance-Based Vesting) for awards beginning in 2018.

10.1.9†* Form of Restricted Stock Unit Award Agreement (Time-Based Vesting for Section 16 Officers) for awards beginning in 2018.

10.1.10†* Form of Restricted Stock Unit Award Agreement (Time-Based Vesting for Non-Section 16 Officers) for awards beginning in 2018.

10.2† Hilltop Holdings Inc. Annual Incentive Plan, effective September 20, 2012 (filed as Exhibit 10.19 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 2012 filed on March 15, 2013 (File No. 001-31987) and incorporated herein by reference).

10.3.1† Retention Agreement, dated May 8, 2012, but effective as of November 30, 2012, by and among Alan B. White, Hilltop Holdings Inc. and PlainsCapital Corporation (f/k/a Meadow Corporation) (filed as Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed on May 11, 2012 (File No. 001-31987) and incorporated herein by reference).

10.3.2† First Amendment to Retention Agreement and Assignment and Assumption Agreement by and among Hilltop Holdings Inc., PlainsCapital Corporation and Alan B. White, dated as of September 12, 2016 (filed as Exhibit 10.2 to the Registrant's Current Report on Form 8-K filed on September 13, 2016 (File No. 001-31987) and incorporated herein by reference).

10.4.1† Employment Agreement, dated as of December 4, 2014, by and between James R. Huffines and Hilltop Holdings Inc. (filed as Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed on December 9, 2014 (File No. 001-31987) and incorporated herein by reference).

10.4.2† First Amendment to Employment Agreement by and between Hilltop Holdings Inc. and James R. Huffines, dated as of September 12, 2016 (filed as Exhibit 10.3 to the Registrant's Current Report on Form 8-K filed on September 13, 2016 (File No. 001-31987) and incorporated herein by reference).

10.5† Employment Agreement, dated as of December 4, 2014, by and between Todd Salmans and Hilltop Holdings Inc. (filed as Exhibit 10.8 to the Registrant's Annual Report on Form 10-K for the year ended

December 31, 2014 (File No. 001-31987) and incorporated herein by reference).

10.5.1†	First Amendment to Employment Agreement, dated as of November 8, 2017, by and between Todd Salmans and Hilltop Holdings Inc. (filed as Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed on November 13, 2017 (File No. 001-31987) and incorporated herein by reference).
10.6†	Compensation arrangement of Jeremy B. Ford (filed as Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed on March 2, 2015 (File No. 001-31987) and incorporated herein by reference).

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10.7†	Compensation arrangement with Darren Parmenter (filed as Exhibit 10.2 to the Registrant's Current Report on Form 8-K filed on March 2, 2015 (File No. 001-31987) and incorporated herein by reference).
10.8†	Employment Agreement, dated as of September 1, 2016, by and between William Furr and Hilltop Holdings Inc. (filed as Exhibit 10.1 to the Registrant's Current Report on Form 8-K/A (Amendment No. 1) filed on September 7, 2016 (File No. 001-31987) and incorporated herein by reference).
10.9.1†	Sublease, dated December 1, 2012, by and between Hunter's Glen/Ford, LTD and Hilltop Holdings Inc. (filed as Exhibit 10.19 to the Registrant's Report on Form 10-K for the year ended December 31, 2013 filed on March 3, 2014 (File No. 001-31987) and incorporated herein by reference).
10.9.2†	First Amendment to Sublease, dated February 28, 2014, by and between Hunter's Glen/Ford, LTD and Hilltop Holdings Inc. (filed as Exhibit 10.20 to the Registrant's Report on Form 10-K for the year ended December 31, 2013 filed on March 3, 2014 (File No. 001-31987) and incorporated herein by reference).
21.1*	List of subsidiaries of the Registrant.
23.1*	Consent of PricewaterhouseCoopers LLP.
31.1*	Certification of Co-Principal Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
31.2*	Certification of Co-Principal Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
31.3*	Certification of Principal Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
32.1*	Certification of Co-Principal Executive Officers and Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase
101.DEF*	XBRL Taxonomy Extension Definition Linkbase
101.LAB*	XBRL Taxonomy Extension Label Linkbase
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase

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*Filed herewith.

†Exhibit is a management contract or compensatory plan.

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SIGNATURES

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

		HILLTOP HOLDINGS INC.
Date: February 15, 2018	By:	/s/ William B. Furr William B. Furr Chief Financial Officer (Principal Financial Officer and duly authorized officer)

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

Signature	Capacity in which Signed	Date
/s/ Jeremy B. Ford Jeremy B. Ford	President, Co-Chief Executive Officer and Director (Co-Principal Executive Officer)	February 15, 2018
/s/ Alan B. White Alan B. White	Co-Chief Executive Officer and Director (Co-Principal Executive Officer)	February 15, 2018
/s/ William B. Furr William B. Furr	Chief Financial Officer (Principal Financial Officer)	February 15, 2018
/s/ Keith E. Bornemann Keith E. Bornemann	Executive Vice President, Corporate Controller (Principal Accounting Officer)	February 15, 2018
Charlotte Jones Anderson	Director	
/s/ Rhodes Bobbitt Rhodes Bobbitt	Director	February 15, 2018
/s/ Tracy A. Bolt Tracy A. Bolt	Director and Audit Committee Member	February 15, 2018
W. Joris Brinkerhoff	Director	
/s/ J. Taylor Crandall J. Taylor Crandall	Director	February 15, 2018
/s/ Charles R. Cummings Charles R. Cummings	Director and Chairman of Audit Committee	February 15, 2018
/s/ Hill A. Feinberg Hill A. Feinberg	Director	February 15, 2018
/s/ Gerald J. Ford Gerald J. Ford	Director	February 15, 2018
/s/ J. Markham Green J. Markham Green	Director and Audit Committee Member	February 15, 2018
/s/ William T. Hill, Jr.	Director	February 15, 2018

William T. Hill, Jr.		
/s/ Lee Lewis Lee Lewis	Director	February 15, 2018
/s/ Andrew J. Littlefair Andrew J. Littlefair	Director	February 15, 2018
/s/ W. Robert Nichols, III W. Robert Nichols, III	Director	February 15, 2018
C. Clifton Robinson	Director	
/s/ Kenneth D. Russell Kenneth D. Russell	Director	February 15, 2018
/s/ A. Haag Sherman A. Haag Sherman	Director	February 15, 2018
/s/ Robert Taylor, Jr. Robert Taylor, Jr.	Director	February 15, 2018
/s/ Carl B. Webb Carl B. Webb	Director	February 15, 2018

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of Hilltop Holdings Inc.

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated balance sheets of Hilltop Holdings Inc. and its subsidiaries (the “Company”) as of December 31, 2017 and 2016, and the related consolidated statements of operations, comprehensive income, stockholders’ equity, and cash flows for each of the three years in the period ended December 31, 2017, including the related notes, as listed in the index appearing under Item 15(a)(1), and the financial statement schedule listed in the index appearing under Item 15(a)(2) (collectively referred to as the “consolidated financial statements”). We also have audited the Company's internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control - Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2017 and 2016, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2017 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control - Integrated Framework (2013) issued by the COSO.

Basis for Opinions

The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Report on Internal Control over Financial Reporting appearing under Item 9A. Our responsibility is to express opinions on the Company’s consolidated financial statements and on the Company's internal control over financial reporting 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 audits to obtain reasonable assurance about whether the consolidated financial statements are free of

material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated 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 regarding the amounts and disclosures in the consolidated 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 consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

Definition and Limitations of Internal Control over Financial Reporting

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

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

/s/ PricewaterhouseCoopers LLP

Dallas, Texas

February 15, 2018

We have served as the Company's auditor since 1998.

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HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share data)

	December 31, 2017	2016
Assets		
Cash and due from banks	$ 486,977	$ 669,357
Federal funds sold	405	21,407
Securities purchased under agreements to resell	186,537	89,430
Assets segregated for regulatory purposes	186,578	180,993
Securities:		
Trading, at fair value	730,685	265,534
Available for sale, at fair value (amortized cost of $767,946 and $598,198, respectively)	765,560	598,007
Held to maturity, at amortized cost (fair value of $349,939 and $345,088, respectively)	355,849	351,831
	1,852,094	1,215,372
Loans held for sale	1,715,357	1,795,463
Non-covered loans, net of unearned income	6,273,669	5,843,499
Allowance for non-covered loan losses	(60,957)	(54,186)
Non-covered loans, net	6,212,712	5,789,313
Covered loans, net of allowance of $2,729 and $413, respectively	179,400	255,714
Broker-dealer and clearing organization receivables	1,464,378	1,497,741
Premises and equipment, net	177,577	190,361
FDIC indemnification asset	29,340	71,313
Covered other real estate owned	36,744	51,642
Other assets	549,447	613,453
Goodwill	251,808	251,808
Other intangible assets, net	36,432	44,695
Total assets	$ 13,365,786	$ 12,738,062
Liabilities and Stockholders' Equity		
Deposits:		
Noninterest-bearing	$ 2,411,849	$ 2,199,483
Interest-bearing	5,566,270	4,864,328
Total deposits	7,978,119	7,063,811
Broker-dealer and clearing organization payables	1,287,563	1,347,128
Short-term borrowings	1,206,424	1,417,289
Securities sold, not yet purchased, at fair value	232,821	153,889
Notes payable	208,809	317,912

Junior subordinated debentures	67,012	67,012
Other liabilities	470,231	496,501
Total liabilities	11,450,979	10,863,542
Commitments and contingencies (see Notes 18 and 19)		
Stockholders' equity:		
Hilltop stockholders' equity:		
Common stock, $0.01 par value, 125,000,000 shares authorized; 95,982,184 and 98,543,774 shares issued and outstanding at December 31, 2017 and 2016, respectively	960	985
Additional paid-in capital	1,526,369	1,572,877
Accumulated other comprehensive income (loss)	(394)	485
Retained earnings	384,545	295,568
Deferred compensation employee stock trust, net	848	903
Employee stock trust (11,672 and 15,492 shares, at cost, respectively)	(247)	(309)
Total Hilltop stockholders' equity	1,912,081	1,870,509
Noncontrolling interests	2,726	4,011
Total stockholders' equity	1,914,807	1,874,520
Total liabilities and stockholders' equity	$ 13,365,786	$ 12,738,062

See accompanying notes.

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HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

	Year Ended December 31,		
	2017	2016	2015
Interest income:			
Loans, including fees	$ 411,988	$ 389,637	$ 390,359
Securities borrowed	41,048	29,518	41,051
Securities:			
Taxable	36,472	26,233	26,584
Tax-exempt	5,807	6,222	6,628
Other	11,841	4,344	5,216
Total interest income	507,156	455,954	469,838
Interest expense:			
Deposits	24,695	15,843	15,523
Securities loaned	32,337	22,510	29,893
Short-term borrowings	13,751	5,803	4,574
Notes payable	10,931	10,849	8,143
Junior subordinated debentures	3,016	2,676	2,401
Other	678	742	721
Total interest expense	85,408	58,423	61,255
Net interest income	421,748	397,531	408,583
Provision for loan losses	14,271	40,620	12,715
Net interest income after provision for loan losses	407,477	356,911	395,868
Noninterest income:			
Net gains from sale of loans and other mortgage production income	538,468	606,991	519,103
Mortgage loan origination fees	93,944	96,267	77,708
Securities commissions and fees	156,464	157,906	160,660
Investment and securities advisory fees and commissions	109,920	115,992	115,932
Net insurance premiums earned	142,298	155,545	162,082
Bargain purchase gain	—	—	81,289
Other	163,970	154,264	110,868
Total noninterest income	1,205,064	1,286,965	1,227,642
Noninterest expense:			
Employees' compensation and benefits	816,994	834,113	765,887
Occupancy and equipment, net	113,943	109,418	119,653
Professional services	101,521	128,176	107,107
Loss and loss adjustment expenses	94,701	89,243	99,066

Other	242,096	251,521	248,303
Total noninterest expense	1,369,255	1,412,471	1,340,016
Income before income taxes	243,286	231,405	283,494
Income tax expense	110,142	83,461	70,915
Net income	133,144	147,944	212,579
Less: Net income attributable to noncontrolling interest	600	2,050	1,606
Income attributable to Hilltop	$ 132,544	$ 145,894	$ 210,973
Dividends on preferred stock	—	—	1,854
Income applicable to Hilltop common stockholders	$ 132,544	$ 145,894	$ 209,119
Earnings per common share:			
Basic	$ 1.36	$ 1.48	$ 2.10
Diluted	$ 1.36	$ 1.48	$ 2.09
Cash dividends declared per common share	$ 0.24	$ 0.06	$ —
Weighted average share information:			
Basic	97,137	98,404	99,074
Diluted	97,353	98,629	99,962

See accompanying notes.

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HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands)

	Year Ended December 31,		
	2017	2016	2015
Net income	$ 133,144	$ 147,944	$ 212,579
Other comprehensive income:			
Net unrealized gains (losses) on securities available for sale, net of tax of $(565), $1,264 and $2,761, respectively	(869)	(2,144)	4,792
Reclassification adjustment for gains (losses) included in net income, net of tax of $(6), $0 and $(1,589), respectively	(10)	—	(2,814)
Comprehensive income	132,265	145,800	214,557
Less: comprehensive income attributable to noncontrolling interest	600	2,050	1,606
Comprehensive income applicable to Hilltop	$ 131,665	$ 143,750	$ 212,951

See accompanying notes.

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HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(in thousands)

	Preferred Stock		Common Stock		Additional Paid-in	Accumulated Other Comprehensive	Retained Earnings (Accumulated	Deferre Compe Employ Stock Trust,
	Shares	Amount	Shares	Amount	Capital	Income (Loss)	Deficit)	Net
Balance, December 31, 2014	114	$ 114,068	90,182	$ 902	$ 1,390,788	$ 651	$ (45,957)	$ —
Net income	—	—	—	—	—	—	210,973	—
Other comprehensive income	—	—	—	—	—	1,978	—	—
Issuance of common stock	—	—	10,113	101	199,932	—	—	—
Stock-based compensation expense	—	—	—	—	8,309	—	—	—
Common stock issued to board members	—	—	14	—	281	—	—	—
Issuance of common stock related to share-based awards, net	—	—	(22)	—	287	—	—	—
Dividends on preferred stock	—	—	—	—	—	—	(1,854)	—
Redemption of preferred stock	(114)	(114,068)	—	—	—	—	—	—
Repurchases of common stock	—	—	(1,391)	(14)	(22,327)	—	(7,687)	—
Deferred compensation plan	—	—	—	—	—	—	—	1,03
Net cash distributed to noncontrolling interest	—	—	—	—	—	—	—	—
	—	$ —	98,896	$ 989	$ 1,577,270	$ 2,629	$ 155,475	$ 1,03

Balance, December 31, 2015								
Net income	—	—	—	—	—	—	145,894	—
Other comprehensive loss	—	—	—	—	—	(2,144)	—	—
Issuance of common stock	—	—	538	5	4,134	—	—	—
Stock-based compensation expense	—	—	—	—	10,058	—	—	—
Common stock issued to board members	—	—	22	—	429	—	—	—
Issuance of common stock related to share-based awards, net	—	—	(96)	(1)	(2,746)	—	—	—
Repurchases of common stock	—	—	(816)	(8)	(16,268)	—	—	—
Dividends on common stock ($0.06 per share)	—	—	—	—	—	—	(5,801)	—
Deferred compensation plan	—	—	—	—	—	—	—	(131)
Net cash distributed from noncontrolling interest	—	—	—	—	—	—	—	—
Balance, December 31, 2016	—	$ —	98,544	$ 985	$ 1,572,877	$ 485	$ 295,568	$ 903
Net income	—	—	—	—	—	—	132,544	—
Other comprehensive loss	—	—	—	—	—	(879)	—	—
Stock-based compensation expense	—	—	—	—	10,307	—	—	—
Common stock issued to board members	—	—	17	—	451	—	—	—
Issuance of common stock related to share-based	—	—	337	4	(3,268)	—	—	—

awards, net								
Repurchases of common stock	—	—	(2,916)	(29)	(53,998)	—	(20,427)	—
Dividends on common stock ($0.24 per share)	—	—	—	—	—	—	(23,140)	—
Deferred compensation plan	—	—	—	—	—	—	—	(55)
Net cash distributed to noncontrolling interest	—	—	—	—	—	—	—	—
Balance, December 31, 2017	—	$ —	95,982	$ 960	$ 1,526,369	$ (394)	$ 384,545	$ 848

See accompanying notes.

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HILLTOP HOLDINGS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Year Ended December 31,		
	2017	2016	2015
Operating Activities			
Net income	$ 133,144	$ 147,944	$ 212,579
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Provision for loan losses	14,271	40,620	12,715
Depreciation, amortization and accretion, net	(13,869)	(49,765)	(83,360)
Net realized gains on securities	(16)	—	(4,403)
Bargain purchase gain	—	—	(81,289)
Deferred income taxes	40,933	(9,690)	17,376
Other, net	12,085	16,564	7,995
Net change in securities purchased under agreements to resell	(97,107)	16,230	(60,919)
Net change in assets segregated for regulatory purposes	(5,585)	(22,380)	99,010
Net change in trading securities	(465,151)	(51,388)	117,639
Net change in broker-dealer and clearing organization receivables	(42,449)	(46,775)	73,344
Net change in FDIC indemnification asset	24,890	20,577	39,936
Net change in other assets	(47,352)	41,315	(59,142)
Net change in broker-dealer and clearing organization payables	(2,412)	(33,180)	(54,048)
Net change in other liabilities	(55,557)	11,752	(104,897)
Net change in securities sold, not yet purchased	78,932	23,845	129,996
Proceeds from sale of mortgage servicing rights asset	17,499	7,586	—
Net gains from sales of loans	(538,468)	(606,991)	(519,103)
Loans originated for sale	(15,014,118)	(16,026,911)	(13,871,473)
Proceeds from loans sold	15,634,027	16,337,299	14,163,781
Net cash provided by (used in) operating activities	(326,303)	(183,348)	35,737
Investing Activities			
Proceeds from maturities and principal reductions of securities held to maturity	56,359	166,522	88,070
Proceeds from sales, maturities and principal reductions of securities available for sale	298,737	396,572	673,950
Purchases of securities held to maturity	(60,939)	(186,875)	(230,404)
Purchases of securities available for sale	(471,047)	(326,810)	(48,121)
Net change in loans	(216,562)	(555,040)	(150,605)
Purchases of premises and equipment and other assets	(31,152)	(41,941)	(31,270)
Proceeds from sales of premises and equipment and other real estate owned	32,297	73,032	110,922

Proceeds from redemption of bank owned life insurance	—	—	822
Net cash received from (paid for) Federal Home Loan Bank and Federal Reserve Bank stock	34,346	(19,021)	(12,172)
Net cash from acquisition	—	—	41,097
Net cash provided by (used in) investing activities	(357,961)	(493,561)	442,289
Financing Activities			
Net change in deposits	857,155	153,131	(601,386)
Net change in short-term borrowings	(210,865)	469,916	20,437
Proceeds from notes payable	403,136	296,993	150,078
Payments on notes payable	(512,193)	(217,630)	(42,571)
Redemption of preferred stock	—	—	(114,068)
Proceeds from issuance of common stock	—	4,139	—
Payments to repurchase common stock	(27,388)	—	(30,028)
Dividends paid on common stock	(23,140)	(5,801)	—
Dividends paid on preferred stock	—	—	(3,539)
Net cash distributed (to) from noncontrolling interest	(1,885)	790	(1,222)
Taxes paid on employee stock awards netting activity	(3,264)	(2,442)	(75)
Other, net	(674)	(868)	718
Net cash provided by (used in) financing activities	480,882	698,228	(621,656)
Net change in cash and cash equivalents	(203,382)	21,319	(143,630)
Cash and cash equivalents, beginning of year	690,764	669,445	813,075
Cash and cash equivalents, end of year	$ 487,382	$ 690,764	$ 669,445
Supplemental Disclosures of Cash Flow Information			
Cash paid for interest	$ 84,309	$ 58,429	$ 59,700
Cash paid for income taxes, net of refunds	$ 85,840	$ 88,899	$ 112,459
Supplemental Schedule of Non-Cash Activities			
Conversion of loans to other real estate owned	$ 8,853	$ 20,184	$ 57,838
Common stock issued in acquisition	$ —	$ —	$ 200,626
Additions to mortgage servicing rights	$ 16,401	$ 23,381	$ 24,974

See accompanying notes.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements

1. Summary of Significant Accounting and Reporting Policies

Nature of Operations

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

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

On January 1, 2015, Hilltop completed its acquisition of SWS Group, Inc. (“SWS”) in a stock and cash transaction (the "SWS Merger"), whereby SWS’s broker-dealer subsidiaries, Southwest Securities, Inc. and SWS Financial Services, Inc., became subsidiaries of Securities Holdings, and SWS’s banking subsidiary, Southwest Securities, FSB (“SWS FSB”), was merged into the Bank. On October 5, 2015, Southwest Securities, Inc. and SWS Financial Services, Inc. were renamed “Hilltop Securities Inc.” (“Hilltop Securities”) and “Hilltop Securities Independent Network Inc.” (“HTS Independent Network”), respectively. On October 22, 2015, the Financial Industry Regulatory Authority (“FINRA”) granted approval to combine First Southwest Company, LLC (“FSC”) and Hilltop Securities, subject to customary conditions. FSC, Hilltop Securities and HTS Independent Network operated as separate broker-dealers, under coordinated leadership from the date of the SWS Merger until January 22, 2016, when FSC was merged into Hilltop Securities to form a combined firm operating under the “Hilltop Securities” name. The term “Hilltop Broker-Dealers” is used to refer to FSC, Hilltop Securities and HTS Independent Network prior to January 22, 2016 and Hilltop Securities and HTS Independent Network after such date.

Basis of Presentation

The preparation of financial statements in conformity with accounting principles generally accepted in the United States ("GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Estimates regarding the allowance for loan losses, the fair values of financial instruments, the amounts receivable from the Federal Deposit Insurance Corporation (the "FDIC") under loss-share agreements (the "FDIC Indemnification Asset"), reserves for losses and loss adjustment expenses ("LAE"), the mortgage loan indemnification liability, and the potential impairment of assets are particularly subject to change. The Company has applied its critical accounting policies and estimation methods consistently in all periods presented in these consolidated financial statements.

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

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

Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

PCC also owns 100% of the outstanding common securities of PCC Statutory Trusts I, II, III and IV (the "Trusts"), which are not included in the consolidated financial statements under the requirements of the Variable Interest Entities Subsections of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC"), because the primary beneficiaries of the Trusts are not within the consolidated group.

Hilltop has a 100% membership interest in Securities Holdings, which operates through its wholly-owned subsidiaries, Hilltop Securities, HTS Independent Network and First Southwest Asset Management, LLC. Hilltop Securities is a broker-dealer registered with the Securities and Exchange Commission ("SEC") and FINRA and a member of the New York Stock Exchange ("NYSE"), HTS Independent Network is an introducing broker-dealer that is also registered with the SEC and FINRA, and First Southwest Asset Management, LLC, a wholly-owned subsidiary of First Southwest Holdings, LLC ("First Southwest"), is a registered investment adviser under the Investment Advisers Act of 1940. As discussed above, prior to January 22, 2016, Securities Holdings' subsidiaries also included FSC, First Southwest's principal subsidiary and formerly a broker-dealer registered with the SEC and FINRA and a member of the NYSE.

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

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

Certain reclassifications have been made to the prior period consolidated financial statements to conform with the current period presentation. In preparing these consolidated financial statements, subsequent events were evaluated through the time the financial statements were issued. Financial statements are considered issued when they are widely distributed to all stockholders and other financial statement users, or filed with the SEC.

Acquisition Accounting

Acquisitions are accounted for under the acquisition method of accounting. Purchased assets, including identifiable intangible assets, and assumed liabilities are recorded at their respective acquisition date fair values. If the fair value of net assets purchased exceeds the consideration given, a bargain purchase gain is recognized. If the consideration given exceeds the fair value of the net assets received, goodwill is recognized.

Securities Purchased Under Agreements to Resell

Securities purchased under agreements to resell (reverse repurchase agreements or reverse repos) are treated as collateralized financings and are carried at the amounts at which the securities will subsequently be resold as specified in the agreements. The Company is in possession of collateral with a fair value equal to or in excess of the contract amounts.

Securities

Management classifies securities at the time of purchase and reassesses such designation at each balance sheet date. Securities held for resale to facilitate principal transactions with customers are classified as trading, and are carried at fair value, with changes in fair value reflected in the consolidated statements of operations. Hilltop reports interest income on trading securities as interest income on securities and other changes in fair value as other noninterest income.

Securities held but not intended to be held to maturity or on a long-term basis are classified as available for sale. Securities included in this category are those that management intends to use as part of its asset/liability management strategy and that may be sold in response to changes in interest rates, resultant prepayment risk, and other factors related to interest rate and resultant prepayment risk changes. Securities available for sale are carried at fair value. Unrealized holding gains and losses on securities available for sale, net of taxes, are reported in other comprehensive income (loss) until realized. Premiums and discounts are recognized in interest income using the effective interest method and consider any optionality that may be embedded in the security.

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Purchases and sales (and related gain or loss) of securities are recorded on the trade date, based on specific identification. Declines in the fair value of available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses to the extent the other-than-temporary impairment ("OTTI") is related to credit losses. The amount of the OTTI related to other factors is recognized in other comprehensive income (loss). In estimating OTTI, management considers in developing its best estimate of cash flows, among other things, (i) the length of time and the extent to which the fair value has been less than cost, (ii) the financial condition and near-term prospects of the issuer, (iii) the historic and implied volatility of the security, (iv) failure of the issuer to make scheduled interest payments and (v) changes to the rating of the security by a rating agency.

Loans Held for Sale

Loans held for sale consist primarily of single-family residential mortgages funded through PrimeLending. These loans are generally on the consolidated balance sheet between 30 and 45 days. Substantially all mortgage loans originated by PrimeLending are sold to various investors in the secondary market, the majority with servicing released. Mortgage loans held for sale are carried at fair value in accordance with the provisions of the Fair Value Option Subsections of the ASC (the "Fair Value Option"). Changes in the fair value of the loans held for sale are recognized in earnings and fees and costs associated with origination are recognized as incurred. The specific identification method is used to determine realized gains and losses on sales of loans, which are reported as net gains (losses) in noninterest income. Loans sold are subject to certain indemnification provisions with investors, including the repurchase of loans sold and repayment of certain sales proceeds to investors under certain conditions. In addition, certain mortgage loans guaranteed by U.S. Government agencies and sold into Government National Mortgage Association ("GNMA") pools may, under certain conditions specified in the government programs, become subject to repurchase by PrimeLending. Such loans subject to repurchase no longer qualify for sale accounting and are reported as loans held for sale in the consolidated balance sheets.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at the amount of unpaid principal reduced by unearned income, net unamortized deferred fees and an allowance for loan losses. Unearned income on installment loans and interest on other loans is recognized using the effective interest method. Net fees received for providing loan commitments and letters of credit that result in loans are deferred and amortized to interest income over the life of the related loan, beginning with the initial borrowing. Net fees on commitments and letters of credit that are not expected to be funded are amortized to noninterest income over the commitment period. Income on direct financing leases is recognized on a basis that achieves a constant periodic rate of return on the outstanding investment.

Impaired loans include non-accrual loans, troubled debt restructurings, purchased credit impaired ("PCI") loans and partially charged-off loans. The accrual of interest on impaired loans is discontinued when, in management's opinion, there is a clear indication that the borrower's cash flow may not be sufficient to meet principal and interest payments, which is generally when a loan is 90 days past due unless the asset is both well secured and in the process of collection. When a loan is placed on non-accrual status, all previously accrued and unpaid interest is charged against income. If the ultimate collectability of principal, wholly or partially, is in doubt, any payment received on a loan on which the accrual of interest has been suspended is applied to reduce principal to the extent necessary to eliminate such doubt. Once the collection of the remaining recorded loan balance is fully expected, interest income is recognized on a cash basis.

The Bank originates loans to customers primarily in Texas. Although the Bank has diversified loan and leasing portfolios and, generally, holds collateral against amounts advanced to customers, its debtors' ability to honor their contracts is substantially dependent upon the general economic conditions of the region and of the industries in which its debtors operate, which consist primarily of agribusiness, construction, energy, real estate and wholesale/retail trade. PrimeLending originates mortgage loans to customers in its offices, which are located throughout the United States. Substantially all mortgage loans originated by PrimeLending are sold to various investors in the secondary market, the majority with servicing released, although PrimeLending does retain servicing in certain circumstances. The Hilltop Broker-Dealers make loans to customers and correspondents through margin transactions originated by both employees and independent retail representatives throughout the United States. The Hilltop Broker-Dealers control or controlled risk by requiring customers to maintain margin collateral in compliance with various regulatory and internal guidelines, which may vary based upon market conditions. Securities owned by customers and held as collateral for margin loans are not included in the consolidated financial statements.

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Management has defined the loans acquired in a business combination as acquired loans. Acquired loans are recorded at estimated fair value on their purchase date with no carryover of the related allowance for loan losses. At acquisition, acquired loans are segregated between those considered to be credit impaired and those without credit impairment at acquisition. To make this determination, management considered such factors as past due status, non-accrual status and credit risk ratings. The fair value of acquired performing loans was determined by discounting expected cash flows, both principal and interest, at prevailing market interest rates. The difference between the fair value and principal balances due at acquisition date, the fair value discount, is accreted into income over the estimated life of each loan.

Loans acquired in the FDIC-assisted transaction whereby the Bank acquired certain assets and assumed certain liabilities of Edinburg, Texas-based First National Bank ("FNB") on September 13, 2013 (the "FNB Transaction") that are subject to a loss-share agreement are referred to as "covered loans" and reported separately in the consolidated balance sheets. Covered loans are reported exclusive of the cash flow reimbursements that may be received from the FDIC. Covered loans are discussed in more detail within Note 6 to the consolidated financial statements.

PCI loans acquired by the Company upon completion of the merger with PCC (the "PlainsCapital Merger") are accounted for on an individual loan basis, while PCI loans acquired in each of the FNB Transaction and SWS Merger are accounted for in pools as well as on an individual loan basis. The Company has established under its PCI accounting policy a framework to aggregate certain acquired loans into various loan pools based on a minimum of two layers of similar risk characteristics for the purpose of determining their respective fair values as of their acquisition dates, and for applying the subsequent recognition and measurement provisions for income accretion and impairment testing. The similar risk characteristics used for the pooling of the FNB and SWS PCI loans are risk grade and loan collateral type.

PCI loans showed evidence of credit deterioration that makes it probable that all contractually required principal and interest payments will not be collected. Their fair value was initially based on an estimate of cash flows, both principal and interest, expected to be collected, discounted at prevailing market rates of interest. Management estimated cash flows using key assumptions such as default rates, loss severity rates assuming default, prepayment speeds and estimated collateral values. The excess of cash flows expected to be collected from a loan or pool over its estimated fair value at acquisition is referred to as the accretable yield and is recognized in interest income using an effective yield method over the remaining life of the loan or pool. The excess of total contractual cash flows over the cash flows expected to be received at acquisition is referred to as the nonaccretable difference. Subsequent to acquisition, management must update these estimates of cash flows expected to be collected at each reporting date. These updates require the continued use of key assumptions and estimates, similar to those used in the initial estimate of fair value.

The Bank accretes the discount for PCI loans for which it can predict the timing and amount of cash flows. PCI loans for which a discount is accreted are reported as performing loans.

Allowance for Loan Losses

The allowance for loan losses is a reserve established through a provision for loan losses charged to expense, which represents management's best estimate of probable losses inherent in the existing portfolio of loans at the balance sheet date. The allowance for loan losses includes allowance allocations calculated in accordance with the regulatory Interagency Policy Statement on the Allowance for Loan and Lease Losses and the Receivables and Contingencies Topics of the ASC. The level of the allowance reflects management's continuing evaluation of industry concentrations, specific credit risks, loan loss experience, current loan portfolio quality, present economic, political and regulatory conditions, and unidentified losses inherent in the current loan portfolio. Portions of the allowance may be allocated for specific credits; however, the entire allowance is available for any credit that, in management's judgment, should be charged off. While management utilizes its best judgment and information available, the ultimate adequacy of the allowance is dependent upon a variety of factors beyond the Bank's control, including the performance of the Bank's loan portfolio, the economy and changes in interest rates.

The Bank's allowance for loan losses consists of three elements: (i) specific valuation allowances established for probable losses on individually impaired loans; (ii) general historical valuation allowances calculated based on historical loan loss experience for homogenous loans with similar collateral; and (iii) valuation allowances to adjust general reserves based on current economic conditions and other qualitative risk factors both internal and external to the Bank.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

The Bank's methodology regarding the calculation of the allowance for loan losses is discussed in more detail within Note 5 to the consolidated financial statements.

Broker-Dealer and Clearing Organization Transactions

Amounts recorded in broker-dealer and clearing organization receivables and payables include securities lending activities, as well as amounts related to securities transactions for either customers of the Hilltop Broker-Dealers or for the accounts of the Hilltop Broker-Dealers. Securities-borrowed and securities-loaned transactions are generally reported as collateralized financings. Securities-borrowed transactions require the Hilltop Broker-Dealers to deposit cash, letters of credit, or other collateral with the lender. With respect to securities loaned, the Hilltop Broker-Dealers receive collateral in the form of cash or other assets in an amount generally in excess of the market value of securities loaned. The Hilltop Broker-Dealers monitor the market value of securities borrowed and loaned on a daily basis, with additional collateral obtained or refunded as necessary. Interest income and interest expense associated with collateralized financings is included in the accompanying consolidated statements of operations.

Insurance Premiums Receivable

Insurance premiums receivable include premiums written and not yet collected. NLC routinely evaluates the receivable balance to determine if an allowance for uncollectible amounts is necessary. At December 31, 2017 and 2016, NLC determined that no valuation allowance was necessary.

Deferred Policy Acquisition Costs

Costs of acquiring insurance vary with, and are primarily related to, the successful acquisition of new and renewal business, primarily consisting of commissions, premium taxes and underwriting expenses, and are deferred and amortized over the terms of the policies or reinsurance treaties to which they relate. Proceeds from reinsurance transactions that represent recovery of acquisition costs reduce applicable unamortized acquisition costs in such a manner that net acquisition costs are capitalized and charged to expense in proportion to net revenue recognized. Future investment income is considered in determining the recoverability of deferred policy acquisition costs. NLC regularly reviews the categories of acquisition costs that are deferred and assesses the recoverability of this asset. A premium deficiency and a corresponding charge to income is recognized if the sum of the expected loss and LAE, unamortized policy acquisition costs, and maintenance costs exceed related unearned insurance premiums and anticipated investment income. At December 31, 2017 and 2016, there was no premium deficiency.

Reinsurance

In the normal course of business, NLC seeks to reduce the loss that may arise from catastrophes or other events that could cause unfavorable underwriting results by reinsuring certain levels of risk in various areas of exposure with other insurance enterprises or reinsurers. Amounts recoverable from reinsurers are estimated in a manner consistent with the reinsured policy. NLC routinely evaluates the receivable balance to determine if any uncollectible balances exist.

Net insurance premiums earned, losses and LAE, and policy acquisition and other underwriting expenses are reported net of the amounts related to reinsurance ceded to other companies. Amounts recoverable from reinsurers related to the portions of the liability for losses and LAE and unearned insurance premiums ceded to them are included in other assets within the consolidated balance sheets. Reinsurance assumed from other companies, including assumed premiums written and earned, and losses and LAE, is accounted for in the same manner as direct insurance written.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation and amortization computed principally on the straight-line method over the estimated useful lives of the assets, which range between 3 and 40 years. Gains or losses on disposals of premises and equipment are included in results of operations.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

Other Real Estate Owned

Real estate acquired through foreclosure ("OREO") is included in other assets within the consolidated balance sheets and is carried at management's estimate of fair value, less estimated cost to sell. Any excess of recorded investment over fair value, less cost to sell, is charged against either the allowance for loan losses or the related PCI pool discount when property is initially transferred to OREO. Subsequent to the initial transfer to OREO, downward valuation adjustments are charged against earnings. Valuation adjustments, revenue and expenses from operations of the properties and resulting gains or losses on sale are included within the consolidated statements of operations in other noninterest income or expense, as appropriate.

Acquired OREO subject to FDIC loss-share agreements is referred to as "covered OREO" and reported separately in the consolidated balance sheets. Covered OREO is reported exclusive of expected reimbursement cash flows from the FDIC. Foreclosed covered loan collateral is transferred into covered OREO at the collateral's fair value, less selling costs. Covered OREO was initially recorded at its estimated fair value based on similar market comparable valuations, less estimated selling costs. Subsequently, loan collateral transferred to OREO is recorded at its net realizable value. Any subsequent valuation adjustments due to declines in fair value of the covered OREO will be charged to noninterest expense, while any recoveries of previous valuation decreases will be credited to noninterest expense.

FDIC Indemnification Asset

The Company has elected to account for the FDIC Indemnification Asset in accordance with the Business Combination Topic of the ASC. The FDIC Indemnification Asset is initially recorded at fair value, based on the discounted value of expected future cash flows under the loss-share agreements. The difference between the present value and the undiscounted cash flows the Bank expects to collect from the FDIC will be accreted into noninterest income or amortized into noninterest expense within the consolidated statements of operations over the life of the FDIC Indemnification Asset. The FDIC Indemnification Asset is reviewed quarterly and the accretion rate is adjusted for changes in the timing of cash flows expected to be collected from the FDIC. Cumulative net losses over the life of the loss-share agreements of less than $240.4 million will reduce the value of the FDIC Indemnification Asset. Any amortization of changes in value of the FDIC Indemnification Asset is limited to the contractual term of the loss-share agreements. Changes to the FDIC Indemnification Asset are recorded as adjustments to other noninterest income or expense, as appropriate, within the consolidated statements of operations over the life of the loss-share agreements.

Debt Issuance Costs

The Company capitalizes debt issuance costs associated with financing of debt. These costs are amortized using the effective interest method over the repayment term of the debt. Unamortized debt issuance costs are presented in the consolidated balance sheets as a direct reduction from the associated debt liability. Debt issuance costs of $0.1 million, $0.1 million, and $0.4 million during 2017, 2016 and 2015, respectively, were amortized and included in interest expense within the consolidated statements of operations. In April 2015, debt issuance costs of $1.9 million were capitalized in connection with Hilltop’s issuance of the 5% senior notes due 2025.

Goodwill

Goodwill, which represents the excess of cost over the fair value of the net assets acquired, is allocated to reporting units and tested for impairment annually, or whenever events or changes in circumstances indicate that the carrying amount should be assessed. The Company performs required annual impairment tests of its goodwill as of October 1st for each of its reporting units, which is one level below an operating segment. Goodwill is assigned to reporting units at the date the goodwill is initially recorded. Once goodwill has been assigned to reporting units, it no longer retains its association with a particular acquisition, and all of the activities within a reporting unit, whether acquired or internally generated, are available to support the value of the goodwill. As of January 1, 2017, the Company adopted the provisions of ASU 2017-04 which removes Step 2 from the goodwill impairment test and eliminates the determination of goodwill impairment through calculation of the implied fair value when the carrying amount of a reporting unit exceeds its fair value. The goodwill impairment test requires the Company to make judgments in determining what assumptions to use in the calculation. The process consists of estimating the fair value of each reporting unit based on valuation techniques, including a discounted cash flow model using revenue and profit forecasts and recent industry transaction and trading multiples of peers, and comparing those estimated fair values with the carrying values of the assets and liabilities of the

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reporting unit, which includes the allocated goodwill. If the estimated fair value is less than the carrying value, the Company will recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value; however, the loss recognized will not exceed the total amount of goodwill allocated to that reporting unit. Additional information concerning the results of the Company's impairment test of goodwill is included in Note 9 to the consolidated financial statements.

Intangibles and Other Long-Lived Assets

Intangible assets are acquired assets that lack physical substance but can be distinguished from goodwill because of contractual or other legal rights or because the asset is capable of being sold or exchanged either on its own or in combination with a related contract, asset or liability. The Company's intangible assets primarily consist of core deposits, trade names and customer relationships. Intangible assets with definite useful lives are generally amortized on the straight-line method over their estimated lives, although certain intangibles, including core deposits, and customer and agent relationships, are amortized on an accelerated basis. Amortization of intangible assets is recorded in other noninterest expense within the consolidated statements of operations. Intangible assets with indefinite useful lives are tested for impairment annually as of October 1st, or more often if events or circumstances indicate there may be impairment, and not amortized until their lives are determined to be definite. Intangible assets with definite useful lives, premises and equipment, and other long-lived 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.

Mortgage Servicing Rights

The Company determines its classes of residential mortgage servicing assets based on the asset type being serviced along with the methods used to manage the risk inherent in the servicing assets, which includes the market inputs used to value the servicing assets. The Company measures its servicing assets at fair value and reports changes in fair value through earnings.

The retained mortgage servicing rights ("MSR") asset is measured at fair value as of the date of sale of the related mortgage loan. Subsequent fair value measurements of the MSR asset are determined by valuing the projected net servicing cash flows, which are then discounted to estimate fair value using a discounted cash flow model. Assumptions used include market discount rates, anticipated prepayment speeds, delinquency and foreclosure rates, and ancillary fee income.

The model assumptions and the MSR asset fair value estimates are compared to observable trades of similar portfolios as well as to MSR asset broker valuations and industry surveys, as available. The expected life of the loan can vary from management's estimates due to prepayments by borrowers, especially when rates fall. Prepayments in excess of management's estimates would negatively impact the recorded value of the MSR asset. The value of the MSR asset is also dependent upon the discount rate used in the model, which is based on current market rates that are reviewed by management on an ongoing basis. A significant increase in the discount rate would reduce the value of the MSR asset.

Derivative Financial Instruments

The Company's hedging policies permit the use of various derivative financial instruments, including forward commitments, interest rate swaps and swaptions, and U.S. Treasury bond futures and options to manage interest rate risk or to hedge specified assets and liabilities. The Company's derivative financial instruments also include interest rate lock commitments ("IRLCs") executed with its customers that allow those customers to obtain a mortgage loan on a future date at an agreed-upon interest rate. The IRLCs, forward commitments, interest rate swaps and swaptions, and U.S. Treasury bond futures and options meet the definition of a derivative under the provisions of the Derivatives and Hedging Topic of the ASC.

Derivatives are recorded at fair value in the consolidated balance sheets. To qualify for hedge accounting, derivatives must be highly effective at reducing the risk associated with the exposure being hedged and must be designated as a hedge at the inception of the derivative contract. If derivative instruments are designated as hedges of fair values, the change in the fair value of both the derivative instrument and the hedged item are included in current earnings. Changes in the fair value of derivatives designated as hedges of cash flows are recorded in other comprehensive income (loss). Actual cash

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receipts and/or payments and related accruals on derivatives related to hedges are recorded as adjustments to the line item where the hedged item's effect on earnings is recorded.

Reserve for Losses and Loss Adjustment Expenses

The liability for losses and LAE includes an amount determined from loss reports and individual cases and an amount, based on past experience, for losses incurred but not reported ("IBNR"). Such liabilities are based on estimates and, while management believes that the amount is adequate, the ultimate liability may be in excess of or less than the amounts provided. The methods for making such estimates and for establishing the resulting liability are continually reviewed, and any adjustments are reflected in earnings currently. The liability for losses and LAE has not been reduced for reinsurance recoverable.

Loss Contingencies

Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated.

Stock-Based Compensation

Stock-based compensation expense for all share-based awards granted is based on the grant date fair value estimated in accordance with the provisions of the Stock Compensation Topic of the ASC. The Company recognizes these compensation costs for only those awards expected to vest over the service period of the award.

Advertising

Advertising costs are expensed as incurred. Advertising expense totaled $4.7 million, $5.3 million and $4.6 million during 2017, 2016 and 2015, respectively.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recorded for the estimated future tax effects of the temporary difference between the tax basis and book basis of assets and liabilities reported in the accompanying consolidated balance sheets. The provision for income tax expense or benefit differs from the amounts of income taxes currently payable because certain items of income and expense included in the consolidated financial statements are recognized in different time periods by taxing authorities. Interest and penalties incurred related to tax matters are charged to other interest expense or other noninterest expense, respectively. The revaluation of deferred tax assets as a result of enacted tax rate changes, such as those found in the Tax Cuts and Jobs Act ("Tax Legislation"), is recognized within income tax expense in continuing operations in the period of enactment.

Benefits from uncertain tax positions are recognized in the consolidated financial statements only when it is more likely than not that the tax position will be sustained upon examination by the appropriate taxing authority having full knowledge of all relevant information. A tax position that meets the more-likely-than-not recognition threshold is measured at the largest amount of cumulative benefit that is greater than fifty percent likely of being realized upon ultimate settlement. Tax positions that previously failed to meet the more-likely-than-not recognition threshold are recognized in the reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not recognition threshold are derecognized in the reporting period in which that threshold is no longer met. If the Company were to prevail on all uncertain tax positions, the effect would be a benefit to the Company's effective tax rate. Due to uncertainties in any tax audit outcome, estimates of the ultimate settlement of unrecognized tax positions may change and the actual tax benefits may differ significantly from the estimate.

Deferred tax assets, including net operating loss and tax credit carry forwards, are reduced by a valuation allowance when, in the opinion of management, it is more-likely-than-not that any portion of these tax attributes will not be realized. Periodic reviews of the carrying amount of deferred tax assets are made when it is more likely than not that all or a portion of a deferred tax asset will not be realized.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

Cash Flow Reporting

For the purpose of presentation in the consolidated statements of cash flows, cash and cash equivalents are defined as the amount included in the consolidated balance sheet captions "Cash and due from banks" and "Federal funds sold". Cash equivalents have original maturities of three months or less.

Repurchases of Common Stock

In accordance with Maryland law, the Company uses the par value method of accounting for its stock repurchases, whereby the par value of the shares is deducted from common stock. The excess of the cost of shares acquired over the par value is allocated to additional paid-in capital based on an estimated average sales price per issued share with the excess amounts charged to retained earnings.

Basic and Diluted Net Income Per Share

Nonvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents are participating securities and are included in the computation of earnings per share pursuant to the two-class method prescribed by the Earnings Per Share Topic of the ASC. The two-class method is an earnings allocation formula that determines earnings per share for each class of common stock and participating security according to dividends declared (or accumulated) and participation rights in undistributed earnings. Restricted Stock Awards, all of which were vested as of September 30, 2017, were the only instruments issued by Hilltop which qualified as participating securities.

Net earnings, less any preferred dividends accumulated for the period (whether or not declared), is allocated between the common stock and participating securities pursuant to the two-class method. Basic earnings per common share is computed by dividing net earnings available to common stockholders by the weighted average number of common shares outstanding during the period, excluding participating nonvested restricted shares.

Diluted earnings per common share is computed in a similar manner, except that first the denominator is increased to include the number of additional common shares that would have been outstanding if potentially dilutive common shares, excluding the participating securities, were issued using the treasury stock method. During 2017, restricted stock units ("RSUs") were the only potentially dilutive non-participating instruments issued by Hilltop, while during

2016 and 2015, stock options and RSUs were the only potentially dilutive non-participating instruments. Next, the Company determines and includes in the diluted earnings per common share calculation the more dilutive effect of the participating securities using the treasury stock method or the two-class method. Undistributed losses are not allocated to the nonvested share-based payment awards (the participating securities) under the two-class method as the holders are not contractually obligated to share in the losses of the Company.

2. Acquisition

SWS Merger

On January 1, 2015, Hilltop completed its acquisition of SWS in a stock and cash transaction, whereby each outstanding share of SWS common stock was converted into the right to receive 0.2496 shares of Hilltop common stock and $1.94 in cash, equating to $6.92 per share based on Hilltop's closing price on December 31, 2014 and resulting in an aggregate purchase price of $349.1 million, consisting of 10.1 million shares of common stock, $78.2 million in cash and $70.3 million associated with Hilltop's existing investment in SWS common stock. The operations acquired in the SWS Merger are included in the Company's operating results beginning January 1, 2015. Such operating results include a bargain purchase gain of $81.3 million and are not necessarily indicative of future operating results.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

The SWS Merger was accounted for using the acquisition method of accounting, and accordingly, purchased assets, including identifiable intangible assets, and assumed liabilities were recorded at their respective acquisition date fair values. The components of the consideration paid are shown in the following table (in thousands).

Fair value of consideration paid:	
Common stock issued	$ 200,626
Cash	78,217
Fair value of Hilltop's existing investment in SWS	70,282
Total consideration paid	$ 349,125

The resulting fair values of the identifiable assets acquired, and liabilities assumed, in the SWS Merger at January 1, 2015 are summarized in the following table (in thousands).

Cash and due from banks	$ 119,314
Federal funds sold and securities purchased under agreements to resell	44,741
Assets segregated for regulatory purposes	181,610
Securities	707,476
Non-covered loans, net	863,819
Broker-dealer and clearing organization receivables	1,221,793
Other assets	159,906
Total identifiable assets acquired	3,298,659
Deposits	(1,287,509)
Broker-dealer and clearing organization payables	(1,109,978)
Short-term borrowings	(164,240)
Securities sold, not yet purchased, at fair value	(140,409)
Notes payable	(76,643)
Other liabilities	(89,466)
Total liabilities assumed	(2,868,245)
Bargain purchase gain	(81,289)
	349,125
Less Hilltop existing investment in SWS	(70,282)
Net identifiable assets acquired	$ 278,843

The bargain purchase gain represents the excess of the estimated fair value of the underlying net tangible assets and intangible assets over the merger consideration. The SWS Merger was a tax-free reorganization under Section 368(a) of the Internal Revenue Code, therefore no income taxes were recorded in connection with the bargain purchase gain. The Company used significant estimates and assumptions to value certain identifiable assets acquired and liabilities

assumed. The bargain purchase gain was primarily driven by the Company's ability to realize acquired deferred tax assets through its consolidated core earnings and the decline in the price of the Company's common stock between the date the fixed conversion ratio was agreed upon and the closing date.

Included within the fair value of other assets in the table above are identifiable intangible assets recorded in connection with the SWS Merger. The allocation to intangible assets is as follows (in thousands).

	Estimated Useful Life (Years)	Gross Intangible Assets
Customer relationships	14	$ 7,300
Core deposits	4	160
		$ 7,460

In connection with the SWS Merger, Hilltop acquired loans both with and without evidence of credit quality deterioration since origination. The acquired loans were initially recorded at fair value with no carryover of any allowance for loan losses. Acquired loans were segregated between those considered to be PCI loans and those without

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

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

	Loans, excluding PCI Loans	PCI Loans	Total Loans
Commercial and industrial	$ 178,603	$ 9,850	$ 188,453
Real estate	324,477	62,218	386,695
Construction and land development	14,708	1,391	16,099
Consumer	3,216	—	3,216
Broker-dealer (1)	269,356	—	269,356
Total	$ 790,360	$ 73,459	$ 863,819

(1) Acquired loans include margin loans to customers and correspondents of $269.4 million associated with acquired broker-dealer operations, none of which are PCI loans.

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

Contractually required principal and interest payments	$ 120,078
Nonaccretable difference	32,040
Cash flows expected to be collected	88,038
Accretable difference	14,579
Fair value of loans acquired with a deterioration of credit quality	$ 73,459

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

Contractually required principal and interest payments	$ 901,672
Contractual cash flows not expected to be collected	39,721
Fair value at acquisition	790,360

3. Fair Value Measurements

Fair Value Measurements and Disclosures

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

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

- Level 1 Inputs: Unadjusted quoted prices in active markets for identical assets or liabilities that the Company can access at the measurement date.
- Level 2 Inputs: Observable inputs other than Level 1 prices. Level 2 inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, yield curves, prepayment speeds, default rates, credit risks and loss severities), and inputs that are derived from or corroborated by market data, among others.

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· Level 3 Inputs: Unobservable inputs that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities. Level 3 inputs include pricing models and discounted cash flow techniques, among others.

Fair Value Option

The Company has elected to measure substantially all of PrimeLending's mortgage loans held for sale and the retained MSR asset at fair value, under the provisions of the Fair Value Option. The Company elected to apply the provisions of the Fair Value Option to these items so that it would have the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. At December 31, 2017 and 2016, the aggregate fair value of PrimeLending's mortgage loans held for sale accounted for under the Fair Value Option was $1.58 billion and $1.75 billion, respectively, and the unpaid principal balance of those loans was $1.53 billion and $1.71 billion, respectively. The interest component of fair value is reported as interest income on loans in the accompanying consolidated statements of operations.

The Company holds a number of financial instruments that are measured at fair value on a recurring basis, either by the application of the Fair Value Option or other authoritative pronouncements. The fair values of those instruments are determined primarily using Level 2 inputs, as further described below.

Trading Securities — Trading securities are reported at fair value primarily using either Level 1 or Level 2 inputs in the same manner as discussed below for available for sale securities.

Available For Sale Securities — Most securities available for sale are reported at fair value using Level 2 inputs. The Company obtains fair value measurements from independent pricing services. As the Company is responsible for the determination of fair value, control processes are designed to ensure that the fair values received from independent pricing services are reasonable and the valuation techniques and assumptions used appear reasonable and consistent with prevailing market conditions. 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 prepayment speeds, credit information and the financial instruments' terms and conditions, among other things. For public common and preferred equity stocks, the determination of fair value uses Level 1 inputs based on observable market transactions.

Loans Held for Sale — Mortgage loans held for sale are reported at fair value, as discussed above, using Level 2 inputs that consist of commitments on hand from investors or prevailing market prices. These instruments are held for relatively short periods, typically no more than 30 days. As a result, changes in instrument-specific credit risk are not

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

Derivatives — Derivatives, which are included in other assets and liabilities within the Company's consolidated balance sheets, are reported at fair value using either Level 2 or Level 3 inputs. PrimeLending and the Hilltop Broker-Dealers use dealer quotes to value forward purchase commitments and forward sale commitments, respectively, executed for both hedging and non-hedging purposes. PrimeLending also issues IRLCs to its customers and the Hilltop Broker-Dealers issue forward purchase commitments to its clients that are valued based on the change in the fair value of the underlying mortgage loan from inception of the IRLC or purchase commitment to the balance sheet date, adjusted for projected loan closing rates. PrimeLending determines the value of the underlying mortgage loan as discussed in "Loans Held for Sale", above. The Hilltop Broker-Dealers determine the value of the underlying mortgage loan from prices of comparable securities used to value forward sale commitments. Additionally, PrimeLending uses dealer quotes to value interest rate swaps and swaptions executed to hedge its MSR asset.

MSR Asset — The MSR asset, which is included in other assets within the Company's consolidated balance sheets, is reported at fair value using Level 3 inputs. The MSR asset is valued by projecting net servicing cash flows, which are then discounted to estimate the fair value. The fair value of the MSR asset is impacted by a variety of factors. Prepayment rates and discount rates, the most significant unobservable inputs, are discussed further in Note 10 to the consolidated financial statements.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

Securities Sold, Not Yet Purchased — Securities sold, not yet purchased are reported at fair value primarily using either Level 1 or Level 2 inputs in the same manner as discussed above for trading and available for sale securities.

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

December 31, 2017	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Trading securities	$ 3,329	$ 727,356	$ —	$ 730,685
Available for sale securities	21,241	744,318	—	765,559
Loans held for sale	—	1,544,631	36,972	1,581,603
Derivative assets	—	34,150	—	34,150
MSR asset	—	—	54,714	54,714
Securities sold, not yet purchased	156,586	76,235	—	232,821
Derivative liabilities	—	13,197	—	13,197

December 31, 2016	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Trading securities	$ 9,481	$ 256,053	$ —	$ 265,534
Available for sale securities	19,840	578,167	—	598,007
Loans held for sale	—	1,712,697	35,801	1,748,498
Derivative assets	—	57,036	—	57,036
MSR asset	—	—	61,968	61,968
Securities sold, not yet purchased	60,715	93,174	—	153,889
Derivative liabilities	—	35,737	—	35,737

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

				Total Gains or Losses (Realized or Unrealized)		
	Balance at Beginning of	Purchases/	Sales/	Included in	Included in Other Comprehensive	Balance at

	Year	Additions	Reductions	Net Income	Income (Loss)	End of Year
Year ended December 31, 2017						
Loans held for sale	$ 35,801	$ 36,891	$ (26,773)	$ (8,947)	$ —	$ 36,972
MSR asset	61,968	16,401	(17,499)	(6,156)	—	54,714
Total	$ 97,769	$ 53,292	$ (44,272)	$ (15,103)	$ —	$ 91,686
Year ended December 31, 2016						
Trading securities	$ 1	$ —	$ —	$ (1)	$ —	$ —
Loans held for sale	25,880	60,999	(39,637)	(11,441)	—	35,801
MSR asset	52,285	23,381	(7,586)	(6,112)	—	61,968
Total	$ 78,166	$ 84,380	$ (47,223)	$ (17,554)	$ —	$ 97,769
Year ended December 31, 2015						
Trading securities	$ —	$ 7,301	$ (3,397)	$ (3,903)	$ —	$ 1
Loans held for sale	9,017	52,800	(25,514)	(10,423)	—	25,880
MSR asset	36,155	24,974	—	(8,844)	—	52,285
Total	$ 45,172	$ 85,075	$ (28,911)	$ (23,170)	$ —	$ 78,166

All net realized and unrealized gains (losses) in the table above are reflected in the accompanying consolidated financial statements. Excluding the trading securities activity noted above, the unrealized gains (losses) relate to financial instruments still held at December 31, 2017.

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Notes to Consolidated Financial Statements (continued)

For Level 3 financial instruments measured at fair value on a recurring basis at December 31, 2017, the significant unobservable inputs used in the fair value measurements were as follows.

Financial instrument	Valuation Technique	Unobservable Inputs	Range (Weighted-Average)
Loans held for sale	Discounted cash flows / Market comparable	Projected price	90 - 95 % (95 %)
MSR asset	Discounted cash flows	Constant prepayment rate	10.93 %
		Discount rate	11.03 %

The Company had no transfers between Levels 1 and 2 during the periods presented.

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

	Year Ended December 31, 2017			Year Ended December 31, 2016			Year Ended December 31, 2015		
	Net Gains (Losses)	Other Noninterest Income	Total Changes in Fair Value	Net Gains (Losses)	Other Noninterest Income	Total Changes in Fair Value	Net Gains (Losses)	Other Noninterest Income	Total Changes in Fair Value
Loans held for sale	$ 10,655	$ —	$ 10,655	$ (8,275)	$ —	$ (8,275)	$ (2,970)	$ —	$ (2,970)
MSR asset	(6,156)	—	(6,156)	(6,112)	—	(6,112)	(8,844)	—	(8,844)

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

Impaired Loans — The Company reports individually impaired loans based on the underlying fair value of the collateral through specific allowances within the allowance for loan losses. PCI loans with a fair value of $172.9 million, $822.8 million and $73.5 million were acquired by the Company upon completion of the PlainsCapital Merger, the FNB Transaction and the SWS Merger, respectively (collectively, the "Bank Transactions"). Substantially all PCI loans acquired in the FNB Transaction are covered by FDIC loss-share agreements. The fair value of PCI loans was determined using Level 3 inputs, including estimates of expected cash flows that incorporated significant unobservable inputs regarding default rates, loss severity rates assuming default, prepayment speeds on acquired loans accounted for in pools ("Pooled Loans"), and estimated collateral values.

At December 31, 2017, estimates for these significant unobservable inputs were as follows.

	PCI Loans					
	PlainsCapital Merger		FNB Transaction		SWS Merger	
Weighted average default rate	64	%	41	%	60	%
Weighted average loss severity rate	66	%	18	%	28	%
Weighted average prepayment speed	0	%	7	%	0	%

At December 31, 2017, the resulting weighted average expected loss on PCI loans associated with the PlainsCapital Merger, FNB Transaction and SWS Merger was 42%, 7% and 17%, respectively.

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

Other Real Estate Owned — The Company determines fair value primarily using independent appraisals of OREO properties. The resulting fair value measurements are classified as Level 2 inputs. In the FNB Transaction, the Bank acquired OREO of $135.2 million, all of which is covered by FDIC loss-share agreements. At December 31, 2017 and 2016, the estimated fair value of covered OREO was $36.7 million and $51.6 million, respectively, and the underlying fair value measurements utilize Level 2 inputs. The fair value of non-covered OREO at December 31, 2017 and 2016

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

was $3.9 million and $4.5 million, respectively, and is included in other assets within the consolidated balance sheets. During the reported periods, all fair value measurements for non-covered OREO subsequent to initial recognition utilized Level 2 inputs.

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

					Total Gains (Losses) for the Year Ended December 31,		
December 31, 2017	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value	2017	2016	2015
Non-covered impaired loans	$ —	$ —	$ 29,063	$ 29,063	$ (49)	$ 2,487	$ (126)
Covered impaired loans	—	—	83,849	83,849	(2,353)	1,156	3,034
Non-covered other real estate owned	—	3,883	—	3,883	(704)	(555)	(28)
Covered other real estate owned	—	10,187	—	10,187	(3,732)	(18,481)	(16,555)

The Fair Value of Financial Instruments Subsection of the ASC requires disclosure of the fair value of financial assets and liabilities, including the financial assets and liabilities previously discussed. The methods for determining estimated fair value for financial assets and liabilities measured at fair value on a recurring or non-recurring basis are discussed above. For other financial assets and liabilities, the Company utilizes quoted market prices, if available, to estimate the fair value of financial instruments. Because no quoted market prices exist for a significant portion of the Company’s financial instruments, the fair value of such instruments has been derived based on management’s assumptions with respect to future economic conditions, the amount and timing of future cash flows, and estimated discount rates. Different assumptions could significantly affect these estimates. Accordingly, the estimates provided herein do not necessarily indicate amounts which could be realized in a current transaction. Further, as it is management’s intent to hold a significant portion of its financial instruments to maturity, it is not probable that the fair values shown below will be realized in a current transaction.

Because of the wide range of permissible valuation techniques and the numerous estimates which must be made, it may be difficult to make reasonable comparisons of the Company’s fair value information to that of other financial institutions. The aggregate estimated fair value amount should in no way be construed as representative of the underlying value of Hilltop and its subsidiaries. The following methods and assumptions are typically used in estimating the fair value disclosures for financial instruments:

Cash and Cash Equivalents — For cash and due from banks and federal funds sold, the carrying amount is a reasonable estimate of fair value.

Securities Purchased Under Agreements to Resell — Securities purchased under agreements to resell are carried at the amounts at which the securities will subsequently be resold as specified in the agreements. The carrying amounts approximate fair value due to their short-term nature.

Assets Segregated for Regulatory Purposes — Assets segregated for regulatory purposes may consist of cash and securities with carrying amounts that approximate fair value.

Held to Maturity Securities — For securities held to maturity, estimated fair value equals quoted market price, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Loans Held for Sale — Loans held for sale consist primarily of certain mortgage loans held for sale that are subject to purchase by related parties. Such loans are reported at fair value, as discussed above, using Level 2 inputs that consist of commitments on hand from investors or prevailing market prices.

Loans — The fair value of non-covered and covered loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities.

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Notes to Consolidated Financial Statements (continued)

Broker-Dealer and Clearing Organization Receivables and Payables — The carrying amount approximates their fair value.

FDIC Indemnification Asset — The fair value of the FDIC Indemnification Asset is based on Level 3 inputs, including the discounted value of expected future cash flows under the loss-share agreements. The discount rate contemplates the credit worthiness of the FDIC as counterparty to this asset, and considers an incremental discount rate risk premium reflective of the inherent uncertainty associated with the timing of the cash flows.

Deposits — The estimated fair value of demand deposits, savings accounts and NOW accounts is the amount payable on demand at the reporting date. The fair value of fixed-maturity certificates of deposit is estimated using the rates currently offered for deposits of similar remaining maturities. The carrying amount for variable-rate certificates of deposit approximates their fair values.

Short-Term Borrowings — The carrying amounts of federal funds purchased, borrowings under repurchase agreements, Federal Home Loan Bank (“FHLB”) and other short-term borrowings approximate their fair values.

Debt — The fair values are estimated using discounted cash flow analysis based on current incremental borrowing rates for similar types of borrowing arrangements.

Other Assets and Liabilities — Other assets and liabilities primarily consists of cash surrender value of life insurance policies and accrued interest receivable and payable with carrying amounts that approximate their fair values using Level 2 inputs. The fair value of certain other receivables and investments is based on Level 3 inputs.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

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

		Estimated Fair Value			
December 31, 2017	Carrying Amount	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total
Financial assets:					
Cash and cash equivalents	$ 487,382	$ 487,382	$ —	$ —	$ 487,382
Securities purchased under agreements to resell	186,537	—	186,537	—	186,537
Assets segregated for regulatory purposes	186,578	186,578	—	—	186,578
Held to maturity securities	355,849	—	349,939	—	349,939
Loans held for sale	133,754	—	133,754	—	133,754
Non-covered loans, net	6,212,712	—	577,889	5,828,868	6,406,757
Covered loans, net	179,400	—	—	269,386	269,386
Broker-dealer and clearing organization receivables	1,464,378	—	1,464,378	—	1,464,378
FDIC indemnification asset	29,340	—	—	20,122	20,122
Other assets	64,862	—	59,053	5,809	64,862
Financial liabilities:					
Deposits	7,978,119	—	7,973,101	—	7,973,101
Broker-dealer and clearing organization payables	1,287,563	—	1,287,563	—	1,287,563
Short-term borrowings	1,206,424	—	1,206,424	—	1,206,424
Debt	275,821	—	289,719	—	289,719
Other liabilities	4,795	—	4,795	—	4,795

		Estimated Fair Value			
December 31, 2016	Carrying Amount	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total
Financial assets:					
Cash and cash equivalents	$ 690,764	$ 690,764	$ —	$ —	$ 690,764
Securities purchased under agreements to resell	89,430	—	89,430	—	89,430
Assets segregated for regulatory purposes	180,993	180,993	—	—	180,993
Held to maturity securities	351,831	—	345,088	—	345,088
Loans held for sale	46,965	—	46,965	—	46,965
Non-covered loans, net	5,789,313	—	502,077	5,459,975	5,962,052

Covered loans, net	255,714	—	—	367,444	367,444
Broker-dealer and clearing organization receivables	1,497,741	—	1,497,741	—	1,497,741
FDIC indemnification asset	71,313	—	—	60,173	60,173
Other assets	62,904	—	58,697	4,207	62,904
Financial liabilities:					
Deposits	7,063,811	—	7,058,837	—	7,058,837
Broker-dealer and clearing organization payables	1,347,128	—	1,347,128	—	1,347,128
Short-term borrowings	1,417,289	—	1,417,289	—	1,417,289
Debt	384,924	—	378,822	—	378,822
Other liabilities	3,708	—	3,708	—	3,708

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

4. Securities

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

	December 31,	
	2017	2016
U.S. Treasury securities	$ —	$ 5,940
U.S. government agencies:		
Bonds	52,078	36,303
Residential mortgage-backed securities	372,817	2,539
Commercial mortgage-backed securities	6,125	15,171
Collateralized mortgage obligations	5,122	5,607
Corporate debt securities	96,182	60,699
States and political subdivisions	170,413	89,946
Unit investment trusts	22,612	41,409
Private-label securitized product	1,631	4,292
Other	3,705	3,628
Totals	$ 730,685	$ 265,534

The Hilltop Broker-Dealers enter into transactions that represent commitments to purchase and deliver securities at prevailing future market prices to facilitate customer transactions and satisfy such commitments. Accordingly, the Hilltop Broker-Dealers' ultimate obligation may exceed the amount recognized in the financial statements. These securities, which are carried at fair value and reported as securities sold, not yet purchased in the consolidated balance sheets, had a value of $232.8 million and $153.9 million at December 31, 2017 and 2016, respectively.

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

	Available for Sale			
December 31, 2017	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. Treasury securities	$ 24,665	$ 107	$ (103)	$ 24,669
U.S. government agencies:				
Bonds	96,177	829	(366)	96,640
Residential mortgage-backed securities	246,707	538	(3,740)	243,505

Commercial mortgage-backed securities	11,966	105	(48)	12,023
Collateralized mortgage obligations	237,848	106	(4,142)	233,812
Corporate debt securities	66,868	1,819	(25)	68,662
States and political subdivisions	64,024	1,099	(115)	65,008
Commercial mortgage-backed securities	—	—	—	—
Equity securities	19,691	1,666	(116)	21,241
Totals	$ 767,946	$ 6,269	$ (8,655)	$ 765,560

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

	Available for Sale			
December 31, 2016	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. Treasury securities	$ 31,701	$ 144	$ (44)	$ 31,801
U.S. government agencies:				
Bonds	121,838	881	(67)	122,652
Residential mortgage-backed securities	135,371	708	(2,941)	133,138
Commercial mortgage-backed securities	8,771	2	(58)	8,715
Collateralized mortgage obligations	117,879	29	(3,206)	114,702
Corporate debt securities	76,866	2,354	(91)	79,129
States and political subdivisions	86,353	1,498	(336)	87,515
Commercial mortgage-backed securities	499	16	—	515
Equity securities	18,920	1,263	(343)	19,840
Totals	$ 598,198	$ 6,895	$ (7,086)	$ 598,007

	Held to Maturity			
December 31, 2017	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. government agencies:				
Bonds	$ 39,015	$ —	$ (1,188)	$ 37,827
Residential mortgage-backed securities	16,130	44	—	16,174
Commercial mortgage-backed securities	71,373	241	(735)	70,879
Collateralized mortgage obligations	173,928	19	(3,969)	169,978
States and political subdivisions	55,403	437	(759)	55,081
Totals	$ 355,849	$ 741	$ (6,651)	$ 349,939

	Held to Maturity			
December 31, 2016	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. government agencies:				
Bonds	$ 40,513	$ —	$ (1,287)	$ 39,226
Residential mortgage-backed securities	19,606	13	(6)	19,613
Commercial mortgage-backed securities	31,767	102	(593)	31,276
Collateralized mortgage obligations	217,954	128	(3,372)	214,710
States and political subdivisions	41,991	70	(1,798)	40,263
Totals	$ 351,831	$ 313	$ (7,056)	$ 345,088

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

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

	December 31, 2017			December 31, 2016		
	Number of Securities	Fair Value	Unrealized Losses	Number of Securities	Fair Value	Unrealized Losses
Available for Sale						
U.S. treasury securities:						
Unrealized loss for less than twelve months	6	$ 15,449	$ 69	7	$ 21,694	$ 44
Unrealized loss for twelve months or longer	1	4,150	34	—	—	—
	7	19,599	103	7	21,694	44
U.S. government agencies:						
Bonds:						
Unrealized loss for less than twelve months	10	83,476	367	1	14,908	67
Unrealized loss for twelve months or longer	—	—	—	—	—	—
	10	83,476	367	1	14,908	67
Residential mortgage-backed securities:						
Unrealized loss for less than twelve months	15	121,968	820	12	109,398	2,941
Unrealized loss for twelve months or longer	11	93,358	2,920	—	—	—
	26	215,326	3,740	12	109,398	2,941
Commercial mortgage-backed securities:						
Unrealized loss for less than twelve months	1	5,048	48	2	7,127	58
Unrealized loss for twelve months or longer	—	—	—	—	—	—
	1	5,048	48	2	7,127	58
Collateralized mortgage obligations:						
Unrealized loss for less than twelve months	16	90,886	819	11	91,144	2,340
Unrealized loss for twelve months or longer	17	80,492	3,323	8	19,320	866
	33	171,378	4,142	19	110,464	3,206
Corporate debt securities:						
	1	5,073	25	3	5,899	91

Unrealized loss for less than twelve months						
Unrealized loss for twelve months or longer	—	—	—	—	—	—
	1	5,073	25	3	5,899	91
States and political subdivisions:						
Unrealized loss for less than twelve months	9	6,981	97	32	17,549	322
Unrealized loss for twelve months or longer	9	2,876	18	1	450	14
	18	9,857	115	33	17,999	336
Equity securities:						
Unrealized loss for less than twelve months	1	944	13	—	—	—
Unrealized loss for twelve months or longer	1	6,800	102	2	11,107	343
	2	7,744	115	2	11,107	343
Total available for sale:						
Unrealized loss for less than twelve months	59	329,825	2,258	68	267,719	5,863
Unrealized loss for twelve months or longer	39	187,676	6,397	11	30,877	1,223
	98	$ 517,501	$ 8,655	79	$ 298,596	$ 7,086

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

	December 31, 2017			December 31, 2016		
	Number of Securities	Fair Value	Unrealized Losses	Number of Securities	Fair Value	Unrealized Losses
Held to Maturity						
U.S. government agencies:						
Bonds:						
Unrealized loss for less than twelve months	1	$ 5,950	$ 50	4	$ 33,225	$ 1,287
Unrealized loss for twelve months or longer	3	31,877	1,138	—	—	—
	4	37,827	1,188	4	33,225	1,287
Residential mortgage-backed securities:						
Unrealized loss for less than twelve months	—	—	—	2	13,178	6
Unrealized loss for twelve months or longer	—	—	—	—	—	—
	—	—	—	2	13,178	6
Commercial mortgage-backed securities:						
Unrealized loss for less than twelve months	7	39,396	271	5	18,891	588
Unrealized loss for twelve months or longer	2	12,659	464	1	1,401	5
	9	52,055	735	6	20,292	593
Collateralized mortgage obligations:						
Unrealized loss for less than twelve months	10	37,064	264	19	187,669	3,372
Unrealized loss for twelve months or longer	12	128,270	3,705	—	—	—
	22	165,334	3,969	19	187,669	3,372
States and political subdivisions:						
Unrealized loss for less than twelve months	22	11,079	71	71	29,862	1,790
Unrealized loss for twelve months or longer	46	18,598	688	1	462	8
	68	29,677	759	72	30,324	1,798
Total held to maturity:						
	40	93,489	656	101	282,825	7,043

Unrealized loss for less than twelve months						
Unrealized loss for twelve months or longer	63	191,404	5,995	2	1,863	13
	103	$ 284,893	$ 6,651	103	$ 284,688	$ 7,056

During 2017, 2016 and 2015, the Company did not record any OTTI. While some of the securities held in the investment portfolio have decreased in value since the date of acquisition, the severity of loss and the duration of the loss position are not believed to be significant enough to warrant OTTI of the securities. Factors considered in the Company's analysis include the reasons for the unrealized loss position, the severity and duration of the unrealized loss position, credit worthiness, and forecasted performance of the investee. The Company does not intend, nor is it likely that the Company will be required to sell, these securities before the recovery of the cost basis.

Expected maturities may differ from contractual maturities because certain borrowers may have the right to call or prepay obligations with or without penalties. The amortized cost and fair value of securities, excluding trading and available for sale equity securities, at December 31, 2017 are shown by contractual maturity below (in thousands).

	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ 101,815	$ 101,922	$ 3,245	$ 3,242
Due after one year through five years	95,284	96,442	2,847	2,843
Due after five years through ten years	30,893	32,064	27,051	26,289
Due after ten years	23,742	24,551	61,275	60,534
	251,734	254,979	94,418	92,908
Residential mortgage-backed securities	246,707	243,505	16,130	16,174
Collateralized mortgage obligations	237,848	233,812	173,928	169,978
Commercial mortgage-backed securities	11,966	12,023	71,373	70,879
	$ 748,255	$ 744,319	$ 355,849	$ 349,939

During 2017, 2016 and 2015, the Company realized net gains from its trading portfolio of $20.2 million, $15.9 million and $12.8 million, respectively. In addition, the Hilltop Broker-Dealers realized net gains from structured product trading activities of $62.8 million, $109.8 million and $0.3 million during 2017, 2016 and 2015, respectively. During 2017 and 2015, the Company had other net realized gains on securities of $16 thousand and $4.4 million, respectively. There were no other net realized gains on securities during 2016. All such realized net gains (losses) are recorded as a component of other noninterest income within the consolidated statements of operations.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

Securities with a carrying amount of $738.5 million and $695.1 million (with a fair value of $730.1 million and $688.1 million, respectively) at December 31, 2017 and 2016, respectively, were pledged to secure public and trust deposits, federal funds purchased and securities sold under agreements to repurchase, and for other purposes as required or permitted by law. Substantially all of these pledged securities were included in the Company's available for sale and held to maturity securities portfolios at December 31, 2017 and 2016.

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

At December 31, 2017 and 2016, NLC had investments on deposit in custody for various state insurance departments with carrying values of $9.3 million and $9.2 million, respectively.

5. Non-Covered Loans and Allowance for Non-Covered Loan Losses

Non-covered loans refer to loans not covered by the FDIC loss-share agreements. Covered loans are discussed in Note 6 to the consolidated financial statements. Non-covered loans summarized by portfolio segment are as follows (in thousands).

	December 31, 2017	2016
Commercial and industrial	$ 1,681,205	$ 1,696,453
Real estate	3,011,524	2,816,767
Construction and land development	962,605	786,850
Consumer	40,446	41,352
Broker-dealer (1)	577,889	502,077
	6,273,669	5,843,499
Allowance for non-covered loan losses	(60,957)	(54,186)
Total non-covered loans, net of allowance	$ 6,212,712	$ 5,789,313

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

The Bank has lending policies in place with the goal of establishing an asset portfolio that will provide a return on stockholders' equity sufficient to maintain capital to assets ratios that meet or exceed established regulations. Loans are underwritten with careful consideration of the borrower's financial condition, the specific purpose of the loan, the primary sources of repayment and any collateral pledged to secure the loan.

Underwriting procedures address financial components based on the size and complexity of the credit. The financial components include, but are not limited to, current and projected cash flows, shock analysis and/or stress testing, and trends in appropriate balance sheet and statement of operations ratios. The Bank's loan policy provides specific underwriting guidelines by portfolio segment, including commercial and industrial, real estate, construction and land development, and consumer loans. The guidelines for each individual portfolio segment set forth permissible and impermissible loan types. With respect to each loan type, the guidelines within the Bank's loan policy provide minimum requirements for the underwriting factors listed above. The Bank's underwriting procedures also include an analysis of any collateral and guarantor. Collateral analysis includes a complete description of the collateral, as well as determined values, monitoring requirements, loan to value ratios, concentration risk, appraisal requirements and other information relevant to the collateral being pledged. Guarantor analysis includes liquidity and cash flow evaluation based on the significance with which the guarantors are expected to serve as secondary repayment sources.

The Bank maintains a loan review department that reviews credit risk in response to both external and internal factors that potentially impact the performance of either individual loans or the overall loan portfolio. The loan review process reviews the creditworthiness of borrowers and determines compliance with the loan policy. The loan review process

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Notes to Consolidated Financial Statements (continued)

complements and reinforces the risk identification and assessment decisions made by lenders and credit personnel. Results of these reviews are presented to management and the Bank's board of directors.

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

	December 31,	
	2017	2016
Carrying amount	$ 37,204	$ 51,432
Outstanding balance	51,064	67,988

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

	Year Ended December 31,		
	2017	2016	2015
Balance, beginning of period	$ 13,116	$ 17,744	$ 12,814
Additions	—	—	14,579
Reclassifications from nonaccretable difference, net(1)	3,836	6,168	19,759
Disposals of loans	(664)	—	(2,371)
Accretion	(9,275)	(10,796)	(27,037)
Balance, end of period	$ 7,013	$ 13,116	$ 17,744

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

The remaining nonaccretable difference for non-covered PCI loans was $19.2 million and $22.8 million at December 31, 2017 and 2016, respectively.

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

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Notes to Consolidated Financial Statements (continued)

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

December 31, 2017	Unpaid Contractual Principal Balance	Recorded Investment with No Allowance	Recorded Investment with Allowance	Total Recorded Investment	Related Allowance
PCI					
Commercial and industrial:					
Secured	$ 19,752	$ 3,610	$ 2,489	$ 6,099	$ 89
Unsecured	—	—	—	—	—
Real estate:					
Secured by commercial properties	34,598	7,583	12,092	19,675	1,391
Secured by residential properties	12,600	5,307	4,558	9,865	325
Construction and land development:					
Residential construction loans	—	—	—	—	—
Commercial construction loans and land development	2,001	428	1,010	1,438	215
Consumer	2,377	12	115	127	18
Broker-dealer	—	—	—	—	—
	71,328	16,940	20,264	37,204	2,038
Non-PCI					
Commercial and industrial:					
Secured	23,666	15,308	2,072	17,380	365
Unsecured	761	616	—	616	—
Real estate:					
Secured by commercial properties	15,504	10,934	3,686	14,620	932
Secured by residential properties	1,596	1,177	—	1,177	—
Construction and land development:					
Residential construction loans	15	—	—	—	—
Commercial construction loans and land development	653	—	611	611	93
Consumer	162	56	—	56	—
Broker-dealer	—	—	—	—	—
	42,357	28,091	6,369	34,460	1,390
	$ 113,685	$ 45,031	$ 26,633	$ 71,664	$ 3,428

December 31, 2016	Unpaid Contractual Principal Balance	Recorded Investment with No Allowance	Recorded Investment with Allowance	Total Recorded Investment	Related Allowance
PCI					
Commercial and industrial:					
Secured	$ 25,354	$ 3,234	$ 5,438	$ 8,672	$ 557
Unsecured	—	—	—	—	—
Real estate:					
Secured by commercial properties	38,005	11,097	17,413	28,510	1,907
Secured by residential properties	13,606	7,401	3,088	10,489	200
Construction and land development:					
Residential construction loans	—	—	—	—	—
Commercial construction loans and land development	5,780	1,391	2,076	3,467	377
Consumer	3,223	237	57	294	56
Broker-dealer	—	—	—	—	—
	85,968	23,360	28,072	51,432	3,097
Non-PCI					
Commercial and industrial:					
Secured	6,311	3,313	1,372	4,685	115
Unsecured	946	925	—	925	—
Real estate:					
Secured by commercial properties	10,134	10,000	—	10,000	—
Secured by residential properties	1,344	1,116	—	1,116	—
Construction and land development:					
Residential construction loans	28	28	—	28	—
Commercial construction loans and land development	738	48	679	727	167
Consumer	246	244	—	244	—
Broker-dealer	—	—	—	—	—
	19,747	15,674	2,051	17,725	282
	$ 105,715	$ 39,034	$ 30,123	$ 69,157	$ 3,379

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

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

	Year Ended December 31,		
	2017	2016	2015
Commercial and industrial:			
Secured	$ 18,418	$ 19,730	$ 25,991
Unsecured	771	486	104
Real estate:			
Secured by commercial properties	36,403	40,014	32,149
Secured by residential properties	11,324	12,085	7,769
Construction and land development:			
Residential construction loans	14	125	111
Commercial construction loans and land development	3,122	4,619	7,462
Consumer	361	659	1,459
Broker-dealer	—	—	—
	$ 70,413	$ 77,718	$ 75,045

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

	December 31, 2017	December 31, 2016
Commercial and industrial:		
Secured	$ 20,262	$ 8,590
Unsecured	616	925
Real estate:		
Secured by commercial properties	14,620	11,034
Secured by residential properties	1,614	1,197
Construction and land development:		
Residential construction loans	—	28
Commercial construction loans and land development	611	727
Consumer	56	244
Broker-dealer	—	—
	$ 37,779	$ 22,745

At December 31, 2017 and 2016, non-covered non-accrual loans included non-covered PCI loans of $3.3 million and $5.0 million, respectively, for which discount accretion has been suspended because the extent and timing of cash

flows from these non-covered PCI loans can no longer be reasonably estimated. In addition to the non-covered non-accrual loans in the table above, $2.7 million and $1.7 million of real estate loans secured by residential properties and classified as held for sale were in non-accrual status at December 31, 2017 and 2016, respectively.

Interest income, including recoveries and cash payments, recorded on non-covered impaired loans was $0.5 million, $0.2 million and $8.9 million during 2017, 2016 and 2015, respectively. Except as noted above, non-covered PCI loans are considered to be performing due to the application of the accretion method.

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

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Information regarding TDRs granted during 2017, 2016 and 2015, respectively, is shown in the following table (in thousands). At December 31, 2017 and 2016, the Bank had nominal unadvanced commitments to borrowers whose loans have been restructured in TDRs.

	Year Ended December 31, 2017			Year Ended December 31, 2016			Year Ended December 31, 2015		
	Number of Loans	Balance at Extension	Balance at End of Period	Number of Loans	Balance at Extension	Balance at End of Period	Number of Loans	Balance at Extension	Balance at End of Period
Commercial and industrial:									
Secured	1	$ 1,357	$ 1,186	1	$ 1,196	$ 944	1	$ 89	$ 82
Unsecured	—	—	—	—	—	—	—	—	—
Real estate:									
Secured by commercial properties	2	4,775	4,629	—	—	—	1	1,083	1,040
Secured by residential properties	—	—	—	—	—	—	—	—	—
Construction and land development:									
Residential construction loans	—	—	—	—	—	—	—	—	—
Commercial construction loans and land development	1	655	611	—	—	—	1	76	—
Consumer	—	—	—	—	—	—	—	—	—
Broker-dealer	—	—	—	—	—	—	—	—	—
	4	$ 6,787	$ 6,426	1	$ 1,196	$ 944	3	$ 1,248	$ 1,122

All of the non-covered loan modifications included in the table above involved payment term extensions. The Bank did not grant principal reductions on any restructured non-covered loans during 2017, 2016 or 2015.

The following table presents information regarding TDRs granted during the twelve months preceding December 31, 2017 and 2016, respectively, for which a payment was at least 30 days past due (dollars in thousands).

	Twelve Months Preceding December 31, 2017			Twelve Months Preceding December 31, 2016		
	Number of Loans	Balance at Extension	Balance at End of Period	Number of Loans	Balance at Extension	Balance at End of Period
Commercial and industrial:						
Secured	—	$ —	$ —	1	$ 1,196	$ 944
Unsecured	—	—	—	—	—	—
Real estate:						
Secured by commercial properties	1	1,481	1,352	—	—	—
Secured by residential properties	—	—	—	—	—	—
Construction and land development:						
Residential construction loans	—	—	—	—	—	—
Commercial construction loans and land development	1	655	611	—	—	—
Consumer	—	—	—	—	—	—
Broker-dealer	—	—	—	—	—	—
	2	$ 2,136	$ 1,963	1	$ 1,196	$ 944

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An analysis of the aging of the Company’s non-covered loan portfolio is shown in the following tables (in thousands).

December 31, 2017	Loans Past Due 30-59 Days	Loans Past Due 60-89 Days	Loans Past Due 90 Days or More	Total Past Due Loans	Current Loans	PCI Loans	Total Loans	Accruing I (Non-PCI) Past Due 90 Days or
Commercial and industrial:								
Secured	$ 2,060	$ 312	$ 5,714	$ 8,086	$ 1,544,131	$ 6,099	$ 1,558,316	$ 640
Unsecured	642	—	—	642	122,247	—	122,889	—
Real estate:								
Secured by commercial properties	442	—	2,195	2,637	2,213,331	19,675	2,235,643	—
Secured by residential properties	1,490	1,290	418	3,198	762,818	9,865	775,881	—
Construction and land development:								
Residential construction loans	315	—	—	315	176,937	—	177,252	—
Commercial construction loans and land development	1,370	101	—	1,471	782,444	1,438	785,353	—
Consumer	194	20	—	214	40,105	127	40,446	—
Broker-dealer	—	—	—	—	577,889	—	577,889	—
	$ 6,513	$ 1,723	$ 8,327	$ 16,563	$ 6,219,902	$ 37,204	$ 6,273,669	$ 640

December 31, 2016	Loans Past Due 30-59 Days	Loans Past Due 60-89 Days	Loans Past Due 90 Days or More	Total Past Due Loans	Current Loans	PCI Loans	Total Loans	Accruing (Non-PC Past Due 90 Days c
Commercial and industrial:								
Secured	$ 4,727	$ 704	$ 6,770	$ 12,201	$ 1,576,239	$ 8,672	$ 1,597,112	$ 3,095
Unsecured	596	1	909	1,506	97,835	—	99,341	1

Real estate:								
Secured by commercial properties	550	9,417	1,492	11,459	1,915,126	28,510	1,955,095	—
Secured by residential properties	506	361	369	1,236	849,947	10,489	861,672	—
Construction and land development:								
Residential construction loans	—	28	—	28	128,624	—	128,652	—
Commercial construction loans and land development	2,500	1,784	48	4,332	650,399	3,467	658,198	—
Consumer	176	31	—	207	40,851	294	41,352	—
Broker-dealer	—	—	—	—	502,077	—	502,077	—
	$ 9,055	$ 12,326	$ 9,588	$ 30,969	$ 5,761,098	$ 51,432	$ 5,843,499	$ 3,096

In addition to the non-covered loans shown in the table above, PrimeLending had $84.5 million and $44.4 million of loans included in loans held for sale (with an unpaid principal balance of $85.2 million and $44.9 million, respectively) that were 90 days past due and accruing interest at December 31, 2017 and 2016, respectively. These loans are guaranteed by U.S. government agencies and include loans that are subject to repurchase, or have been repurchased, by PrimeLending.

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

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

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

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

Substandard — "Substandard" loans are inadequately protected by the current sound worth and paying capacity of the obligor or the collateral pledged, if any. Loans so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected. Many substandard loans are considered impaired.

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

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

December 31, 2017	Pass	Special Mention	Substandard	PCI	Total
Commercial and industrial:					
Secured	$ 1,483,502	$ 17,354	$ 51,361	$ 6,099	$ 1,558,316
Unsecured	121,774	—	1,115	—	122,889
Real estate:					
Secured by commercial properties	2,154,595	7,647	53,726	19,675	2,235,643
Secured by residential properties	756,091	—	9,925	9,865	775,881
Construction and land development:					
Residential construction loans	177,252	—	—	—	177,252
Commercial construction loans and land development	780,905	2,259	751	1,438	785,353
Consumer	40,211	—	108	127	40,446
Broker-dealer	577,889	—	—	—	577,889
	$ 6,092,219	$ 27,260	$ 116,986	$ 37,204	$ 6,273,669

December 31, 2016	Pass	Special Mention	Substandard	PCI	Total
Commercial and industrial:					

Secured	$ 1,531,895	$ 72	$ 56,473	$ 8,672	$ 1,597,112
Unsecured	97,646	—	1,695	—	99,341
Real estate:					
Secured by commercial properties	1,888,231	3,693	34,661	28,510	1,955,095
Secured by residential properties	846,420	—	4,763	10,489	861,672
Construction and land development:					
Residential construction loans	128,624	—	28	—	128,652
Commercial construction loans and land development	653,808	—	923	3,467	658,198
Consumer	40,789	6	263	294	41,352
Broker-dealer	502,077	—	—	—	502,077
	$ 5,689,490	$ 3,771	$ 98,806	$ 51,432	$ 5,843,499

Allowance for Loan Losses

It is management's responsibility to, at the end of each quarter, or more frequently as deemed necessary, analyze the level of the allowance for loan losses to ensure that it is appropriate for the estimated credit losses in the portfolio. Estimated credit losses are the probable current amount of loans that the Company will be unable to collect given facts and circumstances as of the evaluation date. When management determines that a loan, or portion thereof is uncollectible, the loan, or portion thereof, is charged-off against the allowance for loan losses, or for acquired loans accounted for in pools, charged against either the pool discount or the post-acquisition allowance. Recoveries on charge-offs of loans acquired in the Bank Transactions that occurred prior to their acquisition represent contractual cash flows not expected to be collected and are recorded as accretion income. Recoveries on acquired loans charged-off subsequent

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to their acquisition are credited to the allowance for loan loss, except for recoveries on loans accounted for in pools, which are credited to the pool discount.

The Company has developed a methodology that seeks to determine an allowance within the scope of the Receivables and Contingencies Topics of the ASC. Each of the loans that has been determined to be impaired is within the scope of the Receivables Topic. Impaired loans that are equal to or greater than $0.5 million are individually evaluated using one of three impairment measurement methods as of the evaluation date: (1) the present value of expected future cash flows discounted at the loan's effective rate, (2) the loan's observable market price, or (3) the fair value of the collateral if the loan is collateral dependent. Specific reserves are provided in the estimate of the allowance based on the measurement of impairment under these three methods, except for collateral dependent loans, which require the fair value method. All non-impaired loans are within the scope of the Contingencies Topic. Estimates of loss for the Contingencies Topic are calculated based on historical loss, adjusted for qualitative or environmental factors. The Bank uses a rolling three year average net loss rate to calculate historical loss factors. The analysis is conducted by call report loan category, and further disaggregates commercial and industrial loans by collateral type. The analysis uses net charge-off experience by considering charge-offs and recoveries in determining the loss rate. The historical loss calculation for the quarter is calculated by dividing the current quarter net charge-offs for each loan category by the quarter ended loan category balance. The Bank utilizes a weighted average loss rate to better represent recent trends.

While historical loss experience provides a reasonable starting point for the analysis, historical losses are not the sole basis upon which the Company determines the appropriate level for the allowance for loan losses. Management considers recent qualitative or environmental factors that are likely to cause estimated credit losses associated with the existing portfolio to differ from historical loss experience, including but not limited to:

- changes in the volume and severity of past due, non-accrual and classified loans;
- changes in the nature, volume and terms of loans in the portfolio;
- changes in lending policies and procedures;
- changes in economic and business conditions and developments that affect the collectability of the portfolio;
- changes in lending management and staff;
- changes in the loan review system and the degree of oversight by the Bank's board of directors; and
- any concentrations of credit and changes in the level of such concentrations.

Changes in the volume and severity of past due, non-accrual and classified loans, as well as changes in the nature, volume and terms of loans in the portfolio are key indicators of changes that could indicate a necessary adjustment to

the historical loss factors. The magnitude of the impact of these factors on the qualitative assessment of the allowance for loan loss changes from quarter to quarter.

The loan review program is designed to identify and monitor problem loans by maintaining a credit grading process, requiring that timely and appropriate changes be made to reviewed loans and coordinating the delivery of the information necessary to assess the appropriateness of the allowance for loan losses. Loans are evaluated for impaired status when: (i) payments on the loan are delayed, typically by 90 days or more (unless the loan is both well secured and in the process of collection), (ii) the loan becomes classified, (iii) the loan is being reviewed in the normal course of the loan review scope, or (iv) the loan is identified by the servicing officer as a problem.

In connection with the Bank Transactions, the Bank acquired loans both with and without evidence of credit quality deterioration since origination. PCI loans acquired in the PlainsCapital Merger are accounted for on an individual loan basis, while PCI loans acquired in each of the FNB Transaction and SWS Merger are accounted for in pools as well as on an individual loan basis. Cash flows expected to be collected are recast quarterly for each loan or pool. These evaluations require the continued use and updating of key assumptions and estimates such as default rates, loss severity given default and prepayment speed assumptions (similar to those used for the initial fair value estimate). Management judgment must be applied in developing these assumptions. If expected cash flows for a loan or pool decreases, an increase in the allowance for loan losses is made through a charge to the provision for loan losses. If expected cash flows for a loan or pool increase, any previously established allowance for loan losses is reversed and any remaining difference increases the accretable yield. This increase in accretable yield is taken into income over the remaining life of the loan.

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Loans without evidence of credit impairment at acquisition are subsequently evaluated for any required allowance at each reporting date. An allowance for loan losses is calculated using a methodology similar to that described above for originated loans. The allowance as determined for each loan collateral type is compared to the remaining fair value discount for that loan collateral type. If greater, the excess is recognized as an addition to the allowance through a provision for loan losses. If less than the discount, no additional allowance is recorded. Charge-offs and losses first reduce any remaining fair value discount for the loan and once the discount is depleted, losses are applied against the allowance established for that loan.

The allowance for loan losses is subject to regulatory examinations and determinations as to adequacy, which may take into account such factors as the methodology used to calculate the allowance and the size of the allowance. While the Company believes it has an appropriate allowance for the existing non-covered and covered portfolios at December 31, 2017, additional provisions for losses on existing loans may be necessary in the future.

During 2016, the Bank discovered irregularities in connection with a single loan that was in default. As a result, the Bank increased its provision for loan losses and recorded a $24.5 million charge-off during the second quarter of 2016, representing the entire outstanding principal balance of the loan. During the second quarter of 2017, the Bank recorded other noninterest income of $15.0 million from coverage provided by an insurance policy for forgery of a document delivered in connection with this loan.

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

Year Ended December 31, 2017	Commercial and Industrial	Real Estate	Construction and Land Development	Consumer	Broker-Dealer	Total
Balance, beginning of year	$ 21,369	$ 25,236	$ 7,002	$ 424	$ 155	$ 54,186
Provision charged to operations	6,725	3,619	848	16	198	11,406
Loans charged off	(6,253)	(305)	(13)	(208)	—	(6,779)
Recoveries on charged off loans	1,833	225	7	79	—	2,144
Balance, end of year	$ 23,674	$ 28,775	$ 7,844	$ 311	$ 353	$ 60,957

Commercial and Construction and

Year Ended December 31, 2016	Industrial	Real Estate	Land Development	Consumer	Broker-Dealer	Total
Balance, beginning of year	$ 19,845	$ 18,983	$ 6,064	$ 314	$ 209	$ 45,415
Provision charged to (recapture from) operations	33,369	7,297	938	190	(53)	41,741
Loans charged off	(33,776)	(1,439)	—	(203)	(1)	(35,419)
Recoveries on charged off loans	1,931	395	—	123	—	2,449
Balance, end of year	$ 21,369	$ 25,236	$ 7,002	$ 424	$ 155	$ 54,186

	Commercial and		Construction and			
Year Ended December 31, 2015	Industrial	Real Estate	Land Development	Consumer	Broker-Dealer	Total
Balance, beginning of year	$ 18,833	$ 11,131	$ 6,450	$ 461	$ 166	$ 37,041
Provision charged to (recapture from) operations	4,598	7,937	(386)	104	(80)	12,173
Loans charged off	(7,144)	(605)	—	(378)	—	(8,127)
Recoveries on charged off loans	3,558	520	—	127	123	4,328
Balance, end of year	$ 19,845	$ 18,983	$ 6,064	$ 314	$ 209	$ 45,415

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

December 31, 2017	Commercial and Industrial	Real Estate	Construction and Land Development	Consumer	Broker-Dealer	Total
Loans individually evaluated for impairment	$ 16,819	$ 13,782	$ 611	$ —	$ —	$ 31,212
Loans collectively evaluated for impairment	1,658,287	2,968,202	960,556	40,319	577,889	6,205,253
PCI Loans	6,099	29,540	1,438	127	—	37,204
	$ 1,681,205	$ 3,011,524	$ 962,605	$ 40,446	$ 577,889	$ 6,273,669

December 31, 2016	Commercial and Industrial	Real Estate	Construction and Land Development	Consumer	Broker-Dealer	Total
Loans individually evaluated for impairment	$ 4,508	$ 9,704	$ 727	$ 205	$ —	$ 15,144
Loans collectively evaluated for impairment	1,683,273	2,768,064	782,656	40,853	502,077	5,776,923
PCI Loans	8,672	38,999	3,467	294	—	51,432
	$ 1,696,453	$ 2,816,767	$ 786,850	$ 41,352	$ 502,077	$ 5,843,499

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

December 31, 2017	Commercial and Industrial	Real Estate	Construction and Land Development	Consumer	Broker-Dealer	Total
	$ 365	$ 932	$ 93	$ —	$ —	$ 1,390

Loans individually evaluated for impairment						
Loans collectively evaluated for impairment	23,220	26,127	7,536	293	353	57,529
PCI Loans	89	1,716	215	18	—	2,038
	$ 23,674	$ 28,775	$ 7,844	$ 311	$ 353	$ 60,957

December 31, 2016	Commercial and Industrial	Real Estate	Construction and Land Development	Consumer	Broker-Dealer	Total
Loans individually evaluated for impairment	$ 115	$ —	$ 167	$ —	$ —	$ 282
Loans collectively evaluated for impairment	20,697	23,129	6,458	368	155	50,807
PCI Loans	557	2,107	377	56	—	3,097
	$ 21,369	$ 25,236	$ 7,002	$ 424	$ 155	$ 54,186

6. Covered Assets and Indemnification Asset

The Bank acquired certain assets and assumed certain liabilities of FNB in connection with an FDIC-assisted transaction on September 13, 2013 (the “Bank Closing Date”). As part of the Purchase and Assumption Agreement by and among the FDIC (as receiver of FNB), the Bank and the FDIC (the “P&A Agreement”), the Bank and the FDIC entered into loss-share agreements covering future losses incurred on certain acquired loans and OREO. The Company refers to acquired commercial and single family residential loan portfolios and OREO that are subject to the loss-share agreements as “covered loans” and “covered OREO”, respectively, and these assets are presented as separate line items in the Company’s consolidated balance sheets. Collectively, covered loans and covered OREO are referred to as “covered assets”. Pursuant to the loss-share agreements, the FDIC has agreed to reimburse the Bank the following amounts with respect to the covered assets: (i) 80% of net losses on the first $240.4 million of net losses incurred; (ii) 0% of net losses in excess of $240.4 million up to and including $365.7 million of net losses incurred; and (iii) 80% of net losses in excess of $365.7 million of net losses incurred. Net losses are defined as book value losses plus certain defined expenses incurred in the resolution of assets, less subsequent recoveries. Under the loss-share agreement for commercial assets, the amount of subsequent recoveries that are reimbursable to the FDIC for a particular asset is limited to book value losses and expenses actually billed plus any book value charge-offs incurred prior to the Bank Closing Date. There is no limit on the amount of subsequent recoveries reimbursable to the FDIC under the loss-share agreement for single family residential assets. The loss-share agreements for commercial and single family residential assets are in effect for five years and ten years, respectively, from the Bank Closing Date, and the loss recovery provisions to the FDIC are in effect for eight years and ten years, respectively, from the Bank Closing Date. The asset arising from the loss-share agreements, referred to as the “FDIC Indemnification Asset,” is measured separately from the covered loan portfolio because the agreements are not contractually embedded in the covered loans and are not transferable should the Bank choose to dispose of the covered loans.

In accordance with the loss-share agreements, the Bank may be required to make a “true-up” payment to the FDIC approximately ten years following the Bank Closing Date if its actual net realized losses over the life of the loss-share

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agreements are less than the FDIC's initial estimate of losses on covered assets. The "true-up" payment is calculated using a defined formula set forth in the P&A Agreement. At December 31, 2017, the Bank has recorded a related "true-up" payment accrual of $16.3 million based on the current estimate of aggregate realized losses on covered assets over the life of the loss-share agreements.

Covered Loans and Allowance for Covered Loan Losses

Loans acquired in the FNB Transaction that are subject to a loss-share agreement are referred to as "covered loans" and reported separately in the consolidated balance sheets. Covered loans are reported exclusive of the cash flow reimbursements that may be received from the FDIC.

The Bank's portfolio of acquired covered loans had a fair value of $1.1 billion as of the Bank Closing Date, with no carryover of any allowance for loan losses. Acquired covered loans were preliminarily segregated between those considered to be PCI loans and those without credit impairment at acquisition.

In connection with the FNB Transaction, the Bank acquired loans both with and without evidence of credit quality deterioration since origination. The Company's accounting policies for acquired covered loans, including covered PCI loans, are consistent with the accounting policies for acquired non-covered loans, as described in Note 5 to the consolidated financial statements. The Company has established under its PCI accounting policy a framework to aggregate certain acquired covered loans into various loan pools based on a minimum of two layers of similar risk characteristics for the purpose of determining their respective fair values as of their acquisition dates, and for applying the subsequent recognition and measurement provisions for income accretion and impairment testing.

The following table presents the carrying value of the covered loans summarized by portfolio segment (in thousands).

	December 31,	
	2017	2016
Commercial and industrial	$ 1,055	$ 2,697
Real estate	179,359	244,469
Construction and land development	1,715	8,961
	182,129	256,127
Allowance for covered loans	(2,729)	(413)
Total covered loans, net of allowance	$ 179,400	$ 255,714

The following table presents the carrying value and the outstanding contractual balance of the covered PCI loans (in thousands).

	December 31,	
	2017	2016
Carrying amount	$ 87,113	$ 133,754
Outstanding balance	179,019	266,098

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

	Year Ended December 31,		
	2017	2016	2015
Balance, beginning of period	$ 143,731	$ 176,719	$ 193,493
Reclassifications from nonaccretable difference, net(1)	9,110	41,239	70,884
Transfer of loans to covered OREO(2)	(999)	(487)	(1,309)
Accretion	(60,009)	(73,740)	(86,349)
Balance, end of period	$ 91,833	$ 143,731	$ 176,719

(1) Reclassifications from nonaccretable difference are primarily due to net increases in expected cash flows in the quarterly recasts, but may also include the reclassification and immediate income recognition of nonaccretable difference due to the favorable resolution of loans accounted for individually. Reclassifications to nonaccretable difference occur when accruing loans are moved to non-accrual and expected cash flows are no longer predictable and the accretable yield is eliminated.

(2) Transfer of loans to covered OREO is the difference between the value removed from the pool and the expected cash flows for the loan.

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The remaining nonaccretable difference for covered PCI loans was $72.7 million and $94.5 million at December 31, 2017 and 2016, respectively. During 2017, 2016 and 2015, a combination of factors affecting the inputs to the Bank's quarterly recast process led to the reclassifications from nonaccretable difference to accretable yield. These transfers resulted from revised cash flows that reflect better-than-expected performance of the covered PCI loan portfolio as a result of the Bank's strategic decision to dedicate resources to the liquidation of covered loans during the noted periods.

Covered impaired loans include non-accrual loans, TDRs, PCI loans and partially charged-off loans. The amounts shown in the following tables include Pooled Loans, as well as loans accounted for on an individual basis. For Pooled Loans, the recorded investment with allowance and the related allowance consider impairment measured at the pool level.

Covered impaired loans, segregated between those considered to be PCI loans and those without credit impairment at acquisition, are summarized by class in the following tables (in thousands).

December 31, 2017	Unpaid Contractual Principal Balance	Recorded Investment with No Allowance	Recorded Investment with Allowance	Total Recorded Investment	Related Allowance
PCI					
Commercial and industrial:					
Secured	$ 3,783	$ —	$ 194	$ 194	$ 19
Unsecured	5,732	—	—	—	—
Real estate:					
Secured by commercial properties	80,223	2,388	21,171	23,559	1,817
Secured by residential properties	125,361	249	63,107	63,356	861
Construction and land development:					
Residential construction loans	672	—	—	—	—
Commercial construction loans and land development	11,118	4	—	4	—
	226,889	2,641	84,472	87,113	2,697
Non-PCI					
Commercial and industrial:					
Secured	44	—	—	—	—
Unsecured	—	—	—	—	—
Real estate:					

Secured by commercial properties	—	—	—	—	—
Secured by residential properties	6,279	5,370	—	5,370	—
Construction and land development:					
Residential construction loans	—	—	—	—	—
Commercial construction loans and land development	18	12	—	12	—
	6,341	5,382	—	5,382	—
	$ 233,230	$ 8,023	$ 84,472	$ 92,495	$ 2,697

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Notes to Consolidated Financial Statements (continued)

December 31, 2016	Unpaid Contractual Principal Balance	Recorded Investment with No Allowance	Recorded Investment with Allowance	Total Recorded Investment	Related Allowance
PCI					
Commercial and industrial:					
Secured	$ 10,579	$ 1,024	$ 189	$ 1,213	$ 13
Unsecured	3,259	299	—	299	—
Real estate:					
Secured by commercial properties	143,934	26,415	26,222	52,637	271
Secured by residential properties	148,384	73,240	1,161	74,401	60
Construction and land development:					
Residential construction loans	766	—	—	—	—
Commercial construction loans and land development	23,522	5,204	—	5,204	—
	330,444	106,182	27,572	133,754	344
Non-PCI					
Commercial and industrial:					
Secured	52	52	—	52	—
Unsecured	—	—	—	—	—
Real estate:					
Secured by commercial properties	396	310	—	310	—
Secured by residential properties	4,175	3,537	—	3,537	—
Construction and land development:					
Residential construction loans	—	—	—	—	—
Commercial construction loans and land development	24	20	—	20	—
	4,647	3,919	—	3,919	—
	$ 335,091	$ 110,101	$ 27,572	$ 137,673	$ 344

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

	Year Ended December 31,		
	2017	2016	2015
Commercial and industrial:			
Secured	$ 730	$ 3,530	$ 9,934
Unsecured	150	1,040	4,293

Real estate:			
Secured by commercial properties	38,253	75,159	162,812
Secured by residential properties	73,332	88,794	121,069
Construction and land development:			
Residential construction loans	—	331	1,017
Commercial construction loans and land development	2,620	13,067	33,278
	$ 115,085	$ 181,921	$ 332,403

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

Covered non-accrual loans are summarized by class in the following table (in thousands).

	December 31, 2017	December 31, 2016
Commercial and industrial:		
Secured	$ —	$ 52
Unsecured	—	—
Real estate:		
Secured by commercial properties	—	730
Secured by residential properties	5,087	3,035
Construction and land development:		
Residential construction loans	—	—
Commercial construction loans and land development	17	19
	$ 5,104	$ 3,836

At December 31, 2016, covered non-accrual loans included covered PCI loans of $0.4 million for which discount accretion has been suspended because the extent and timing of cash flows from these covered PCI loans can no longer be reasonably estimated. The amount of such loans included in covered non-accrual loans at December 31, 2017 was nominal.

Interest income, including recoveries and cash payments, recorded on covered impaired loans was $1.3 million, $1.1 million, and $17.2 million during 2017, 2016 and 2015, respectively. Except as noted above, covered PCI loans are considered to be performing due to the application of the accretion method.

The Bank classifies loan modifications of covered loans as TDRs in a manner consistent with that of non-covered loans as discussed in Note 5 to the consolidated financial statements. Information regarding TDRs granted in 2015 is shown in the following table (in thousands). There were no TDRs granted during 2017 or 2016. Pooled Loans are not in the scope of the disclosure requirements for TDRs. At December 31, 2017 and 2016, the Bank had nominal unadvanced commitments to borrowers whose loans have been restructured in TDRs.

	Year Ended December 31, 2015		
	Number of Loans	Balance at Extension	Balance at End of Period

Commercial and industrial:			
Secured	—	$ —	$ —
Unsecured	—	—	—
Real estate:			
Secured by commercial properties	1	573	—
Secured by residential properties	7	860	824
Construction and land development:			
Residential construction loans	—	—	—
Commercial construction loans and land development	—	—	—
	8	$ 1,433	$ 824

During 2015, the covered loan modifications included in the table above included two loans involving payment term extensions, six loans that involved an A/B Note restructure, and six loans that included interest rate adjustments. The Bank did not grant principal reductions on any restructured covered loans.

There were no TDRs granted during the twelve months preceding December 31, 2017 or 2016 for which a payment was at least 30 days past due.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

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

December 31, 2017	Loans Past Due 30 59 Days	Loans Past Due 60 89 Days	Loans Past Due 90 Days or More	Total Past Due Loans	Current Loans	PCI Loans	Total Loans	Accruing Loans (Non PCI) Past 90 Days or More
Commercial and industrial:								
Secured	$ —	$ —	$ —	$ —	$ 861	$ 194	$ 1,055	$ —
Unsecured	—	—	—	—	—	—	—	—
Real estate:								
Secured by commercial properties	209	113	—	322	11,472	23,559	35,353	—
Secured by residential properties	5,624	1,211	3,226	10,061	70,589	63,356	144,006	283
Construction and land development:								
Residential construction loans	—	—	—	—	—	—	—	—
Commercial construction loans and land development	38	—	—	38	1,673	4	1,715	—
	$ 5,871	$ 1,324	$ 3,226	$ 10,421	$ 84,595	$ 87,113	$ 182,129	$ 283

December 31, 2016	Loans Past Due 30 59 Days	Loans Past Due 60 89 Days	Loans Past Due 90 Days or More	Total Past Due Loans	Current Loans	PCI Loans	Total Loans	Accruing Loans (Non PCI) Past 90 Days or More
Commercial and industrial:								
Secured	$ —	$ 6	$ 96	$ 102	$ 1,083	$ 1,213	$ 2,398	$ 44
Unsecured	—	—	—	—	—	299	299	—
Real estate:								
Secured by commercial properties	96	229	—	325	19,132	52,637	72,094	—

Secured by residential properties	3,511	1,345	1,479	6,335	91,639	74,401	172,375	129
Construction and land development:								
Residential construction loans	—	—	—	—	—	—	—	—
Commercial construction loans and land development	15	—	—	15	3,742	5,204	8,961	—
	$ 3,622	$ 1,580	$ 1,575	$ 6,777	$ 115,596	$ 133,754	$ 256,127	$ 173

The Bank assigns a risk grade to each of its covered loans in a manner consistent with the existing loan review program and risk grading matrix used for non-covered loans, as described in Note 5 to the consolidated financial statements. The following tables present the internal risk grades of covered loans in the portfolio by class (in thousands).

December 31, 2017	Pass	Special Mention	Substandard	PCI	Total
Commercial and industrial:					
Secured	$ 429	$ —	$ 432	$ 194	$ 1,055
Unsecured	—	—	—	—	—
Real estate:					
Secured by commercial properties	10,961	—	833	23,559	35,353
Secured by residential properties	68,544	356	11,750	63,356	144,006
Construction and land development:					
Residential construction loans	—	—	—	—	—
Commercial construction loans and land development	1,649	—	62	4	1,715
	$ 81,583	$ 356	$ 13,077	$ 87,113	$ 182,129

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

December 31, 2016	Pass	Special Mention	Substandard	PCI	Total
Commercial and industrial:					
Secured	$ 592	$ —	$ 593	$ 1,213	$ 2,398
Unsecured	—	—	—	299	299
Real estate:					
Secured by commercial properties	17,996	—	1,461	52,637	72,094
Secured by residential properties	90,563	461	6,950	74,401	172,375
Construction and land development:					
Residential construction loans	—	—	—	—	—
Commercial construction loans and land development	2,281	—	1,476	5,204	8,961
	$ 111,432	$ 461	$ 10,480	$ 133,754	$ 256,127

The Bank's impairment methodology for the covered loans is consistent with that of non-covered loans as discussed in Note 5 to the consolidated financial statements. To the extent there is experienced or projected credit deterioration on the acquired covered loan pools subsequent to amounts estimated at the previous quarterly recast date and expected cash flows for a loan or pool decreases, an increase in the allowance for loan losses is made through a charge to the provision for loan losses. If expected cash flows for a loan or pool increase, any previously established allowance for loan losses is reversed and any remaining difference increases the accretable yield. This increase in accretable yield is taken into income over the remaining life of the loan. Additionally, provision for credit losses will be recorded on advances on covered loans subsequent to the acquisition date in a manner consistent with the allowance for non-covered loan losses.

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

Year Ended December 31, 2017	Commercial and Industrial	Real Estate	Construction and Land Development	Total
Balance, beginning of year	$ 35	$ 378	$ —	$ 413
Provision charged to (recaptured from) operations	32	2,840	(7)	2,865
Loans charged off	(49)	(522)	—	(571)
Recoveries on charged off loans	6	6	10	22
Balance, end of year	$ 24	$ 2,702	$ 3	$ 2,729

Year Ended December 31, 2016	Commercial and Industrial	Real Estate	Construction and Land Development	Total

Balance, beginning of year	$ 758	$ 774	$ —	$ 1,532
Provision recaptured from operations	(717)	(351)	(53)	(1,121)
Loans charged off	(6)	(62)	(51)	(119)
Recoveries on charged off loans	—	17	104	121
Balance, end of year	$ 35	$ 378	$ —	$ 413

Year Ended December 31, 2015	Commercial and Industrial	Real Estate	Construction and Land Development	Total
Balance, beginning of year	$ 1,193	$ 3,334	$ 84	$ 4,611
Provision charged to operations	258	189	95	542
Loans charged off	(915)	(2,869)	(179)	(3,963)
Recoveries on charged off loans	222	120	—	342
Balance, end of year	$ 758	$ 774	$ —	$ 1,532

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

December 31, 2017	Commercial and Industrial	Real Estate	Construction and Land Development	Total
Loans individually evaluated for impairment	$ —	$ —	$ —	$ —
Loans collectively evaluated for impairment	861	92,444	1,711	95,016
PCI Loans	194	86,915	4	87,113
	$ 1,055	$ 179,359	$ 1,715	$ 182,129

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

December 31, 2016	Commercial and Industrial	Real Estate	Construction and Land Development	Total
Loans individually evaluated for impairment	$ —	$ —	$ —	$ —
Loans collectively evaluated for impairment	1,185	117,431	3,757	122,373
PCI Loans	1,512	127,038	5,204	133,754
	$ 2,697	$ 244,469	$ 8,961	$ 256,127

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

December 31, 2017	Commercial and Industrial	Real Estate	Construction and Land Development	Total
Loans individually evaluated for impairment	$ —	$ —	$ —	$ —
Loans collectively evaluated for impairment	5	24	3	32
PCI Loans	19	2,678	—	2,697
	$ 24	$ 2,702	$ 3	$ 2,729

December 31, 2016	Commercial and Industrial	Real Estate	Construction and Land Development	Total
Loans individually evaluated for impairment	$ —	$ —	$ —	$ —
Loans collectively evaluated for impairment	22	47	—	69
PCI Loans	13	331	—	344
	$ 35	$ 378	$ —	$ 413

Covered Other Real Estate Owned

A summary of the activity in covered OREO is as follows (in thousands).

Year Ended December 31,

	2017	2016	2015
Balance, beginning of year	$ 51,642	$ 99,090	$ 136,945
Additions to covered OREO	6,700	13,876	50,465
Dispositions of covered OREO	(17,866)	(42,843)	(71,765)
Valuation adjustments in the period	(3,732)	(18,481)	(16,555)
Balance, end of year	$ 36,744	$ 51,642	$ 99,090

During 2017, 2016 and 2015, the Bank wrote down certain covered OREO assets to fair value to reflect new appraisals on certain OREO acquired in the FNB Transaction and OREO acquired from the foreclosure on certain FNB loans acquired in the FNB Transaction. Although the Bank recorded a fair value discount on the acquired assets upon acquisition, in some cases additional downward valuations were required. The downward valuations recorded during the periods presented above were related to covered assets subject to the loss-share agreements with the FDIC.

These additional downward valuation adjustments reflect changes to the assumptions regarding the fair value of the OREO, including in some cases the intended use of the OREO, due to the availability of more information as well as the passage of time. The process of determining fair value is subjective in nature and requires the use of significant estimates and assumptions. Although the Bank makes market-based assumptions when valuing acquired assets, new information may come to light that causes estimates to increase or decrease. When the Bank determines, based on subsequent information, that its estimates require adjustment, the Bank records the adjustment. The accounting for such adjustments requires that the decreases to fair value be recorded at the time such new information is received, while increases to fair value are recorded when the asset is subsequently sold.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

FDIC Indemnification Asset

A summary of the activity in the FDIC Indemnification Asset is as follows (in thousands).

	Year Ended December 31,		
	2017	2016	2015
Balance, beginning of year	$ 71,313	$ 91,648	$ 130,437
FDIC Indemnification Asset accretion (amortization)	(17,083)	242	1,147
Transfers to due from FDIC and other	(24,890)	(20,577)	(39,936)
Balance, end of year	$ 29,340	$ 71,313	$ 91,648

As of December 31, 2017, the Bank had billed $147.8 million to and collected $145.8 million from the FDIC, which represented reimbursable covered losses and expenses through September 30, 2017. During 2017, the Bank recorded $17.1 million of amortization related to the FDIC Indemnification Asset due to lower than projected collections from the FDIC than originally estimated at the Bank Closing Date.

7. Cash and Due from Banks

Cash and due from banks consisted of the following (in thousands).

	December 31,	
	2017	2016
Cash on hand	$ 44,765	$ 49,152
Clearings and collection items	92,271	78,328
Deposits at Federal Reserve Bank	248,442	354,948
Deposits at Federal Home Loan Bank	1,501	4,237
Deposits in FDIC-insured institutions	99,998	182,692
	$ 486,977	$ 669,357

The amounts above include interest-bearing deposits of $302.2 million and $479.3 million at December 31, 2017 and 2016, respectively. Cash on hand and deposits at the Federal Reserve Bank satisfy regulatory reserve requirements at December 31, 2017.

8. Premises and Equipment

The components of premises and equipment are summarized as follows (in thousands).

	December 31,	
	2017	2016
Land and premises	$ 111,203	$ 111,295
Furniture and equipment	207,552	190,914
	318,755	302,209
Less accumulated depreciation and amortization	(141,178)	(111,848)
	$ 177,577	$ 190,361

The amounts shown above include gross assets recorded under capital leases of $8.4 million and $8.4 million, with accumulated amortization of $3.3 million and $2.5 million at December 31, 2017 and 2016, respectively.

Occupancy expense was reduced by rental income of $1.8 million, $2.0 million and $2.2 million during 2017, 2016 and 2015, respectively. Depreciation and amortization expense on premises and equipment, which includes amortization of capital leases, amounted to $34.6 million, $35.4 million and $37.2 million during 2017, 2016 and 2015, respectively.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

9. Goodwill and Other Intangible Assets

At both December 31, 2017 and 2016, the carrying amount of goodwill of $251.8 million was comprised of $24.0 million recorded in connection with the acquisition of NLC and $227.8 million recorded in connection with the PlainsCapital Merger.

Other intangible assets of $36.4 million and $44.7 million at December 31, 2017 and 2016, respectively, include an indefinite lived intangible asset with an estimated fair value of $3.0 million related to state licenses acquired as a part of the NLC acquisition in January 2007.

The Company performed required annual impairment tests of its goodwill and other intangible assets having an indefinite useful life as of October 1st for each of its reporting units. At October 1, 2017, the Company determined that the estimated fair value of each of its reporting units exceeded its carrying value. The Company estimated the fair values of its reporting units based on both a market and income approach using historical, normalized actual and forecasted results. Based on this evaluation, the Company concluded that the goodwill and other identifiable intangible assets were fully realizable.

The Company's evaluation includes multiple assumptions, including estimated discounted cash flows and other estimates that may change over time. If future discounted cash flows become less than those projected by the Company, future impairment charges may become necessary that could have a materially adverse impact on the Company's results of operations and financial condition. As quoted market prices in active stock markets are relevant evidence of fair value, a significant decline in the Company's common stock trading price may indicate an impairment of goodwill.

Based on the results of the previously noted annual quantitative analysis as of October 1, 2017, the fair values of each of the Company's reporting units indicated no impairment of goodwill. This analysis and the resulting estimated fair value of the insurance reporting unit exceeded the carrying value by approximately 12%, which represented a decline in the estimated excess fair value over carrying value from recent annual goodwill assessments. This decrease in the excess fair value over carrying value from the 2016 assessment to the 2017 assessment was primarily a result of a reduction in projected discounted cash flows driven by the insurance reporting unit's current operating performance being below expectations, which was primarily attributable to catastrophic and sub-catastrophic weather-related events which occurred in 2017. In the event future operating performance is below management's forecasted projections, there are negative changes to long-term growth rates or discount rates increase, the fair value of the insurance reporting unit may decline and the Company may be required to record a goodwill impairment charge.

The carrying value of intangible assets subject to amortization was as follows (in thousands).

December 31, 2017	Estimated Useful Life (Years)	Gross Intangible Assets	Accumulated Amortization	Net Intangible Assets
Core deposits	4 - 12	$ 38,930	$ (26,381)	$ 12,549
Trademarks and trade names	15 - 20	20,000	(7,860)	12,140
Noncompete agreements	4 - 6	11,650	(10,529)	1,121
Customer contracts and relationships	12 - 14	21,400	(13,906)	7,494
Agent relationships	13	3,600	(3,472)	128
		$ 95,580	$ (62,148)	$ 33,432

December 31, 2016	Estimated Useful Life (Years)	Gross Intangible Assets	Accumulated Amortization	Net Intangible Assets
Core deposits	4 - 12	$ 38,930	$ (22,255)	$ 16,675
Trademarks and trade names	15 - 20	20,000	(6,877)	13,123
Noncompete agreements	4 - 6	11,650	(9,306)	2,344
Customer contracts and relationships	12 - 14	21,400	(12,097)	9,303
Agent relationships	13	3,600	(3,350)	250
		$ 95,580	$ (53,885)	$ 41,695

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Hilltop Holdings Inc. and Subsidiaries
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Amortization expense related to intangible assets during 2017, 2016 and 2015 was $8.3 million, $10.2 million and $12.4 million, respectively.

The estimated aggregate future amortization expense for intangible assets at December 31, 2017 is as follows (in thousands).

2018	$ 7,289
2019	5,142
2020	4,352
2021	3,607
2022	3,222
Thereafter	9,820
	$ 33,432

10. Mortgage Servicing Rights

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

	Year Ended December 31,		
	2017	2016	2015
Balance, beginning of year	$ 61,968	$ 52,285	$ 36,155
Additions	16,401	23,381	24,974
Sales	(17,499)	(7,586)	—
Changes in fair value:			
Due to changes in model inputs or assumptions (1)	(1,722)	(153)	(2,150)
Due to customer payoffs	(4,434)	(5,959)	(6,694)
Balance, end of year	$ 54,714	$ 61,968	$ 52,285

	December 31,	
	2017	2016
Mortgage loans serviced for others	$ 4,762,042	$ 5,480,943
MSR asset as a percentage of serviced mortgage loans	1.15 %	1.13 %

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

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

	December 31,	
	2017	2016
Weighted average constant prepayment rate	10.93 %	10.47 %
Weighted average discount rate	11.03 %	10.95 %
Weighted average life (in years)	6.9	6.9

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

	December 31,	
	2017	2016
Constant prepayment rate:		
Impact of 10% adverse change	$ (1,948)	$ (2,297)
Impact of 20% adverse change	(3,839)	(4,471)
Discount rate:		
Impact of 10% adverse change	(2,135)	(2,539)
Impact of 20% adverse change	(4,103)	(4,882)

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

Contractually specified servicing fees, late fees and ancillary fees earned of $20.7 million, $23.8 million and $19.6 million during 2017, 2016 and 2015, respectively, were included in other noninterest income within the consolidated statements of operations.

11. Deposits

Deposits are summarized as follows (in thousands).

	December 31,	
	2017	2016
Noninterest-bearing demand	$ 2,411,849	$ 2,199,483
Interest-bearing:		
NOW accounts	1,202,752	1,252,832
Money market	2,222,555	1,626,218
Brokered - money market	101,624	125,272
Demand	411,771	384,847
Savings	218,812	279,911
Time	1,313,482	1,145,859
Brokered - time	95,274	49,389
	$ 7,978,119	$ 7,063,811

At December 31, 2017, deposits include $778.8 million of time deposit accounts that meet or exceed the FDIC insurance limit of $250,000. Scheduled maturities of interest-bearing time deposits at December 31, 2017 are as follows (in thousands).

2018	$ 791,721
2019	509,244

2020	82,839
2021	15,155
2022 and thereafter	9,797
	$ 1,408,756

12. Short-term Borrowings

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

	December 31,	
	2017	2016
Federal funds purchased	$ 101,775	$ 87,125
Securities sold under agreements to repurchase	539,149	195,164
Federal Home Loan Bank	250,000	1,000,000
Short-term bank loans	315,500	135,000
	$ 1,206,424	$ 1,417,289

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

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

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

	Year Ended December 31,		
	2017	2016	2015
Average balance during the year	$ 588,847	$ 368,102	$ 315,904
Average interest rate during the year	1.06 %	0.58 %	0.33 %
Maximum month-end balance during the year	904,704	520,715	514,776

	December 31,	
	2017	2016
Average interest rate at end of year	1.21 %	0.42 %
Securities underlying the agreements at end of year:		
Carrying value	$ 581,636	$ 209,877
Estimated fair value	$ 598,300	$ 206,641

FHLB short-term borrowings mature over terms not exceeding 365 days and are collateralized by FHLB Dallas stock, nonspecified real estate loans and certain specific commercial real estate loans. At December 31, 2017, the Bank had available collateral of $3.3 billion, substantially all of which was blanket collateral. Other information regarding FHLB short-term borrowings is shown in the following tables (dollars in thousands).

	Year Ended December 31,		
	2017	2016	2015
Average balance during the year	$ 390,616	$ 361,475	$ 294,959
Average interest rate during the year	1.08 %	0.46 %	0.27 %
Maximum month-end balance during the year	$ 850,000	$ 1,000,000	$ 600,000

	December 31,	
	2017	2016
Average interest rate at end of year	1.30 %	0.55 %

The Hilltop Broker-Dealers use short-term bank loans periodically to finance securities owned, margin loans to customers and correspondents, and underwriting activities. Interest on the borrowings varies with the federal funds rate. The weighted average interest rate on the borrowings at December 31, 2017 and 2016 was 2.27% and 1.59%, respectively.

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Hilltop Holdings Inc. and Subsidiaries
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13. Notes Payable

Notes payable consisted of the following (in thousands).

	December 31,	
	2017	2016
Senior Notes due April 2025, net of discount of $1,545 and $1,689, respectively	$ 148,455	$ 148,311
FHLB notes, net of premium of $436 and $948, respectively, with maturities ranging from February 2018 to June 2030 and interest payable monthly	19,402	102,596
Insurance company note payable due March 2035, paid off in June 2017	—	20,000
NLIC note payable due May 2033, three-month LIBOR plus 4.10% (5.71% at December 31, 2017) with interest payable quarterly	10,000	10,000
NLIC note payable due September 2033, three-month LIBOR plus 4.05% (5.66% at December 31, 2017) with interest payable quarterly	10,000	10,000
ASIC note payable due April 2034, three-month LIBOR plus 4.05% (5.66% at December 31, 2017) with interest payable quarterly	7,500	7,500
Insurance company line of credit due December 30, 2018, 3.25% plus a calculated index rate (4.00% at December 31, 2017) with interest payable quarterly	1,000	3,000
Ventures Management lines of credit, with interest payable monthly	12,452	16,505
	$ 208,809	$ 317,912

Senior Notes

On April 9, 2015, Hilltop completed an offering of $150.0 million aggregate principal amount of its 5% senior notes due 2025 (“Senior Unregistered Notes”) in a private offering that was exempt from the registration requirements of the Securities Act of 1933, as amended (the “Securities Act”). The Senior Unregistered Notes were offered within the United States only to qualified institutional buyers pursuant to Rule 144A under the Securities Act, and to persons outside of the United States under Regulation S under the Securities Act. The Senior Unregistered Notes were issued pursuant to an indenture, dated as of April 9, 2015, by and between Hilltop and U.S. Bank National Association, as trustee. The net proceeds from the offering, after deducting estimated fees and expenses and the initial purchasers’ discounts, were approximately $148 million. Hilltop used the net proceeds of the offering to redeem all of Hilltop’s outstanding Non-Cumulative Perpetual Preferred Stock, Series B at an aggregate liquidation value of $114.1 million, plus accrued but unpaid dividends of $0.4 million, and Hilltop utilized the remainder for general corporate purposes. Unamortized debt issuance costs presented as a reduction from the Senior Notes are discussed further in Note 1 to the consolidated financial statements.

In connection with the issuance of the Senior Unregistered Notes, on April 9, 2015, the Company entered into a registration rights agreement with the initial purchasers of the Senior Unregistered Notes. Under the terms of the registration rights agreement, the Company agreed to offer to exchange the Senior Unregistered Notes for notes registered under the Securities Act (the “Senior Registered Notes”). The terms of the Senior Registered Notes are substantially identical to the Senior Unregistered Notes for which they were exchanged (including principal amount, interest rate, maturity and redemption rights), except that the Senior Registered Notes generally are not subject to transfer restrictions. On May 22, 2015 and subject to the terms and conditions set forth in the Senior Registered Notes prospectus, the Company commenced an offer to exchange the Senior Unregistered Notes for Senior Registered Notes. Substantially all of the Senior Unregistered Notes were tendered in the exchange offer, and on June 22, 2015, the Company fulfilled its requirements under the registration rights agreement for the Senior Unregistered Notes by issuing Senior Registered Notes in exchange for the tendered Senior Unregistered Notes. The Senior Registered Notes and the Senior Unregistered Notes that remain outstanding are collectively referred to as the “Senior Notes.”

The Senior Notes bear interest at a rate of 5% per year, payable semi-annually in arrears in cash on April 15 and October 15 of each year. The Senior Notes will mature on April 15, 2025, unless Hilltop redeems the Senior Notes, in whole at any time or in part from time to time, on or after January 15, 2025 (three months prior to the maturity date of the Senior Notes) at its election at a redemption price equal to 100% of the principal amount of the Senior Notes to be redeemed plus accrued and unpaid interest to, but excluding, the redemption date.

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The indenture contains covenants that limit the Company's ability to, among other things and subject to certain significant exceptions: (i) dispose of or issue voting stock of certain of the Company's bank subsidiaries or subsidiaries that own voting stock of the Company's bank subsidiaries, (ii) incur or permit to exist any mortgage, pledge, encumbrance or lien or charge on the capital stock of certain of the Company's bank subsidiaries or subsidiaries that own capital stock of the Company's bank subsidiaries and (iii) sell all or substantially all of the Company's assets or merge or consolidate with or into other companies. The indenture also provides for certain events of default, which, if any of them occurs, would permit or require the principal amount, premium, if any, and accrued and unpaid interest on the then outstanding Senior Notes to be declared immediately due and payable.

Federal Home Loan Bank notes

The FHLB notes, assumed by the Bank in the SWS Merger, have interest rates ranging from 1.19% to 5.70%, with a weighted average interest rate of 2.10% at December 31, 2017. The FHLB notes, as well as other borrowings from the FHLB, are collateralized by FHLB stock, a blanket lien on commercial and real estate loans, as well as by the amount of securities that are in safekeeping at the FHLB, the value of which was $3.3 billion at December 31, 2017.

NLIC, ASIC and Insurance Company Notes Payable

On June 14, 2017, NLC paid off the $20.0 million insurance company note payable due March 2035.

The NLIC and ASIC notes payable to unaffiliated companies are each subordinated in right of payment to all policy claims and other indebtedness of NLIC and ASIC, respectively. Further, all payments of principal and interest require the prior approval of the Insurance Commissioner of the State of Texas and are only payable to the extent that the statutory surplus of NLIC exceeds $30 million and ASIC exceeds $15 million.

The NLIC and ASIC loan agreements relating to the notes payable contain various covenants pertaining to limitations on additional debt, dividends, officer and director compensation, and minimum capital requirements. The Company was in compliance with the covenants at December 31, 2017.

NLC has entered into an indenture relating to the NLIC and ASIC notes payable which provides that (i) if a person or group becomes the beneficial owner directly or indirectly of 50% or more of its equity securities and (ii) if NLC's ratings are downgraded by a nationally recognized statistical rating organization (as defined in the Securities

Exchange Act of 1934, as amended (the “Exchange Act”), then each holder of the notes governed by such indenture has the right to require that NLC purchase such holder’s notes in whole or in part at a price equal to 100% of the outstanding principal amount.

Insurance Company Line of Credit

The Company’s insurance subsidiary has a line of credit with a financial institution which allows for borrowings by NLC of up to $7.5 million and is collateralized by substantially all of NLC’s assets. The loan agreements relating to the line of credit contain various financial and other covenants which must be maintained until all indebtedness to the financial institution is repaid. The Company was in compliance with the covenants at December 31, 2017.

Ventures Management Lines of Credit

At December 31, 2017, Ventures Management’s ABAs had combined available lines of credit totaling $70.0 million, $30.0 million of which was with a single unaffiliated bank, while $40.0 million was with the Bank. At December 31, 2017, the outstanding balance of $12.5 million was related to a single line of credit with an unaffiliated bank with a stated interest rate of the greater of a calculated index rate on mortgage notes or 2.75%. The calculated index rate on mortgage notes held at December 31, 2017 was 3.09%. The Ventures Management lines of credit are collateralized by mortgage notes, and the loan agreements relating to the lines of credit contain various financial and other covenants which must be maintained until all indebtedness to the financial institution is repaid. The Company was in compliance with the covenants at December 31, 2017.

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Scheduled Maturities

Scheduled maturities for notes payable outstanding at December 31, 2017 are as follows (in thousands).

2018	$ 25,791
2019	—
2020	3,425
2021	508
2022	203
Thereafter	179,991
	$ 209,918

14. Junior Subordinated Debentures and Trust Preferred Securities

PCC has four statutory Trusts, three of which were formed under the laws of the state of Connecticut and one of which, PCC Statutory Trust IV, was formed under the laws of the state of Delaware. The Trusts were created for the sole purpose of issuing and selling preferred securities and common securities, using the resulting proceeds to acquire junior subordinated debentures issued by PCC (the "Debentures"). Accordingly, the Debentures are the sole assets of the Trusts, and payments under the Debentures are the sole revenue of the Trusts. All of the common securities are owned by PCC; however, PCC is not the primary beneficiary of the Trusts. Accordingly, the Trusts are not included in the Company's consolidated financial statements.

The Trusts have issued $65,000,000 of floating rate preferred securities and $2,012,000 of common securities and have invested the proceeds from the securities in floating rate Debentures of PCC.

Information regarding the PCC Debentures is shown in the following table (in thousands).

Investor	Issue Date	Amount
PCC Statutory Trust I	July 31, 2001	$ 18,042

PCC Statutory Trust II	March 26, 2003	$ 18,042
PCC Statutory Trust III	September 17, 2003	$ 15,464
PCC Statutory Trust IV	February 22, 2008	$ 15,464

The stated term of the Debentures is 30 years with interest payable quarterly. The rate on the Debentures, which resets quarterly, is 3-month LIBOR plus an average spread of 3.22%. The total average interest rate at December 31, 2017 was 4.72%. The term, rate and other features of the preferred securities are the same as the Debentures. PCC's obligations under the Debentures and related documents, taken together, constitute a full and unconditional guarantee of the Trust's obligations under the preferred securities.

15. Income Taxes

The significant components of the income tax provision are as follows (in thousands).

	Year Ended December 31,		
	2017	2016	2015
Current:			
Federal	$ 63,769	$ 82,970	$ 49,570
State	5,440	10,181	3,969
	69,209	93,151	53,539
Deferred:			
Federal	40,176	(6,732)	17,295
State	757	(2,958)	81
	40,933	(9,690)	17,376
	$ 110,142	$ 83,461	$ 70,915

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The income tax provision differs from the amount that would be computed by applying the statutory Federal income tax rate of 35% to income before income taxes as a result of the following (in thousands).

	Year Ended December 31,		
	2017	2016	2015
Computed tax at federal statutory rate	$ 85,150	$ 80,992	$ 99,223
Tax effect of:			
Tax Legislation	28,363	—	—
Non-taxable acquisition gain	(6,682)	—	(33,426)
Nondeductible transaction costs	774	2,608	3,969
Nondeductible expenses	3,089	3,301	3,215
State income taxes	4,028	4,708	2,632
Tax-exempt income, net	(2,758)	(2,850)	(2,563)
Valuation allowance	—	(2,094)	(1,889)
Share-based compensation benefit	(412)	(2,391)	—
Other	(1,410)	(813)	(246)
	$ 110,142	$ 83,461	$ 70,915

The components of the tax effects of temporary differences that give rise to the net deferred tax asset included in other assets within the consolidated balance sheets are as follows (in thousands).

	December 31,	
	2017	2016
Deferred tax assets:		
Net operating and built-in loss carryforward	$ 11,697	$ 21,381
Covered loans	20,024	43,512
Purchase accounting adjustment - loans	4,859	10,682
Allowance for loan losses	15,105	20,703
Compensation and benefits	15,860	44,368
Legal and other reserves	4,359	15,985
Foreclosed property	6,400	16,486
Other	11,961	19,297
	90,265	192,414
Deferred tax liabilities:		
Premises and equipment	10,288	21,013
FDIC Indemnification Asset	3,502	21,600
Intangible assets	8,994	17,392
Derivatives	4,527	8,581
Loan servicing	13,184	23,187

Other	8,156	18,868
	48,651	110,641
Net deferred tax asset	$ 41,614	$ 81,773

The Tax Legislation enacted on December 22, 2017 significantly revises the U.S. corporate income tax by lowering corporate income tax rates. The Company's results during the fourth quarter and full year of 2017 include the estimated impact of a non-recurring, non-cash charge of $28.4 million as a result of the enactment of the Tax Legislation. The charge was primarily due to the revaluation of deferred tax assets as a result of the reduction in the corporate tax rate from 35% to 21%, and other anticipated impacts associated with the Tax Legislation. Certain Tax Legislation amounts are considered reasonable estimates as of December 31, 2017 and could be adjusted during the measurement period, which will end in December 2018, as a result of further refinement of calculations, changes in interpretations and assumptions made, guidance that may be issued and actions the Company may take as a result of the Tax Legislation.

The Company's effective tax rate was 45.3%, 36.1% and 25.0% during 2017, 2016 and 2015, respectively. The effective tax rate during 2017 was higher than the statutory rate primarily due to the revaluation of deferred tax assets as a result of the Tax Legislation, partially offset by a non-taxable gain recorded in the resolution of the SWS appraisal proceedings as the SWS Merger was a tax-free reorganization. The effective tax rate during 2016 was relatively consistent with the

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

statutory rate, but did include effects related to non-deductible transaction costs associated with the SWS Merger, offset by the reversal of a valuation allowance of $2.2 million previously established on a deferred tax asset associated with the SWS Merger and the recognition of excess tax benefits on share-based payment awards as a result of the Company's adoption of the provisions of Accounting Standards Update ("ASU") 2016-09 as of January 1, 2016 as discussed in Note 33 to the consolidated financial statements. The lower effective tax rate during 2015 was primarily due to no income taxes being recorded during 2015 in connection with the bargain purchase gain of $81.3 million associated with the SWS Merger. In addition, during 2015, the Company recorded an income tax benefit of $2.1 million as a result of the SWS Merger to reverse the deferred tax liability for the difference between book and tax basis on Hilltop's investment in SWS common stock and also reversed a valuation allowance of $1.9 million previously established on a deferred tax asset for a capital loss carryforward.

At December 31, 2017 and 2016, the Company had net operating loss carryforwards for Federal income tax purposes of $29.9 million and $37.8 million, respectively (or $6.3 million and $13.2 million, respectively, on a tax effected basis at applicable rates for respective tax years). The net operating loss carryforwards are subject to an annual Section 382 limitation on their usage. These net operating loss carryforwards expire in starting in 2032. The Company expects to realize its current deferred tax asset for these net operating loss carryforwards through the implementation of certain tax planning strategies, core earnings, and reversal of timing differences. At December 31, 2017, the Company also had a recognized built-in loss ("RBIL") carryover of $20.5 million from the ownership change resulting from the SWS Merger. These RBILs, if recognized during a five year recognition period before January 1, 2020, are subject to the annual Section 382 limitation rules similar to the Company's net operating loss carryforwards. The RBIL's are expected to be fully realized prior to any expiration. The Company's remaining net unrealized built-in loss of $9.8 million, if recognized during a five year recognition period before January 1, 2020, would also be subject to the Section 382 limitation.

Based on the Company's evaluation of its deferred tax assets, management determined that no valuation allowance against its gross deferred tax assets was necessary at December 31, 2017 or 2016.

GAAP requires the measurement of uncertain tax positions. Uncertain tax positions are the difference between a tax position taken, or expected to be taken in a tax return, and the benefit recognized for accounting purposes. At December 31, 2017 and 2016, the total amount of gross unrecognized tax benefits was $1.6 million and $1.7 million, respectively, of which $1.2 million and $1.1 million, respectively, if recognized, would favorably impact the Company's effective tax rate. The aggregate changes in gross unrecognized tax benefits, which excludes interest and penalties, are as follows (in thousands).

	Year Ended December 31,		
	2017	2016	2015
Balance, beginning of year	$ 1,704	$ 644	$ 644

Increases related to tax positions taken during a prior year	476	844	—
Decreases related to tax positions taken during a prior year	(1,273)	—	—
Increases related to tax positions taken during the current year	667	216	—
Balance, end of year	$ 1,574	$ 1,704	$ 644

The Company believes that it is reasonably possible that certain state matters may be concluded in the next twelve months. Specific positions that may be resolved include issues involving apportionment and various other matters. At December 31, 2017, the unrecognized tax benefit is recorded as taxes receivable, which is included in other assets within the consolidated balance sheet.

The Company files income tax returns in U.S. federal and numerous state jurisdictions. The Company is subject to tax audits in numerous jurisdictions in the United States until the applicable statute of limitations expires. The Company is no longer subject to U.S. federal tax examinations for tax years prior to 2014. The Company is open for various state tax audits for tax years 2013 and later. The Company is currently under income tax examination by a state authority for tax years 2013 through 2015. As of December 31, 2017, the state authority has not proposed any significant adjustments to the Company's tax positions for which the Company does not have adequate reserves.

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16. Employee Benefits

Hilltop and its subsidiaries have benefit plans that provide for elective deferrals by employees under Section 401(k) of the Internal Revenue Code. Employee contributions are determined by the level of employee participation and related salary levels per Internal Revenue Service regulations. Hilltop and its subsidiaries match a portion of employee contributions based on the amount of eligible employees' contributions and salaries. In addition, Hilltop, PCC and the Bank made additional contributions to employees' 401(k) accounts based on achievement of certain corporate objectives through December 31, 2015. The amount charged to operating expense for these matching contributions totaled $13.9 million, $15.1 million and $12.6 million during 2017, 2016 and 2015, respectively.

Effective upon the completion of the PlainsCapital Merger, the Company recorded a liability of $8.9 million associated with separate retention agreements entered into between Hilltop and two executive officers. At December 31, 2017 and 2016, the recorded liability, including interest, was $9.1 million and $9.0 million, respectively.

The Bank purchased $15.0 million of flexible premium universal life insurance in 2001 to help finance the annual expense incurred in providing various employee benefits. At December 31, 2017 and 2016, the carrying value of the policies included in other assets was $25.8 million and $24.8 million, respectively. During 2017, 2016 and 2015, the Bank recorded income of $0.6 million, $0.6 million and $0.8 million, respectively, related to the policies that was reported in other noninterest income within the consolidated statement of operations.

Deferred Compensation Plan

As a result of the SWS Merger, the Company assumed a deferred compensation plan (the "SWS Plan") that allows former SWS eligible officers and employees to defer a portion of their bonus compensation and commissions. The SWS Plan matched 15% of the deferrals made by participants up to a predetermined limit through matching contributions that vest ratably over four years. Pursuant to the terms of the SWS Plan, the trustee periodically purchased the former SWS common stock in the open market. As a result of the SWS Merger, the former SWS common shares were converted into Hilltop common stock based on the terms of the merger agreement. No further contributions can be made to this plan.

The assets of the SWS Plan are held in a rabbi trust and primarily include investments in company-owned life insurance ("COLI") and Hilltop common stock. These assets are consolidated with those of the Company. Investments in COLI are carried at the cash surrender value of the insurance policies and recorded in other assets within the consolidated balance sheet at December 31, 2017 and 2016, respectively. Investments in Hilltop common stock, which

are carried at cost, and the corresponding liability related to the deferred compensation plan are presented as components of stockholders' equity as employee stock trust and deferred compensation employee stock trust, net, respectively, at December 31, 2017 and 2016, respectively.

17. Related Party Transactions

Pursuant to a Sublease Agreement, Diamond A Administration Company LLC ("Diamond A Admin"), an affiliate of Gerald J. Ford, the current Chairman of the Board of Hilltop and the beneficial owner of 16.2% of Hilltop common stock at December 31, 2017, currently provides office space to Hilltop at a cost of $24 thousand per month. This Sublease Agreement continues in effect until July 31, 2018 or such earlier date that the base lease expires.

Jeremy B. Ford, a director and the President and Co-Chief Executive Officer of Hilltop, is the beneficiary of a trust that owns a 49% limited partnership interest in Diamond A Financial, L.P. Diamond A Financial, L.P. owned 16.2% of the outstanding Hilltop common stock at December 31, 2017. He also is a director and the Secretary of Diamond A Admin, which provides office space to Hilltop as described in the preceding paragraph. Diamond A Admin is owned by Hunter's Glen/Ford, Ltd., a limited partnership in which a trust for the benefit of Jeremy B. Ford is a 46% limited partner.

Jeremy B. Ford is the son of Gerald J. Ford. Corey G. Prestidge, Hilltop's General Counsel and Secretary, is the son-in-law of Gerald J. Ford. Accordingly, Messrs. Jeremy Ford and Corey Prestidge are brothers-in-law.

In the ordinary course of business, the Bank has granted loans to certain directors, executive officers and their affiliates (collectively referred to as related parties) totaling $34.6 million and $27.3 million at December 31, 2017 and 2016, respectively. These loans were made on substantially the same terms, including interest rates and collateral, as those

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prevailing at the time for comparable transactions with other unaffiliated persons and do not involve more than normal risk of collectability. For such loans during 2017, total principal additions were $12.0 million and total principal payments were $4.7 million.

At December 31, 2017 and 2016, the Bank held deposits of related parties of $151.0 million and $154.8 million, respectively.

A related party is the lessor in an operating lease with the Bank. The Bank’s minimum payment under the lease is $0.5 million annually through 2028, for an aggregate remaining obligation of $5.5 million at December 31, 2017.

The Bank purchases loans from a company for which a related party serves as a director, president and chief executive officer. At December 31, 2017 and 2016, the outstanding balance of the purchased loans was $2.1 million and $3.0 million, respectively. The loans were purchased with recourse to the Company in the ordinary course of business and the related party had no direct financial interest in the transaction.

18. Commitments and Contingencies

The Bank acts as agent on behalf of certain correspondent banks in the purchase and sale of federal funds that aggregated $3.0 million and $19.0 million at December 31, 2017 and 2016, respectively.

Legal Matters

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

as the estimates themselves will be adjusted, accordingly.

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

Following completion of Hilltop's acquisition of SWS, several purported holders of shares of SWS common stock (the "Petitioners") filed petitions in the Court of Chancery of the State of Delaware (the "Court") seeking appraisal for their shares pursuant to Section 262 of the Delaware General Corporation Law. These petitions were consolidated as In re SWS Group, Inc., C.A. No. 10554-VCG. On May 30, 2017, the Court issued its Memorandum Opinion in the matter. The Court found the "fair value" of the shares of SWS common stock as of the date of the transaction was $6.38 per share. Accordingly, Hilltop paid cash of $6.38 per share, plus statutory interest from the effective date of the merger until the date of payment, to the Petitioners and the other stockholders of SWS who properly demanded appraisal rights under Delaware law, collectively representing 7,438,453 shares. Each outstanding share of SWS common stock, other than shares held by Hilltop, in treasury by SWS or by stockholders who properly demanded appraisal rights under Delaware law, was converted into the right to receive 0.2496 shares of Hilltop common stock and $1.94 in cash, the aggregate value of which was $6.92 per share of SWS common stock as of the effective date of the merger. The

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resolution of this matter resulted in 1,856,638 shares of HTH common stock, which had been held in escrow during the pendency of the proceeding, being returned to the Company’s pool of authorized but unissued shares of common stock and a pre-tax net increase to other noninterest income of $11.6 million during the second quarter of 2017. This change in common stock is reflected in repurchases of common stock within the consolidated statements of stockholders’ equity. Petitioners filed an appeal to the Court’s Memorandum Opinion. The Company also filed a cross-appeal in the matter and intends to vigorously defend the Petitioners’ appeal.

The Company is involved in information-gathering requests and investigations (both formal and informal), as well as reviews, examinations and proceedings (collectively, “Inquiries”) by various governmental regulatory agencies, law enforcement authorities and self-regulatory bodies regarding certain of its businesses, business practices and policies, as well as the conduct of persons with whom it does business. Additional Inquiries will arise from time to time. In connection with those Inquiries, the Company receives document requests, subpoenas and other requests for information. The Inquiries, including the Inquiry described below, could develop into administrative, civil or criminal proceedings or enforcement actions that could result in consequences that have a material effect on the Company's consolidated financial position, results of operations or cash flows as a whole. Such consequences could include adverse judgments, findings, settlements, penalties, fines, orders, injunctions, restitution, or alterations in the Company’s business practices, and could result in additional expenses and collateral costs, including reputational damage.

As a part of an industry-wide Inquiry, PrimeLending received a subpoena from the Office of Inspector General of the U.S. Department of Housing and Urban Development (“HUD”) regarding mortgage-related practices, including those relating to origination practices for loans insured by the Federal Housing Administration (the “FHA”). On August 20, 2014, PrimeLending received a Civil Investigative Demand from the United States Department of Justice (the “DOJ”) related to this Inquiry. According to the Civil Investigative Demand, the DOJ is conducting an investigation to determine whether PrimeLending has violated the False Claims Act in connection with originating and underwriting single-family residential mortgage loans insured by the FHA. The DOJ has advised PrimeLending that, based upon its review of a sample of loans for which an FHA insurance claim was paid by HUD, some of the loans do not meet FHA underwriting guidelines. PrimeLending, based upon its own review of the loan sample, does not agree with the sampling methodology and loan analysis employed by the DOJ. Remedies in these proceedings or settlements may include statutory damages, indemnification, fines and/or penalties. Many institutions have settled these matters on terms that included large monetary penalties. PrimeLending has fully cooperated with this Inquiry, continues to discuss this matter with the DOJ and adjusts its indemnification reserve based upon such discussions.

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

Indemnification Liability Reserve

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

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

An additional reserve has been established for probable agency, investor or other party losses that may have been incurred, but not yet reported to the mortgage origination segment based upon a reasonable estimate of such losses.

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

At December 31, 2017 and 2016, the mortgage origination segment's indemnification liability reserve totaled $23.5 million and $18.2 million, respectively. The provision for indemnification losses was $4.0 million, $4.6 million and $4.0 million during 2017, 2016 and 2015, respectively.

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

	Representation and Warranty Specific Claims Activity - Origination Loan Balance		
	Year Ended December 31,		
	2017	2016	2015
Balance, beginning of year	$ 40,669	$ 57,298	$ 53,906
Claims made	42,330	21,410	71,783
Claims resolved with no payment	(37,439)	(19,696)	(38,862)
Repurchases	(6,490)	(4,164)	(14,884)
Indemnification payments	(5,368)	(14,179)	(14,645)
Balance, end of year	$ 33,702	$ 40,669	$ 57,298

	Indemnification Liability Reserve Activity		
	Year Ended December 31,		
	2017	2016	2015
Balance, beginning of year	$ 18,239	$ 16,640	$ 17,619
Additions for new sales	3,962	4,638	4,006
Repurchases	(466)	(392)	(1,420)
Early payment defaults	(228)	(241)	(64)
Indemnification payments	(713)	(2,482)	(3,027)
Change in reserves for loans sold in prior years	2,678	76	(474)
Balance, end of year	$ 23,472	$ 18,239	$ 16,640

	December 31,	
	2017	2016

Reserve for Indemnification Liability:		
Specific claims	$ 646	$ 1,661
Incurred but not reported claims	22,826	16,578
Total	$ 23,472	$ 18,239

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

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Other Contingencies

In connection with the FNB Transaction, the Bank entered into two loss-share agreements with the FDIC that collectively cover $1.2 billion of loans and OREO acquired in the FNB Transaction. Pursuant to the loss-share agreements, the FDIC has agreed to reimburse the Bank the following amounts with respect to the covered assets: (i) 80% of net losses on the first $240.4 million of net losses incurred; (ii) 0% of net losses in excess of $240.4 million up to and including $365.7 million of net losses incurred; and (iii) 80% of net losses in excess of $365.7 million of net losses incurred. Net losses are defined as book value losses plus certain defined expenses incurred in the resolution of assets, less subsequent recoveries. Under the loss-share agreement for commercial assets, the amount of subsequent recoveries that are reimbursable to the FDIC for a particular asset is limited to book value losses and expenses actually billed plus any book value charge-offs incurred prior to the Bank Closing Date. There is no limit on the amount of subsequent recoveries reimbursable to the FDIC under the loss-share agreement for single family residential assets. The loss-share agreements for commercial and single family residential assets are in effect for five years and ten years, respectively, from the Bank Closing Date and the loss recovery provisions to the FDIC are in effect for eight years and ten years, respectively, from the Bank Closing Date. As part of the loss-share agreements, the Bank is subject to annual FDIC compliance audits. As discussed in Note 6 to the consolidated financial statements, and in accordance with the loss-share agreements, the Bank may be required to make a "true-up" payment to the FDIC approximately ten years following the Bank Closing Date if its actual net realized losses over the life of the loss-share agreements are less than the FDIC's initial estimate of losses on covered assets. The "true-up" payment is calculated using a defined formula set forth in the P&A Agreement. While the ultimate amount of any "true-up" payment is unknown at this time and will vary based upon the amount of future losses or recoveries within the covered loan portfolio, the Bank has recorded a related "true-up" payment accrual of $16.3 million at December 31, 2017 based on the current estimate of aggregate realized losses on covered assets over the life of the loss-share agreements. The initial estimate of the FDIC Indemnification Asset at the Bank Closing Date was recorded at the present value of 80% of $240.4 million. As of December 31, 2017, the Bank projects that the sum of actual plus projected covered losses and reimbursable expenses subject to the loss-share agreements will be less than $240.4 million. As of December 31, 2017, the Bank had billed $184.7 million of covered net losses to the FDIC, of which 80%, or $147.8 million, were reimbursable under the loss-share agreements. As of December 31, 2017, the Bank had received aggregate reimbursements of $145.8 million from the FDIC, which represented reimbursable covered losses and expenses through September 30, 2017.

As discussed in Note 16 to the consolidated financial statements, effective upon completion of the PlainsCapital Merger, Hilltop entered into separate retention agreements with two executive officers, one having an initial term of three years (with automatic one-year renewals at the end of two years and each anniversary thereof) and the other having an initial term of two years (with automatic one-year renewals at the end of the first year and each anniversary thereof). Each of these retention agreements provides for severance pay benefits if the executive officer's employment is terminated without "cause".

In addition to these retention agreements, Hilltop and its subsidiaries maintain employment contracts with certain officers that provide for benefits in the event of a "change in control" as defined in these agreements.

Hilltop and its subsidiaries lease space, primarily for branch facilities and automated teller machines, under noncancelable operating leases with remaining terms, including renewal options, of 1 to 11 years and under capital leases with remaining terms of 4 to 11 years. Rental expense under the operating leases was $43.5 million, $41.9 million and $40.3 million in 2017, 2016 and 2015, respectively.

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Future minimum lease payments under these agreements follow (in thousands).

	Operating Leases	Capital Leases
2018	$ 36,602	$ 1,444
2019	30,127	1,491
2020	24,461	1,528
2021	16,429	1,451
2022	14,306	1,127
Thereafter	31,422	4,125
Total minimum lease payments	$ 153,347	11,166
Amount representing interest		(3,497)
Present value of minimum lease payments		$ 7,669

19. Financial Instruments with Off-Balance Sheet Risk

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

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

In the aggregate, the Bank had outstanding unused commitments to extend credit of $1.9 billion at December 31, 2017 and outstanding financial and performance standby letters of credit of $24.4 million at December 31, 2017.

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

In the normal course of business, the Hilltop Broker-Dealers execute, settle, and finance various securities transactions that may expose the Hilltop Broker-Dealers to off-balance sheet risk in the event that a customer or counterparty does not fulfill its contractual obligations. Examples of such transactions include the sale of securities not yet purchased by customers or for the accounts of the Hilltop Broker-Dealers, use of derivatives to support certain non-profit housing organization clients, clearing agreements between the Hilltop Broker-Dealers and various clearinghouses and broker-dealers, secured financing arrangements that involve pledged securities, and when-issued underwriting and purchase commitments.

20. Stock-Based Compensation

Pursuant to the Hilltop Holdings Inc. 2012 Equity Incentive Plan (the "2012 Plan"), the Company may grant nonqualified stock options, stock appreciation rights, restricted stock, RSUs, performance awards, dividend equivalent rights and other awards to employees of the Company, its subsidiaries and outside directors of the Company. In the aggregate, 4,000,000 shares of common stock may be delivered pursuant to awards granted under the 2012 Plan. At December 31, 2017, 1,634,804 shares of common stock remain available for issuance pursuant to the 2012 Plan, including shares that may be delivered pursuant to outstanding awards. Compensation expense related to the 2012 Plan was $10.8 million, $10.5 million and $8.6 million during 2017, 2016 and 2015, respectively.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

During 2017, 2016 and 2015, Hilltop granted 16,859, 21,224 and 13,631 shares of common stock, respectively, to certain non-employee members of the Company's board of directors for services rendered to the Company pursuant to the 2012 Plan.

Restricted Stock Awards and RSUs

The Compensation Committee of the board of directors of the Company issued restricted shares of Hilltop common stock ("Restricted Stock Awards") and RSUs pursuant to the 2012 Plan.

The Restricted Stock Awards generally cliff vested on the third anniversary of the grant date and were subject to service conditions set forth in the award agreements, with associated costs recognized on a straight-line basis over the respective vesting periods. The award agreements governing the Restricted Stock Awards provided for accelerated vesting under certain conditions. As of September 30, 2017, all remaining Restricted Stock Awards had vested and none were outstanding.

Certain RSUs are subject to time-based vesting conditions and generally provided for a cliff vest on the third anniversary of the grant date, while other RSUs provided for vesting based upon the achievement of certain performance goals over a three-year period subject to service conditions set forth in the award agreements, with associated costs generally recognized on a straight-line basis over the respective vesting periods. The RSUs are not transferable, and the shares of common stock issuable upon conversion of vested RSUs may be subject to transfer restrictions for a period of one year following conversion, subject to certain exceptions. In addition, the applicable RSU award agreements provide for accelerated vesting under certain conditions.

The following table summarizes information about Restricted Stock Award and RSU activity for the noted periods (shares in thousands).

Restricted Stock Awards		RSUs	
Outstanding	Weighted Average Grant Date Fair Value	Outstanding	Weighted Average Grant Date Fair Value
466	$ 13.32	435	$ 23.14

Balance, December 31, 2014				
Granted	63	$ 19.95	491	$ 19.61
Vested/Released	(54)	$ 19.58	(12)	$ 22.45
Forfeited	(22)	$ 13.25	(39)	$ 21.93
Balance, December 31, 2015	453	$ 13.50	875	$ 21.22
Granted	-	$ -	598	$ 17.78
Vested/Released	(447)	$ 13.41	(7)	$ 22.22
Forfeited	(2)	$ 19.72	(10)	$ 20.70
Balance, December 31, 2016	4	$ 19.95	1,456	$ 19.83
Granted	-	$ -	450	$ 26.37
Vested/Released	(4)	$ 19.95	(451)	$ 22.48
Forfeited	-	$ -	(137)	$ 22.41
Balance, December 31, 2017	-	$ -	1,318	$ 20.89

Vested/Released Restricted Stock Awards and RSUs include an aggregate of 252,133 shares withheld to satisfy employee statutory tax obligations during 2017, 2016 and 2015. Pursuant to certain RSU award agreements, an aggregate of 35,685 vested RSUs at December 31, 2017 require deferral of the settlement in shares and statutory tax obligations to a future date.

During 2017, the Compensation Committee of the board of directors of the Company awarded certain executives and key employees an aggregate of 392,877 RSUs pursuant to the 2012 Plan. At December 31, 2017, 313,301 of these outstanding RSUs are subject to time-based vesting conditions and generally cliff vest on the third anniversary of the

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grant date, and 79,576 of these outstanding RSUs will cliff vest based upon the achievement of certain performance goals over a three-year period.

At December 31, 2017, in the aggregate, 1,035,199 of the outstanding RSUs are subject to time-based vesting conditions and generally cliff vest on the third anniversary of the grant date, and 282,329 outstanding RSUs cliff vest based upon the achievement of certain performance goals over a three-year period. At December 31, 2017, unrecognized compensation expense related to outstanding RSUs of $12.6 million is expected to be recognized over a weighted average period of 1.24 years.

21. Regulatory Matters

Banking and Hilltop

PlainsCapital and Hilltop are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory — and possibly additional discretionary — actions by regulators that, if undertaken, could have a direct, material effect on the consolidated financial statements. The regulations require PlainsCapital and Hilltop to meet specific capital adequacy guidelines that involve quantitative measures of assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices.

In January 2015, the comprehensive capital framework ("Basel III") for U.S. banking organizations became effective for PlainsCapital and Hilltop for reporting periods beginning after January 1, 2015 (subject to a phase-in period through January 2019). Under Basel III, total capital consists of two tiers of capital, Tier 1 and Tier 2. Tier 1 capital is further composed of common equity Tier 1 capital and additional Tier 1 capital. Total capital is the sum of Tier 1 capital and Tier 2 capital. The Company performs reviews of the classification and calculation of risk-weighted assets to ensure accuracy and compliance with the Basel III regulatory capital requirements. The capital classifications are also subject to qualitative judgments by the regulators about components, risk weightings and other factors. Quantitative measures established by regulation to ensure capital adequacy require the companies to maintain minimum amounts and ratios (set forth in the following table) of Tier 1 capital (as defined in the regulations) to total average assets (as defined), and minimum ratios of common equity Tier 1, Tier 1 and total capital (as defined) to risk-weighted assets (as defined).

In order to avoid limitations on capital distributions, including dividend payments, stock repurchases and certain discretionary bonus payments to executive officers, Basel III also implemented a capital conservation buffer, which requires a banking organization to hold a buffer above its minimum risk-based capital requirements. This buffer will

help to ensure that banking organizations conserve capital when it is most needed, allowing them to better weather periods of economic stress. The buffer is measured relative to risk-weighted assets. The phase-in of the capital conservation buffer requirements began on January 1, 2016 for Hilltop and the Bank. Based on the actual ratios as shown in the table below, Hilltop and the Bank exceed each of the capital conservation buffer requirements in effect as of December 31, 2017, as well as the fully phased-in requirements through 2019.

In addition, under the final rules, bank holding companies with less than $15 billion in assets as of December 31, 2009 are allowed to continue to include junior subordinated debentures in Tier 1 capital, subject to certain restrictions. However, if an institution grows to above $15 billion in assets as a result of an acquisition, or organically grows to above $15 billion in assets and then makes an acquisition, the combined trust preferred issuances must be phased out of Tier 1 and into Tier 2 capital (75% in 2015 and 100% in 2016). All of the debentures issued to the Trusts, less the common stock of the Trusts, qualified as Tier 1 capital as of December 31, 2017, under guidance issued by the Board of Governors of the Federal Reserve System.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

The following tables show PlainsCapital's and Hilltop's actual capital amounts and ratios in accordance with Basel III compared to the regulatory minimum capital requirements including conservation buffer in effect at the end of the period and on a fully phased-in basis as if such requirements were currently in effect as measured at December 31, 2017 and 2016, respectively (dollars in thousands). Based on the actual capital amounts and ratios shown in the following table, PlainsCapital's ratios place it in the "well capitalized" (as defined) capital category under regulatory requirements.

			Minimum Capital Requirements Including Conservation Buffer		
	Actual Amount	Ratio	In Effect at End of Period Ratio	Fully Phased In Ratio	To Be Well Capitalized Ratio
December 31, 2017					
Tier 1 capital (to average assets):					
PlainsCapital	$ 1,147,527	12.32 %	4.0 %	4.0 %	5.0 %
Hilltop	1,688,358	12.94 %	4.0 %	4.0 %	N/A
Common equity Tier 1 capital (to risk-weighted assets):					
PlainsCapital	1,147,527	14.47 %	5.75 %	7.0 %	6.5 %
Hilltop	1,639,009	17.71 %	5.75 %	7.0 %	N/A
Tier 1 capital (to risk-weighted assets):					
PlainsCapital	1,147,527	14.47 %	7.25 %	8.5 %	8.0 %
Hilltop	1,688,358	18.24 %	7.25 %	8.5 %	N/A
Total capital (to risk-weighted assets):					
PlainsCapital	1,212,793	15.29 %	9.25 %	10.5 %	10.0 %
Hilltop	1,738,325	18.78 %	9.25 %	10.5 %	N/A

			Minimum Capital Requirements Including Conservation Buffer		
	Actual Amount	Ratio	In Effect at End of Period Ratio	Fully Phased In Ratio	To Be Well Capitalized Ratio
December 31, 2016					
Tier 1 capital (to average assets):					
PlainsCapital	$ 1,108,484	12.35 %	4.0 %	4.0 %	5.0 %
Hilltop	1,652,101	13.51 %	4.0 %	4.0 %	N/A

Common equity Tier 1 capital (to risk-weighted assets):									
PlainsCapital	1,108,484	14.64	%	5.125	%	7.0	%	6.5	%
Hilltop	1,602,400	18.30	%	5.125	%	7.0	%	N/A	
Tier 1 capital (to risk-weighted assets):									
PlainsCapital	1,108,484	14.64	%	6.625	%	8.5	%	8.0	%
Hilltop	1,652,101	18.87	%	6.625	%	8.5	%	N/A	
Total capital (to risk-weighted assets):									
PlainsCapital	1,164,767	15.38	%	8.625	%	10.5	%	10.0	%
Hilltop	1,693,240	19.34	%	8.625	%	10.5	%	N/A	

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

A reconciliation of equity capital to common equity Tier 1, Tier 1 and total capital (as defined) is as follows (in thousands).

	December 31, 2017		December 31, 2016	
	PlainsCapital	Hilltop	PlainsCapital	Hilltop
Total equity capital	$ 1,379,402	$ 1,912,081	$ 1,337,746	$ 1,870,509
Add:				
Net unrealized holding losses (gains) on securities available for sale and held in trust	3,520	394	2,303	(485)
Deduct:				
Goodwill and other disallowed intangible assets	(235,395)	(273,466)	(231,565)	(267,624)
Common equity Tier 1 capital (as defined)	1,147,527	1,639,009	1,108,484	1,602,400
Add: Tier 1 capital				
Trust preferred securities	—	65,000	—	65,000
Deduct:				
Additional Tier 1 capital deductions	—	(15,651)	—	(15,299)
Tier 1 capital (as defined)	1,147,527	1,688,358	1,108,484	1,652,101
Add: Allowable Tier 2 capital				
Allowance for loan losses	65,266	65,618	56,283	56,438
Deduct:				
Additional Tier 2 capital deductions	—	(15,651)	—	(15,299)
Total capital (as defined)	$ 1,212,793	$ 1,738,325	$ 1,164,767	$ 1,693,240

Broker-Dealer

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

At December 31, 2017, the net capital position of each of the Hilltop Broker-Dealers was as follows (in thousands).

	Hilltop Securities		HTS Independent Network
Net capital	$ 186,770		$ 3,278
Less: required net capital	10,513		250
Excess net capital	$ 176,257		$ 3,028
Net capital as a percentage of aggregate debit items	35.5	%	
Net capital in excess of 5% aggregate debit items	$ 160,487		

Under certain conditions, Hilltop Securities may be required to segregate cash and securities in a special reserve account for the benefit of customers under Rule 15c3-3 promulgated under the Exchange Act. Assets segregated under the provisions of the Exchange Act are not available for general corporate purposes. At December 31, 2017 and 2016, the Hilltop Broker-Dealers held cash of $186.6 million and $181.0 million, respectively, segregated in special reserve bank accounts for the benefit of customers. The Hilltop Broker-Dealers were not required to segregate cash or securities in special reserve accounts for the benefit of proprietary accounts of introducing broker-dealers at December 31, 2017 and 2016.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

Mortgage Origination

As a mortgage originator, PrimeLending and its subsidiaries are subject to minimum net worth and liquidity requirements established by HUD and GNMA, as applicable. On an annual basis, PrimeLending and its subsidiaries submit audited financial statements to HUD and GNMA, as applicable, documenting their respective compliance with minimum net worth and liquidity requirements. As of December 31, 2017, PrimeLending and its subsidiaries' net worth and liquidity exceeded the amounts required by both HUD and GNMA, as applicable.

Insurance

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

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

	December 31,	
	2017	2016
Capital and surplus:		
National Lloyds Insurance Company	$ 93,812	$ 131,328
American Summit Insurance Company	22,778	30,462

	Year Ended December 31,		
	2017	2016	2015
Statutory net income (loss):			
National Lloyds Insurance Company	$ (1,785)	$ 13,043	$ 9,000
American Summit Insurance Company	742	2,124	1,611

Regulations of the Texas Department of Insurance require insurance companies to maintain minimum levels of statutory surplus to ensure their ability to meet their obligations to policyholders. At December 31, 2017, the Company's insurance subsidiaries had statutory surplus in excess of the minimum required.

The NAIC has adopted a risk based capital ("RBC") formula for insurance companies that establishes minimum capital requirements indicating various levels of available regulatory action on an annual basis relating to insurance risk, asset credit risk, interest rate risk and business risk. The RBC formula is used by the NAIC and certain state insurance regulators as an early warning tool to identify companies that require additional scrutiny or regulatory action. At December 31, 2017, the Company's insurance subsidiaries' RBC ratio exceeded the level at which regulatory action would be required.

22. Stockholders' Equity

The Bank is subject to certain restrictions on the amount of dividends it may declare without prior regulatory approval. At December 31, 2017, $181.7 million of its earnings was available for dividend declaration without prior regulatory approval.

At December 31, 2017, the maximum aggregate dividend that may be paid to NLC from its insurance company subsidiaries without regulatory approval was $16.2 million.

Dividends

During 2017, the Company declared and paid cash dividends of $0.24 per common share, or $23.1 million. During 2016, the Company declared and paid cash dividends of $0.06 per common share, or $5.8 million.

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On January 25, 2018, the Company announced that its board of directors declared a quarterly cash dividend of $0.07 per common share, payable on February 28, 2018, to all common stockholders of record as of the close of business on February 15, 2018.

Stock Repurchase Programs

The Company's board of directors has periodically approved stock repurchase programs under which it authorized the Company to repurchase its outstanding common stock. Under the respective stock repurchase program authorized, the Company could repurchase shares in open-market purchases or through privately negotiated transactions as permitted under Rule 10b-18 promulgated under the Exchange Act. The extent to which the Company repurchased its shares and the timing of such repurchases depended upon market conditions and other corporate considerations, as determined by Hilltop's management team. Repurchased shares will be returned to the Company's pool of authorized but unissued shares of common stock.

During 2015, the Company paid $30.0 million to repurchase and retire an aggregate of 1,390,977 shares of common stock at an average price of $21.56 per share. This stock repurchase program terminated effective December 2015. In January 2017, the Company's board of directors reauthorized the stock repurchase program originally approved during the second quarter of 2016 through January 2018. During 2017, the Company paid $27.4 million to repurchase an aggregate of 1,057,656 shares of common stock at an average price of $25.87 per share. This stock repurchase program expired in January 2018. All purchases were funded from available cash balances.

In January 2018, the Company's board of directors authorized a stock repurchase program through January 2019, under which the Company may repurchase, in the aggregate, up to $50.0 million of its outstanding common stock.

Series B Preferred Stock

As a result of the PlainsCapital Merger, the outstanding shares of PCC's Non-Cumulative Perpetual Preferred Stock, Series C, all of which were held by the U.S. Treasury, were converted on a one-for-one basis into 114,068 shares of Hilltop Non-Cumulative Perpetual Preferred Stock, Series B ("Hilltop Series B Preferred Stock"). The terms of the Hilltop Series B Preferred Stock provided for the payment of non-cumulative dividends on a quarterly basis. The dividend rate, as a percentage of the liquidation amount, fluctuated until December 31, 2013 based upon changes in the level of "qualified small business lending" ("QSBL") by the Bank. The shares of Hilltop Series B Preferred Stock were senior to shares of Hilltop common stock with respect to dividends and liquidation preference, and qualified as Tier 1 Capital for regulatory purposes.

The dividend rate on the Hilltop Series B Preferred Stock had been fixed at 5.0% since January 1, 2014, based upon the level of QSBL at September 30, 2013. On April 28, 2015, as discussed in Note 13 to the consolidated financial statements, Hilltop used the net proceeds of the offering of Senior Notes to redeem all shares of Hilltop Series B Preferred Stock at an aggregate liquidation value of $114.1 million, plus accrued but unpaid dividends of $0.4 million.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

23. Other Noninterest Income and Expense

The following table shows the components of other noninterest income and expense (in thousands).

	Year Ended December 31,		
	2017	2016	2015
Other noninterest income:			
Net gains from Hilltop Broker-Dealer trading activities	$ 70,922	$ 86,383	$ 44,042
Net gains from trading securities portfolio	20,210	15,926	12,796
Service charges on depositor accounts	14,429	14,162	15,169
SWS Merger appraisal proceeding	11,757	—	—
Trust fees	7,485	6,782	7,113
Insurance commissions	4,819	4,206	3,819
Insurance direct billing and other policy fees	4,353	4,818	5,329
Revenue from check and stored value cards	3,169	5,036	7,099
Rent and other income from other real estate owned	1,280	1,461	3,559
FDIC Indemnification Asset accretion	—	242	1,147
Other	25,546	15,248	10,795
	$ 163,970	$ 154,264	$ 110,868
Other noninterest expense:			
Software and information technology	$ 45,891	$ 38,421	$ 39,250
Brokerage commissions and fees	22,884	24,654	16,637
Mortgage origination and servicing	22,353	25,736	19,375
Unreimbursed loan closing costs	20,428	31,234	35,253
Business development	18,619	19,738	18,291
FDIC Indemnification Asset amortization	17,083	—	—
Travel, meals and entertainment	12,839	13,683	12,748
Funding fees	8,464	7,451	5,865
Amortization of intangible assets	8,263	10,174	12,375
Office supplies	7,806	8,719	8,247
OREO and repossessed assets	4,004	13,438	12,570
FDIC "true-up"	2,100	8,750	5,475
Other	51,362	49,523	62,217
	$ 242,096	$ 251,521	$ 248,303

24. Derivative Financial Instruments

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

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

Non-Hedging Derivative Instruments and the Fair Value Option

As discussed in Note 3 to the consolidated financial statements, the Company has elected to measure substantially all mortgage loans held for sale at fair value under the provisions of the Fair Value Option. The election provides the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without applying complex hedge accounting provisions. The fair values of PrimeLending's IRLCs, forward commitments, and interest rate swaps and swaptions, and U.S. Treasury bond futures and options are recorded in other assets or other liabilities, as appropriate, and changes in the fair values of these derivative instruments are recorded as a component of net gains from sale of loans and other mortgage production income. The fair value of PrimeLending's derivative instruments decreased $13.1 million during 2017 and increased $8.0 million and $17.3 million during 2016 and 2015, respectively. Changes in fair value are attributable to changes in the volume of IRLCs, mortgage loans held for sale, commitments to purchase and sell MBSs and MSR assets, and changes in market interest rates. Changes in market interest rates also conversely affect the value of PrimeLending's mortgage loans held for sale and its MSR asset, which are measured at fair value under the Fair Value Option. The effect of the change in market interest rates on PrimeLending's loans held for sale and MSR asset is discussed in Note 3 to the consolidated financial statements. The fair values of the Hilltop Broker-Dealers' and the Bank's derivative instruments are recorded in other assets or other liabilities, as appropriate. The fair values of the Hilltop Broker-Dealers' derivatives increased $8.1 million during 2017, compared with a decrease of $23.4 million during 2016 and an increase of $43.7 million during 2015. The fair values of the Bank's derivatives increased $0.3 million during 2017 and $0.4 million during 2016, compared with a decrease of $0.2 million during 2015. The changes in fair value were recorded as a component of other noninterest income.

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

	December 31, 2017		December 31, 2016	
	Notional Amount	Estimated Fair Value	Notional Amount	Estimated Fair Value
Derivative instruments:				
IRLCs	$ 850,850	$ 18,851	$ 944,550	$ 23,269
Customer-based written options	21,637	38	—	—
Customer-based purchased options	21,637	(38)	—	—
Commitments to purchase MBSs	2,831,635	(921)	3,616,922	(1,155)
Commitments to sell MBSs	4,963,498	2,972	5,609,250	(532)
Interest rate swaps and swaptions	25,971	51	32,452	(283)
U.S. Treasury bond futures and options (1)	214,500	—	297,000	—

(1)Changes in the fair value of these contracts are settled daily with PrimeLending's counterparty.

PrimeLending has cash collateral advances totaling $0.8 million to offset net liability derivative positions on its commitments to sell MBSs at December 31, 2017, compared to a payable totaling $19.1 million on its net liability derivative position on its commitments to sell MBSs at December 31, 2016. In addition, PrimeLending advanced cash collateral totaling $3.2 million and $3.2 million on its U.S. Treasury bond futures and options at December 31, 2017 and 2016, respectively. These amounts are included in other assets within the consolidated balance sheets.

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

25. Balance Sheet Offsetting

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

	Gross Amounts of Recognized Assets	Gross Amounts Offset in the Balance Sheet	Net Amounts of Assets Presented in the Balance Sheet	Gross Amounts Not Offset in the Balance Sheet		
				Financial Instruments	Cash Collateral Pledged	Net Amount
December 31, 2017						
Securities borrowed: Institutional counterparties	$ 1,386,821	$ —	$ 1,386,821	$ (1,327,536)	$ —	$ 59,285
Interest rate options: Customer counterparties	38	—	38	—	—	38
Reverse repurchase agreements: Institutional counterparties	186,537	—	186,537	(186,026)	—	511
Forward MBS derivatives: Institutional counterparties	3,576	—	3,576	(3,576)	—	—
	$ 1,576,972	$ —	$ 1,576,972	$ (1,517,138)	$ —	$ 59,834
December 31, 2016						
Securities borrowed: Institutional counterparties	$ 1,436,069	$ —	$ 1,436,069	$ (1,385,664)	$ —	$ 50,405

Reverse repurchase agreements:						
Institutional counterparties	89,430	—	89,430	(89,369)	—	61
Forward MBS derivatives:						
Institutional counterparties	21,366	(3,893)	17,473	(9,012)	—	8,461
	$ 1,546,865	$ (3,893)	$ 1,542,972	$ (1,484,045)	$ —	$ 58,927

				Gross Amounts Not Offset in the Balance Sheet		
	Gross Amounts of Recognized Liabilities	Gross Amounts Offset in the Balance Sheet	Net Amounts of Liabilities Presented in the Balance Sheet	Financial Instruments	Cash Collateral Pledged	Net Amount
December 31, 2017						
Securities loaned:						
Institutional counterparties	$ 1,215,093	$ —	$ 1,215,093	$ (1,157,198)	$ —	$ 57,895
Interest rate options:						
Institutional counterparties	38	—	38	—	—	38
Interest rate swaps and swaptions:						
Institutional counterparties	35	(86)	(51)	(1,059)	—	(1,110)
Repurchase agreements:						
Institutional counterparties	409,058	—	409,058	(409,058)	—	—
Customer counterparties	130,091	—	130,091	(130,091)	—	—
Forward MBS derivatives:						
Institutional counterparties	2,696	(1,171)	1,525	(1,295)	—	230
	$ 1,757,011	$ (1,257)	$ 1,755,754	$ (1,698,701)	$ —	$ 57,053
December 31, 2016						
Securities loaned:						

Institutional counterparties	$ 1,283,676	$ —	$ 1,283,676	$ (1,237,868)	$ —	$ 45,808
Interest rate swaps and swaptions:						
Institutional counterparties	297	(14)	283	(3,000)	—	(2,717)
Repurchase agreements:						
Institutional counterparties	39,970	—	39,970	(39,970)	—	—
Customer counterparties	155,194	—	155,194	(155,194)	—	—
Forward MBS derivatives:						
Institutional counterparties	19,159	—	19,159	(19,159)	—	—
	$ 1,498,296	$ (14)	$ 1,498,282	$ (1,455,191)	$ —	$ 43,091

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

Secured Borrowing Arrangements

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

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

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

The following tables present the remaining contractual maturities of repurchase agreement and securities lending transactions accounted for as secured borrowings (in thousands). The Company had no repurchase-to-maturity transactions outstanding at both December 31, 2017 and 2016.

Remaining Contractual Maturities

December 31, 2017	Overnight and Continuous	Up to 30 Days	30-90 Days	Greater Than 90 Days	Total
Repurchase agreement transactions:					
U.S. Treasury and agency securities	$ 181,915	$ —	$ —	$ —	$ 181,915
Asset-backed securities	357,234	—	—	—	357,234
Securities lending transactions:					
Corporate securities	11,499	—	—	—	11,499
Equity securities	1,203,594	—	—	—	1,203,594
Total	$ 1,754,242	$ —	$ —	$ —	$ 1,754,242
Gross amount of recognized liabilities for repurchase agreement and securities lending transactions in offsetting disclosure above					$ 1,754,242
Amount related to agreements not included in offsetting disclosure above					$ —

	Remaining Contractual Maturities				
December 31, 2016	Overnight and Continuous	Up to 30 Days	30-90 Days	Greater Than 90 Days	Total
Repurchase agreement transactions:					
U.S. Treasury and agency securities	$ 195,164	$ —	$ —	$ —	$ 195,164
Securities lending transactions:					
Corporate securities	14,816	—	—	—	14,816
Equity securities	1,268,860	—	—	—	1,268,860
Total	$ 1,478,840	$ —	$ —	$ —	$ 1,478,840
Gross amount of recognized liabilities for repurchase agreement and securities lending transactions in offsetting disclosure above					$ 1,478,840
Amount related to agreements not included in offsetting disclosure above					$ —

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

26. Broker-Dealer and Clearing Organization Receivables and Payables

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

	December 31,	
	2017	2016
Receivables:		
Securities borrowed	$ 1,386,821	$ 1,436,069
Securities failed to deliver	25,491	33,834
Trades in process of settlement	29,412	10,223
Other	22,654	17,615
	$ 1,464,378	$ 1,497,741
Payables:		
Securities loaned	$ 1,215,093	$ 1,283,676
Correspondents	30,160	31,040
Securities failed to receive	37,864	31,724
Other	4,446	688
	$ 1,287,563	$ 1,347,128

27. Deferred Policy Acquisition Costs

Policy acquisition expenses, primarily commissions, premium taxes and underwriting expenses related to the successful issuance of a new or renewal policy incurred by NLC are deferred and charged against income ratably over the terms of the related policies. A summary of the activity in deferred policy acquisition costs is as follows (in thousands).

	Year Ended December 31,		
	2017	2016	2015
Balance, beginning of year	$ 18,603	$ 19,874	$ 20,416
Acquisition expenses capitalized	34,934	37,231	39,716
Amortization charged to income	(36,549)	(38,502)	(40,258)
Balance, end of year	$ 16,988	$ 18,603	$ 19,874

Amortization is included in policy acquisition and other underwriting expenses in the accompanying consolidated statements of operations.

28. Reserve for Losses and Loss Adjustment Expenses

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

	December 31,	
	2017	2016
Reserve for unpaid losses and allocated LAE balance, net	$ 17,470	$ 25,203
Reinsurance recoverables on unpaid losses	11,495	9,434
Unallocated LAE	1,248	1,189
Reserve for unpaid losses and LAE balance, gross	$ 30,213	$ 35,826

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

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

Accident Year	Year Ended December 31, 2017 Paid	Incurred	December 31, 2017 Total of IBNR Reserves Plus Expected Development on Reported Claims	Cumulative Number of Reported Claims
2013	110,813	111,121	8	15,687
2014	83,346	84,074	119	13,099
2015	85,507	87,262	591	15,016
2016	81,682	85,189	2,622	21,277
2017	77,855	88,079	4,282	20,927
Total	439,203	$ 455,725		
	948	All outstanding reserves prior to 2013, net of reinsurance		
	$ 17,470	Reserve for unpaid losses and allocated LAE, net of reinsurance		

29. Reinsurance Activity

NLC limits the maximum net loss that can arise from large risks or risks in concentrated areas of exposure by reinsuring (ceding) certain levels of risk. Substantial amounts of business are ceded, and these reinsurance contracts do not relieve NLC from its obligations to policyholders. Such reinsurance includes quota share, excess of loss, catastrophe, and other forms of reinsurance on essentially all property and casualty lines of insurance. Net insurance premiums earned, losses and LAE and policy acquisition and other underwriting expenses are reported net of the amounts related to reinsurance ceded to other companies. Amounts recoverable from reinsurers related to the portions of the liability for losses and LAE and unearned insurance premiums ceded to them are reported as assets. Failure of reinsurers to honor their obligations could result in losses to NLC; consequently, allowances are established for amounts deemed uncollectible as NLC evaluates the financial condition of its reinsurers and monitors concentrations of credit risk arising from similar geographic regions, activities, or economic characteristics of the reinsurers to minimize its exposure to significant losses from reinsurer insolvencies. At December 31, 2017, total reinsurance recoverables and receivables had a carrying value of $13.1 million, which is included in other assets within the consolidated balance sheet. There was no allowance for uncollectible accounts at December 31, 2017, based on NLC's

quality requirements.

Reinsurers with a balance in excess of 5% of the Company’s outstanding reinsurance receivables at December 31, 2017 are listed below (in thousands).

	Balances Due From Reinsurers	A.M. Best Rating
Arch Reinsurance Co.	$ 1,115	N/A
Partner Reinsurance Co.	1,947	A
Aspen Bermuda	865	A
R&V Versicherung AG	1,927	N/A
Everest Re	767	A+
Lloyd's Syndicate #2001	729	A+
	$ 7,350	

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

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

	Year Ended December 31,					
	2017		2016		2015	
	Written	Earned	Written	Earned	Written	Earned
Premiums from direct business	$ 137,091	$ 144,990	$ 152,970	$ 159,884	$ 167,025	$ 169,334
Reinsurance assumed	12,150	11,767	11,338	11,024	10,714	10,283
Reinsurance ceded	(12,280)	(14,459)	(14,962)	(15,363)	(17,170)	(17,535)
Net premiums	$ 136,961	$ 142,298	$ 149,346	$ 155,545	$ 160,569	$ 162,082

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

	Year Ended December 31,		
	2017	2016	2015
Losses and LAE incurred	$ 138,358	$ 113,494	$ 123,017
Reinsurance recoverables	(43,657)	(24,251)	(23,951)
Net loss and LAE incurred	$ 94,701	$ 89,243	$ 99,066

Catastrophic coverage

NLC's liabilities for losses and LAE include liabilities for reported losses, liabilities for IBNR losses and liabilities for LAE less a reduction for reinsurance recoverables related to those liabilities. The amount of liabilities for reported claims is based primarily on a claim-by-claim evaluation of coverage, liability, injury severity or scope of property damage, and any other information considered relevant to estimating exposure presented by the claim. The amounts of liabilities for IBNR losses and LAE are estimated on the basis of historical trends, adjusted for changes in loss costs, underwriting standards, policy provisions, product mix and other factors. Estimating the liability for unpaid losses and LAE is inherently judgmental and is influenced by factors that are subject to significant variation. Liabilities for LAE are intended to cover the ultimate cost of settling claims, including investigation and defense of lawsuits resulting from such claims. Based upon the contractual terms of the reinsurance agreements, reinsurance recoverables offset, in part, NLC's gross liabilities.

Effective July 1, 2017, NLC renewed its catastrophic excess of loss reinsurance coverage for a two year period. At December 31, 2017, NLC had catastrophic excess of loss reinsurance coverage of losses per event in excess of

$8 million retention by NLIC and $1.5 million retention by ASIC. ASIC maintained an underlying layer of coverage, providing $6.5 million in excess of its $1.5 million retention to bridge to the primary program. The reinsurance in excess of $8 million is comprised of three layers of protection: $17 million in excess of $8 million retention and/or loss; $30 million in excess of $25 million loss; and $50 million in excess of $55 million loss. NLIC and ASIC retain no participation in any of the layers, beyond the first $8 million and $1.5 million, respectively. At December 31, 2017, total retention for any one catastrophe that affects both NLIC and ASIC was limited to $8 million in the aggregate.

Effective January 1, 2018, NLC renewed its underlying excess of loss contract that provides $10.0 million aggregate coverage in excess of NLC's per event retention of $1.0 million and aggregate retention of $17.5 million for sub-catastrophic events. As of January 1, 2018, NLC retains 17.5% participation in this coverage, up from no participation during 2017.

During August and September 2017, NLC experienced losses related to Hurricane Harvey in excess of retention. As of December 31, 2017, the total gross losses and LAE incurred associated with Hurricane Harvey was $18.2 million. However, because the losses exceeded retention, net exposure to NLC was $3.4 million retention and $1.4 million in reinstatement premiums. During 2016 and 2015, NLC experienced no significant catastrophes that resulted in losses in excess of retention at NLIC or ASIC.

There were 16 tornado, hail and wind storms during 2017 that fit the coverage criteria for the underlying excess of loss contract providing aggregate coverage for sub-catastrophic events. These events had a gross incurred loss total of $38.1 million, which developed a reinsured recoverable of $4.6 million at the 100% subscription level. During 2016, the 15 tornado, hail and wind storms that exceeded retention had incurred losses of $44.0 million, which developed a reinsured recoverable of $10.0 million at the 100% subscription level. During 2015, the 12 tornado, hail and wind storms

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that exceeded retention had incurred losses of $35.3 million, which developed a reinsured recoverable of $9.1 million at the 91% subscription level. These losses have no effect on net loss and LAE incurred beyond retention because the catastrophic events exceeded retention levels and are fully recoverable. Any losses beyond the reinsurance coverage limits of $10.0 million for 2016 and $9.1 million for 2015 are retained by the Company and have an effect on the net loss and LAE incurred. The primary financial effect beyond the reinsurance retention is additional reinstatement premium payable to the affected reinsurers. In addition to the $1.4 million in reinstatement premiums noted above related to Hurricane Harvey in 2017, reinstatement premiums during 2017, 2016 and 2015 of $1.4 million, $0.6 million and $0.2 million, respectively, were recorded as ceded premiums.

30. Segment and Related Information

The Company currently has four reportable business segments that are organized primarily by the core products offered to the segments' respective customers. These segments reflect the manner in which operations are managed and the criteria used by the Company's chief operating decision maker function to evaluate segment performance, develop strategy and allocate resources. The chief operating decision maker function consists of the Company's President and Co-Chief Executive Officer and the Company's Vice Chairman and Co-Chief Executive Officer.

The banking segment includes the operations of the Bank, the broker-dealer segment includes the operations of Securities Holdings, the mortgage origination segment is composed of PrimeLending, and the insurance segment is composed of NLC.

Corporate includes certain activities not allocated to specific business segments. These activities include holding company financing and investing activities, merchant banking investment opportunities, and management and administrative services to support the overall operations of the Company including, but not limited to, certain executive management, corporate relations, legal, finance and acquisition costs.

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

Year Ended	Banking	Broker-Dealer	Mortgage Origination	Insurance	Corporate	All Other and Eliminations	Hilltop Consolidated

December 31, 2017							
Net interest income (expense)	$ 366,581	$ 43,735	$ (915)	$ 2,861	$ (10,069)	$ 19,555	$ 421,748
Provision for loan losses	14,073	198	—	—	—	—	14,271
Noninterest income	59,904	368,421	632,388	151,382	12,798	(19,829)	1,205,064
Noninterest expense	248,404	347,314	581,899	158,354	33,983	(699)	1,369,255
Income (loss) before income taxes	$ 164,008	$ 64,644	$ 49,574	$ (4,111)	$ (31,254)	$ 425	$ 243,286

ar Ended December 31, 2016	Banking	Broker-Dealer	Mortgage Origination	Insurance	Corporate	All Other and Eliminations	Hilltop Consolidate
t interest income (expense)	$ 363,083	$ 31,172	$ (11,589)	$ 3,164	$ (7,257)	$ 18,958	$ 397,531
ovision for loan losses	40,673	(53)	—	—	—	—	40,620
ninterest income	52,579	385,766	704,126	164,841	2	(20,349)	1,286,965
ninterest expense	244,715	377,524	614,741	146,601	29,938	(1,048)	1,412,471
ome (loss) before income es	$ 130,274	$ 39,467	$ 77,796	$ 21,404	$ (37,193)	$ (343)	$ 231,405

Year Ended December 31, 2015	Banking	Broker-Dealer	Mortgage Origination	Insurance	Corporate	All Other and Eliminations	Hilltop Consolidated
Net interest income (expense)	$ 369,493	$ 32,971	$ (10,423)	$ 3,187	$ (5,109)	$ 18,464	$ 408,583
Provision for loan losses	12,795	(80)	—	—	—	—	12,715
Noninterest income	62,639	334,495	597,163	171,185	81,289	(19,129)	1,227,642
Noninterest expense	243,926	367,812	539,257	158,720	31,926	(1,625)	1,340,016
Income (loss) before income taxes	$ 175,411	$ (266)	$ 47,483	$ 15,652	$ 44,254	$ 960	$ 283,494

	Banking	Broker-Dealer	Mortgage Origination	Insurance	Corporate	All Other and Eliminations	Hilltop Consolidate
December 31, 2017							
Goodwill	$ 207,741	$ 7,008	$ 13,071	$ 23,988	$ —	$ —	$ 251,808
Total assets	$ 9,558,718	$ 3,394,911	$ 1,937,327	$ 291,639	$ 2,106,978	$ (3,923,787)	$ 13,365,78
December 31, 2016							
Goodwill	$ 207,741	$ 7,008	$ 13,071	$ 23,988	$ —	$ —	$ 251,808
Total assets	$ 9,527,518	$ 2,777,849	$ 2,042,458	$ 347,252	$ 2,032,749	$ (3,989,764)	$ 12,738,06

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

31. Earnings per Common Share

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

	Year Ended December 31,		
	2017	2016	2015
Basic earnings per share:			
Income attributable to Hilltop	$ 132,544	$ 145,894	$ 209,119
Less: income applicable to participating shares	—	(6)	(952)
Net earnings available to Hilltop common stockholders	$ 132,544	$ 145,888	$ 208,167
Weighted average shares outstanding - basic	97,137	98,404	99,074
Basic earnings per common share	$ 1.36	$ 1.48	$ 2.10
Diluted earnings per share:			
Income attributable to Hilltop	$ 132,544	$ 145,894	$ 209,119
Weighted average shares outstanding - basic	97,137	98,404	99,074
Effect of potentially dilutive securities	216	225	888
Weighted average shares outstanding - diluted	97,353	98,629	99,962
Diluted earnings per common share	$ 1.36	$ 1.48	$ 2.09

32. Condensed Financial Statements of Parent

Condensed financial statements of Hilltop (parent only) follow (in thousands). Investments in subsidiaries are determined using the equity method of accounting.

Condensed Statements of Operations and Comprehensive Income

Year Ended December 31,

	2017	2016	2015
Dividends from bank and bank holding company subsidiaries	$ 53,000	$ 87,826	$ —
Dividends from nonbank subsidiaries	41,500	—	—
Investment income	312	382	445
Interest expense	10,381	7,639	5,554
Bargain purchase gain	—	—	81,289
Other income	12,798	2	—
General and administrative expense	33,983	29,938	31,926
Income before income taxes, equity in undistributed earnings of subsidiaries and preferred stock activity	63,246	50,633	44,254
Income tax benefit	(15,577)	(10,077)	(9,562)
Equity in undistributed earnings of subsidiaries	54,321	87,234	158,763
Net income	$ 133,144	$ 147,944	$ 212,579
Other comprehensive income (loss), net	(879)	(2,144)	1,978
Comprehensive income	$ 132,265	$ 145,800	$ 214,557

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

Condensed Balance Sheets

	December 31, 2017	2016	2015
Assets:			
Cash and cash equivalents	$ 96,764	$ 118,290	$ 55,542
Investment in subsidiaries:			
Bank and bank holding company subsidiaries	1,340,093	1,304,917	1,271,581
Nonbank subsidiaries	603,631	609,539	545,502
Other assets	66,490	3	32,922
Total assets	$ 2,106,978	$ 2,032,749	$ 1,905,547
Liabilities and Stockholders' Equity:			
Accounts payable and accrued expenses	$ 46,442	$ 13,929	$ 20,419
Notes payable	148,455	148,311	148,174
Stockholders' equity	1,912,081	1,870,509	1,736,954
Total liabilities and stockholders' equity	$ 2,106,978	$ 2,032,749	$ 1,905,547

Condensed Statements of Cash Flows

	Year Ended December 31, 2017	2016	2015
Operating Activities:			
Net income	$ 133,144	$ 147,944	$ 212,579
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Equity in undistributed earnings of subsidiaries	(54,321)	(87,234)	(158,763)
Bargain purchase gain	—	—	(81,289)
Deferred income taxes	2,511	(2,063)	12,429
Other, net	(57,380)	20,812	2,443
Net cash provided by (used in) operating activities	23,954	79,459	(12,601)
Investing Activities:			
Reimbursement from nonbank subsidiaries	—	6,000	—
Capital contribution to bank and bank holding company subsidiaries	(10,000)	—	—
Capital contribution to nonbank subsidiaries	—	(20,000)	—
Cash paid for acquisition	—	—	(78,217)
Other, net	(4,241)	(98)	(31)
Net cash used in investing activities	(14,241)	(14,098)	(78,248)
Financing Activities:			
Proceeds from issuance of common stock	—	4,139	—
Payments to repurchase common stock	(27,388)	—	(30,028)
Proceeds from issuance of notes payable	—	—	148,078

Dividends paid on common stock	(23,140)	(5,801)	—
Dividends paid on preferred stock	—	—	(3,539)
Redemption of preferred stock	—	—	(114,068)
Other, net	19,289	(951)	—
Net cash provided by (used in) financing activities	(31,239)	(2,613)	443
Net change in cash and cash equivalents	(21,526)	62,748	(90,406)
Cash and cash equivalents, beginning of year	118,290	55,542	145,948
Cash and cash equivalents, end of year	$ 96,764	$ 118,290	$ 55,542
Supplemental Schedule of Non-Cash Activities:			
Common stock issued in acquisition	$ —	$ —	$ 200,626

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Hilltop Holdings Inc. and Subsidiaries
Notes to Consolidated Financial Statements (continued)

During 2017, Hilltop used $47.1 million in cash to repurchase common stock associated with the resolution of the contingency on appraisal proceedings from the SWS Merger. This activity is reflected in the other line item within operating activities in the above condensed statement of cash flows of Hilltop. Additionally, certain assets and liabilities, including $20.6 million of cash, were transferred from PCC to Hilltop in 2017 due to organizational changes. This activity is reflected in the other line item within financing activities in the above condensed statement of cash flows of Hilltop.

During 2015, as further discussed in Note 13 to the consolidated financial statements, Hilltop completed an offering of $150.0 million aggregate principal amount of its 5% Senior Notes due 2025 and used the net proceeds of the offering to redeem all Hilltop's outstanding Series B Preferred Stock at an aggregate liquidation value of $114.1 million, plus accrued but unpaid dividends of $0.4 million, and utilized the remainder for general corporate purposes.

33. Recently Issued Accounting Standards

In February 2018, FASB issued Accounting Standards Update ("ASU") 2018-02 to help organizations address certain stranded income tax effects in accumulated other comprehensive income ("AOCI") resulting from the Tax Legislation. The amendment provides financial statement preparers with an option to reclassify stranded tax effects within AOCI to retained earnings in each period in which the effect of the changes in the U.S. federal corporate income tax rate in the Tax Legislation (or portion thereof) is recorded. The amendment also includes disclosure requirements regarding the issuer's accounting policy for releasing income tax effects from AOCI. The amendment is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2018. Early adoption is permitted, and organizations should apply the provisions of the amendment either in the period of adoption or retrospectively to each period (or periods) in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Legislation is recognized. The Company is currently evaluating the provisions of the amendment and the impact on its future consolidated financial statements.

In May 2017, FASB issued ASU 2017-09 which provides clarity and reduces both diversity in practice and cost and complexity associated with changes to the terms or conditions of a share-based payment award and, specifically, which changes require an entity to apply modification accounting. The amendments in this update are effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2017. The Company has adopted the amendments as of January 1, 2018, which are expected to have a significant effect on the Company's consolidated financial statements.

In April 2017, FASB issued ASU 2017-08 which shortens the amortization period for the premium on certain purchased callable debt securities to the earliest call date. The amendment is effective for annual periods, and interim reporting periods within those annual periods, beginning after December 15, 2018, using the modified retrospective

transition method. As permitted within the amendment, the Company elected to early adopt and apply the provisions of this amendment as of January 1, 2017. This adoption had no effect on the Company's consolidated financial statements.

In January 2017, FASB issued ASU 2017-01 which provides guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The amendment is effective for annual periods, and interim reporting periods within those annual periods, beginning after December 15, 2017, using the prospective method. The Company has adopted the amendments as of January 1, 2018, and will prospectively apply its provisions.

In October 2016, FASB issued ASU No. 2016-16 which addresses improvement in accounting for income tax consequences of intra-equity transfers of assets other than inventory. The amendment requires that an entity recognize the income tax consequences of the intra-equity transfer of an asset other than inventory when the transfer occurs. The amendments are effective for annual periods, and interim reporting periods within those annual periods, beginning after December 15, 2017, using the modified retrospective transition method. The Company has adopted the amendments as of January 1, 2018, which are not expected to have a significant effect on the Company's consolidated financial statements.

In August 2016, FASB issued ASU 2016-15 to add or clarify guidance on the classification of certain cash receipts and payments in the statement of cash flows and to eliminate the diversity in practice related to such classifications. The amendments are effective for annual periods, and interim reporting periods within those annual periods, beginning after

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December 15, 2017 using a retrospective transition method. The Company has adopted the amendments as of January 1, 2018, which are not expected to have a significant effect on the Company's consolidated financial statements.

In June 2016, FASB issued ASU 2016-13 which sets forth a "current expected credit loss" (CECL) model which requires entities to measure all credit losses expected over the life of an exposure (or pool of exposures) for financial instruments held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. This replaces the existing incurred loss model and is applicable to the measurement of credit losses on financial assets measured at amortized cost and applies to some off-balance sheet credit exposures. The amendment also requires enhanced disclosures to help financial statement users better understand significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an entity's portfolio. The amendments are effective for annual periods, and interim reporting periods within those annual periods, beginning after December 15, 2019 with a cumulative-effect adjustment to retained earnings as of the beginning of the reporting period of adoption. The Company does not intend to adopt the provisions of the amendment early. The Company has formed a cross-functional implementation team to evaluate the provisions of the amendment and the impact on its future consolidated financial statements through the identification of data requirements and determination of necessary modifications to its existing credit loss estimation methodologies, systems and processes. The magnitude of the change in allowance for loan losses will depend on, among other things, the portfolio composition and quality at the adoption date, as well as economic conditions and forecasts at that time.

In February 2016, FASB issued ASU 2016-02 related to leases. The new standard is intended to increase transparency and comparability among organizations and require lessees to record a right-to-use asset and liability representing the obligation to make lease payments for long-term leases. Accounting by lessors will remain largely unchanged. The amendments are effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2018. Adoption will require a modified retrospective transition where the lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented. Early adoption is permitted, however, the Company does not intend to adopt the provisions of the amendment early. The Company's implementation efforts are on-going, including the installation of a software solution, which will aid in determining the magnitude of the increases in assets and liabilities and their impact on the consolidated financial statements. The Company expects to recognize lease liabilities and corresponding right-of-use assets (at their present value) related to predominantly all of the future minimum lease payments required under operating leases as disclosed in Note 18 to the consolidated financial statements. However, the population of contracts subject to balance sheet recognition and their initial measurement remains under evaluation.

In January 2016, FASB issued ASU 2016-01 related to financial instruments. This amendment requires that most equity investments be measured at fair value, with subsequent changes in fair value recognized in net income. The amendment also impacts financial liabilities under the Fair Value Option and the presentation and disclosure requirements for financial instruments and modifies the required process used to evaluate deferred tax assets on available for sale securities. The amendment is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2017. The Company has adopted the amendment as of January 1, 2018, which resulted in $21.2 million of available for sale equity securities being reclassified within the consolidated balance sheet

consistent with the provisions of the new amendment, while certain other equity investments of approximately $40 million will continue to be included in other assets within the consolidated balance sheet. The adoption of the amendment resulted in approximately $3 million being reclassified from accumulated other comprehensive income to retained earnings, representing an increase to retained earnings as of January 1, 2018. All subsequent changes in fair value related to these equity investments will be recognized in net income. Additionally, the enhanced disclosures required by the new standard will be included in subsequent filings, including the disclosure of the fair value of the loan portfolio using and exit price method instead of the current discounted cash flow method. These disclosure changes are not expected to have a significant effect on the Company's consolidated financial statements.

In July 2015, the FASB issued ASU 2015-14, which deferred the effective date of ASU 2014-09 by one year, to clarify the principles for recognizing revenue from contracts with customers. The FASB has subsequently issued several amendments to the standard, including clarification of principal versus agent considerations, narrow scope improvements and other technical corrections. The amendments outline a single comprehensive model for entities to depict the transfer of goods or services to customers in amounts that reflect the payment to which a company expects to be entitled in exchange for those goods or services. The amendments also require additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and

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Notes to Consolidated Financial Statements (continued)

changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. The amendments are effective for annual periods, and interim reporting periods within those annual periods, beginning after December 15, 2017 and may be adopted using either a full retrospective transition method or a modified, cumulative-effect approach wherein the guidance is applied only to existing contracts as of the date of initial application and to new contracts entered into thereafter. The Company has adopted the amendments as of January 1, 2018 using the cumulative-effect approach. The Company gathered an inventory of contracts with customers and performed an in-depth assessment of these contracts for evaluation under the amendments. A majority of the Company's revenues are not subject to the new guidance. The revenue recognition policies within the Company's broker-dealer segment were the most affected upon adoption. Specifically, the new guidance required changes to the principal versus agent conclusion for certain advisory and underwriting revenues and expenses which, as of January 1, 2018, are recorded on a gross basis while legacy guidance required recognizing these revenues net of the related expenses. Conversely, certain contract costs related to clearing and retail operations are now netted against the revenues while the legacy guidance required recognizing these revenues and expenses on a gross basis. As the measurement and timing of revenue recognition was not affected for any of the Company's revenue streams, the implementation of the new guidance had no impact on opening retained earnings as of January 1, 2018. The enhanced disclosures required by the new standard are being developed and will be included in subsequent filings in accordance with the new standard, but are not expected to have a significant effect on the Company's consolidated financial statements.

34. Selected Quarterly Financial Information (Unaudited)

Selected quarterly financial information is summarized as follows (in thousands, except per share data).

	Year Ended December 31, 2017				
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Full Year
Interest income	$ 133,665	$ 128,944	$ 136,306	$ 108,241	$ 507,156
Interest expense	24,973	23,964	20,330	16,141	85,408
Net interest income	108,692	104,980	115,976	92,100	421,748
Provision for loan losses	5,453	1,260	5,853	1,705	14,271
Noninterest income	290,456	298,477	344,692	271,439	1,205,064
Noninterest expense	328,670	353,842	366,251	320,492	1,369,255
Income before income taxes	65,025	48,355	88,564	41,342	243,286
Income tax expense	51,350	18,003	25,754	15,035	110,142
Net income	13,675	30,352	62,810	26,307	133,144
Less: Net income attributable to noncontrolling interest	247	146	334	(127)	600
Income attributable to Hilltop	$ 13,428	$ 30,206	$ 62,476	$ 26,434	$ 132,544

Earnings per common share:

Basic	$ 0.14	$ 0.31	$ 0.64	$ 0.27	$ 1.36
Diluted	$ 0.14	$ 0.31	$ 0.63	$ 0.27	$ 1.36
Cash dividends declared per common share	$ 0.06	$ 0.06	$ 0.06	$ 0.06	$ 0.24

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Notes to Consolidated Financial Statements (continued)

	Year Ended December 31, 2016				
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Full Year
Interest income	$ 118,335	$ 115,263	$ 114,202	$ 108,154	$ 455,954
Interest expense	14,211	16,093	13,805	14,314	58,423
Net interest income	104,124	99,170	100,397	93,840	397,531
Provision for loan losses	4,347	3,990	28,876	3,407	40,620
Noninterest income	309,127	354,458	346,005	277,375	1,286,965
Noninterest expense	355,784	364,133	367,365	325,189	1,412,471
Income before income taxes	53,120	85,505	50,161	42,619	231,405
Income tax expense	17,582	33,017	18,439	14,423	83,461
Net income	35,538	52,488	31,722	28,196	147,944
Less: Net income attributable to noncontrolling interest	217	556	648	629	2,050
Income attributable to Hilltop	$ 35,321	$ 51,932	$ 31,074	$ 27,567	$ 145,894
Earnings per common share:					
Basic	$ 0.36	$ 0.53	$ 0.32	$ 0.28	$ 1.48
Diluted	$ 0.36	$ 0.53	$ 0.32	$ 0.28	$ 1.48
Cash dividends declared per common share	$ 0.06	$ —	$ —	$ —	$ 0.06

35. Subsequent Event

On February 13, 2018, the Company entered into a definitive agreement to acquire privately-held, Houston-based The Bank of River Oaks (“BORO”) in an all-cash transaction. Under the terms of the definitive agreement, the Company has agreed to pay cash in the aggregate amount of $85 million to the shareholders and option holders of BORO. As of December 31, 2017, BORO had unaudited total assets, gross loans and deposits of approximately $454 million, $344 million and $406 million, respectively. The transaction is subject to customary closing conditions, including regulatory approvals and approval by shareholders of BORO, and is expected to close during the third quarter of 2018.

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

Net of Reinsurance

(in thousands)

	Incurred Losses and Allocated Loss Adjustment Expenses, Net of Reinsurance					December 31, 2017	
	December 31, 2017					Total of Incurred But Not Reported Reserves Plus Development On	Cumulative Number of
Accident Year	2013 Unaudited	2014 Unaudited	2015 Unaudited	2016 Unaudited	2017 Unaudited	Reported Claims	Reported Claims
2013	$ 107,793	$ 108,951	$ 111,006	$ 111,011	$ 111,121	$ 8	15,687
2014		83,784	85,037	84,221	84,074	119	13,099
2015			89,646	88,477	87,262	591	15,016
2016				84,771	85,189	2,622	21,277
2017					88,079	4,282	20,927
					$ 455,725		

	Cumulative Paid Losses and Allocated Loss Adjustment Expenses, Net of Reinsurance				
	December 31, 2017				
Accident Year	2013 Unaudited	2014 Unaudited	2015 Unaudited	2016 Unaudited	2017 Unaudited
2013	$ 94,238	$ 104,938	$ 108,099	$ 109,662	$ 110,813
2014		70,831	79,713	81,684	83,346
2015			71,820	82,940	85,507
2016				71,543	81,682
2017					77,855
Total					$ 439,203
All outstanding reserves prior to 2013, net of reinsurance					948
Reserve for unpaid losses and allocated loss adjustment expenses, net of reinsurance					$ 17,470