

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

**FORM 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the quarterly period ended September 30, 2020  
OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_.  
Commission File Number: 001-36682

**VERITEX HOLDINGS, INC.**

(Exact name of registrant as specified in its charter)

**Texas**  
(State or other jurisdiction of  
incorporation or organization)

**27-0973566**  
(I.R.S. employer  
identification no.)

**8214 Westchester Drive, Suite 800**  
**Dallas, Texas**  
(Address of principal executive offices)

**75225**  
(Zip code)

**(972) 349-6200**

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol	Name of each exchange on which registered
Common Stock, par value \$0.01	VBTX	Nasdaq Global Market

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

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

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

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

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

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

As of November 3, 2020, there were 49,661,232 outstanding shares of the registrant's common stock, par value \$0.01 per share.

VERITEX HOLDINGS, INC. AND SUBSIDIARIES

	<u>Page</u>	
<b><u>PART I — FINANCIAL INFORMATION</u></b>		
<u>Item 1.</u>	<u>Financial Statements – (Unaudited)</u>	3
	<u>Condensed Consolidated Balance Sheets as of September 30, 2020 and December 31, 2019</u>	4
	<u>Condensed Consolidated Statements of Income for the Three and Nine Months Ended September 30, 2020 and 2019</u>	5
	<u>Condensed Consolidated Statements of Comprehensive Income for the Three and Nine Months Ended September 30, 2020 and 2019</u>	6
	<u>Condensed Consolidated Statements of Changes in Stockholders' Equity for the Three and Nine Months Ended September 30, 2020 and 2019</u>	7
	<u>Condensed Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2020 and 2019</u>	9
	<u>Notes to Condensed Consolidated Financial Statements</u>	10
<u>Item 2.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	53
<u>Item 3.</u>	<u>Quantitative and Qualitative Disclosures about Market Risk</u>	84
<u>Item 4.</u>	<u>Controls and Procedures</u>	85
<b><u>PART II — OTHER INFORMATION</u></b>		
<u>Item 1.</u>	<u>Legal Proceedings</u>	86
<u>Item 1A.</u>	<u>Risk Factors</u>	86
<u>Item 2.</u>	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	87
<u>Item 3.</u>	<u>Defaults Upon Senior Securities</u>	88
<u>Item 4.</u>	<u>Mine Safety Disclosures</u>	88
<u>Item 5.</u>	<u>Other Information</u>	88
<u>Item 6.</u>	<u>Exhibits</u>	88
	<b><u>SIGNATURES</u></b>	90

**PART I. FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**VERITEX HOLDINGS, INC. AND SUBSIDIARIES**  
**Condensed Consolidated Balance Sheets**  
**as of September 30, 2020 and December 31, 2019**  
**(Dollars in thousands, except par value and share information)**

	September 30, 2020 (Unaudited)	December 31, 2019
<b>ASSETS</b>		
Cash and due from banks	\$ 40,792	\$ 65,151
Interest bearing deposits in other banks	87,975	186,399
Total cash and cash equivalents	128,767	251,550
Debt securities available-for-sale, at fair value	1,060,456	964,365
Debt securities held-to-maturity (fair value of \$34,223 and \$34,810, at September 30, 2020 and December 31, 2019, respectively)	30,984	32,965
Equity securities	15,180	14,697
Federal Home Loan Bank of Dallas Stock ("FHLB") and Federal Reserve Bank Stock	81,825	68,348
Investment in trusts	1,018	1,018
Total investments	1,189,463	1,081,393
Loans held for sale	13,928	14,080
Loans held for investment, Paycheck Protection Program ("PPP") loans, carried at fair value	405,465	—
Loans held for investment, mortgage warehouse ("MW")	544,845	183,628
Loans held for investment, excluding MW and PPP	5,789,293	5,737,577
Less: Allowance for credit losses	(121,591)	(29,834)
Total loans held for investment, net	6,618,012	5,891,371
Bank-owned life insurance	82,366	80,915
Bank premises, furniture and equipment, net	115,794	118,536
Other real estate owned	5,796	5,995
Intangible assets, net of accumulated amortization of \$28,531 and \$19,997, at September 30, 2020 and December 31, 2019, respectively	64,716	72,263
Goodwill	370,840	370,840
Other assets	112,693	67,994
<b>Total assets</b>	<b>\$ 8,702,375</b>	<b>\$ 7,954,937</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Deposits:		
Noninterest-bearing deposits	\$ 1,920,715	\$ 1,556,500
Interest-bearing transaction and savings deposits	2,821,945	2,654,972
Certificates and other time deposits	1,479,896	1,682,878
<b>Total deposits</b>	<b>6,222,556</b>	<b>5,894,350</b>
Accounts payable and other liabilities	66,096	37,427
Accrued interest payable	3,444	6,569
Advances from FHLB	1,082,756	677,870
Subordinated debentures and subordinated notes	140,158	145,571
Securities sold under agreements to repurchase	2,028	2,353
<b>Total liabilities</b>	<b>7,517,038</b>	<b>6,764,140</b>
Commitments and contingencies (Notes 8 and 11)		
Stockholders' equity:		
Common stock, \$0.01 par value; 75,000,000 shares authorized; 55,464,960 and 54,876,580 shares issued at September 30, 2020 and December 31, 2019, respectively; 49,650,038 and 51,063,869 shares outstanding at September 30, 2020 and December 31, 2019, respectively	555	549
Additional paid-in capital	1,124,148	1,117,879
Retained earnings	157,639	147,911
Accumulated other comprehensive income	47,155	19,061
Treasury stock, 5,814,922 and 3,812,711 shares at cost at September 30, 2020 and December 31, 2019, respectively	(144,160)	(94,603)
<b>Total stockholders' equity</b>	<b>1,185,337</b>	<b>1,190,797</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 8,702,375</b>	<b>\$ 7,954,937</b>

See accompanying Notes to Condensed Consolidated Financial Statements.

**VERITEX HOLDINGS, INC. AND SUBSIDIARIES**  
**Condensed Consolidated Statements of Income (Unaudited)**  
**For the Three and Nine Months Ended September 30, 2020 and 2019**  
**(Dollars in thousands, except per share amounts)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2020	2019	2020	2019
<b>Interest and dividend income:</b>				
Loans, including fees	\$ 68,685	\$ 85,811	\$ 216,986	\$ 258,344
Investment securities	7,852	7,687	23,074	22,316
Deposits in financial institutions and Fed Funds sold	65	1,329	1,122	4,255
Other investments	827	816	2,568	2,129
<b>Total interest and dividend income</b>	<b>77,429</b>	<b>95,643</b>	<b>243,750</b>	<b>287,044</b>
<b>Interest expense:</b>				
Transaction and savings deposits	2,105	10,381	11,128	32,152
Certificates and other time deposits	5,004	10,283	19,759	29,220
Advances from FHLB	2,707	3,081	8,387	7,323
Subordinated debentures and subordinated notes	1,743	1,024	5,444	3,116
<b>Total interest expense</b>	<b>11,559</b>	<b>24,769</b>	<b>44,718</b>	<b>71,811</b>
<b>Net interest income</b>	<b>65,870</b>	<b>70,874</b>	<b>199,032</b>	<b>215,233</b>
Provision for credit losses	8,692	9,674	56,640	18,021
Provision for unfunded commitments	1,447	—	8,127	—
<b>Net interest income after provision for credit losses</b>	<b>55,731</b>	<b>61,200</b>	<b>134,265</b>	<b>197,212</b>
<b>Noninterest income:</b>				
Service charges and fees on deposit accounts	3,130	3,667	9,732	10,606
Loan fees	1,787	2,252	5,027	5,861
(Loss) gain on sales of investment securities	(8)	—	2,871	(1,414)
Gain on sale of mortgage loans held for sale	472	32	922	394
Government guaranteed loan income, net	2,257	930	13,702	4,148
Rental income	502	643	1,600	1,629
Other	1,655	906	4,478	1,724
<b>Total noninterest income</b>	<b>9,795</b>	<b>8,430</b>	<b>38,332</b>	<b>22,948</b>
<b>Noninterest expense:</b>				
Salaries and employee benefits	20,553	17,530	59,442	53,874
Occupancy and equipment	3,980	4,044	12,247	12,187
Professional and regulatory fees	3,159	2,750	8,151	8,982
Data processing and software expense	2,452	2,252	6,975	6,485
Marketing	1,062	708	2,706	2,288
Amortization of intangibles	2,840	2,712	8,232	8,191
Telephone and communications	345	361	972	1,381
Merger and acquisition expense	—	1,035	—	38,042
COVID expenses	132	—	1,377	—
Other	1,885	3,238	11,912	10,089
<b>Total noninterest expense</b>	<b>36,408</b>	<b>34,630</b>	<b>112,014</b>	<b>141,519</b>
<b>Income before income tax expense</b>	<b>29,118</b>	<b>35,000</b>	<b>60,583</b>	<b>78,641</b>
Income tax expense	6,198	7,595	9,501	16,953
<b>Net income</b>	<b>\$ 22,920</b>	<b>\$ 27,405</b>	<b>\$ 51,082</b>	<b>\$ 61,688</b>
Basic earnings per share	\$ 0.46	\$ 0.52	\$ 1.02	\$ 1.15
Diluted earnings per share	\$ 0.46	\$ 0.51	\$ 1.02	\$ 1.13

See accompanying Notes to Condensed Consolidated Financial Statements.

**VERITEX HOLDINGS, INC. AND SUBSIDIARIES**  
**Condensed Consolidated Statements of Comprehensive Income (Unaudited)**  
**For the Three and Nine Months Ended September 30, 2020 and 2019**  
(Dollars in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2020	2019	2020	2019
<b>Net income</b>	\$ 22,920	\$ 27,405	\$ 51,082	\$ 61,688
<b>Other comprehensive income:</b>				
Net unrealized gains on securities available-for-sale:				
Change in net unrealized gains on securities available-for-sale during the period	2,400	7,212	35,660	29,892
Reclassification adjustment for net (gains) losses included in net income	—	—	(2,879)	1,414
Net unrealized gains on securities available-for-sale	2,400	7,212	32,781	31,306
Net unrealized gains on derivative instruments designated as cash flow hedges	4,105	413	3,170	2,033
Other comprehensive income, before tax	6,505	7,625	35,951	33,339
Income tax expense	1,364	1,529	7,857	6,572
Other comprehensive income, net of tax	5,141	6,096	28,094	26,767
<b>Comprehensive income</b>	<u>\$ 28,061</u>	<u>\$ 33,501</u>	<u>\$ 79,176</u>	<u>\$ 88,455</u>

See accompanying Notes to Condensed Consolidated Financial Statements.

VERITEX HOLDINGS, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Changes in Stockholders' Equity (Unaudited)  
For the Three and Nine Months Ended September 30, 2020 and 2019  
(Dollars in thousands)

Three Months Ended September 30, 2020

	Common Stock		Treasury Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total
	Shares	Amount	Shares	Amount				
<b>Balance at June 30, 2020</b>	49,632,747	\$ 555	5,814,922	\$(144,160)	\$ 1,122,063	\$ 143,277	\$ 42,014	\$ 1,163,749
Restricted stock units vested, net of 1,224 shares withheld to cover tax withholdings	14,585	—	—	—	(21)	—	—	(21)
Exercise of employee stock options, no shares withheld for taxes or exercise	2,706	—	—	—	28	—	—	28
Stock based compensation	—	—	—	—	2,078	—	—	2,078
Net income	—	—	—	—	—	22,920	—	22,920
Dividends paid	—	—	—	—	—	(8,558)	—	(8,558)
Other comprehensive income	—	—	—	—	—	—	5,141	5,141
<b>Balance at September 30, 2020</b>	<u>49,650,038</u>	<u>\$ 555</u>	<u>5,814,922</u>	<u>\$(144,160)</u>	<u>\$ 1,124,148</u>	<u>\$ 157,639</u>	<u>\$ 47,155</u>	<u>\$ 1,185,337</u>

Three Months Ended September 30, 2019

	Common Stock		Treasury Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total
	Shares	Amount	Shares	Amount				
<b>Balance at June 30, 2019</b>	53,457,486	\$ 535	1,181,862	\$(29,873)	\$ 1,112,238	\$ 104,652	\$ 17,741	\$ 1,205,293
Restricted stock units vested, net of 148 shares withheld to cover tax withholdings	352	—	—	—	(6)	—	—	(6)
Exercise of employee stock options, no shares withheld for taxes or exercise	92,572	1	—	—	998	—	—	999
Stock buyback	(1,177,241)	(12)	1,177,241	(28,961)	—	—	—	(28,973)
Stock based compensation	—	—	—	—	1,429	—	—	1,429
Reclassification of liability-classified awards to equity awards	—	—	—	—	—	—	—	—
Net income	—	—	—	—	—	27,405	—	27,405
Dividends paid	—	—	—	—	—	(6,713)	—	(6,713)
Other comprehensive income	—	—	—	—	—	—	6,096	6,096
<b>Balance at September 30, 2019</b>	<u>52,373,169</u>	<u>\$ 524</u>	<u>2,359,103</u>	<u>\$(58,834)</u>	<u>\$ 1,114,659</u>	<u>\$ 125,344</u>	<u>\$ 23,837</u>	<u>\$ 1,205,530</u>

**VERITEX HOLDINGS, INC. AND SUBSIDIARIES**  
**Condensed Consolidated Statements of Changes in Stockholders' Equity (Unaudited)**  
**For the Three and Nine Months Ended September 30, 2020 and 2019**  
**(Dollars in thousands)**

Nine Months Ended September 30, 2020

	Common Stock		Treasury Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total
	Shares	Amount	Shares	Amount				
<b>Balance at December 31, 2019</b>	51,063,869	\$ 549	3,812,711	\$ (94,603)	\$ 1,117,879	\$ 147,911	\$ 19,061	\$ 1,190,797
Restricted stock units vested, net of 22,404 shares withheld to cover tax withholdings	100,864	1	—	—	(665)	—	—	(664)
Exercise of employee stock options, net of 98,836 and 139,715 shares withheld to cover tax withholdings and exercise price, respectively	477,516	5	—	—	944	—	—	949
Stock warrants exercised	10,000	—	—	—	109	—	—	109
Stock buyback	(2,002,211)	—	2,002,211	(49,557)	—	—	—	(49,557)
Stock based compensation	—	—	—	—	5,881	—	—	5,881
Net income	—	—	—	—	—	51,082	—	51,082
Dividends paid	—	—	—	—	—	(25,849)	—	(25,849)
CECL impact on date of adoption	—	—	—	—	—	(15,505)	—	(15,505)
Other comprehensive income	—	—	—	—	—	—	28,094	28,094
<b>Balance at September 30, 2020</b>	<u>49,650,038</u>	<u>\$ 555</u>	<u>5,814,922</u>	<u>\$ (144,160)</u>	<u>\$ 1,124,148</u>	<u>\$ 157,639</u>	<u>\$ 47,155</u>	<u>\$ 1,185,337</u>

Nine Months Ended September 30, 2019

	Common Stock		Treasury Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Total
	Shares	Amount	Shares	Amount				
<b>Balance at December 31, 2018</b>	24,253,894	\$ 243	10,000	\$ (70)	\$ 449,427	\$ 83,968	\$ (2,930)	\$ 530,638
Issuance of common shares in connection with the acquisition of Green Bancorp, Inc. ("Green"), net of offering costs of \$788	29,532,957	295	—	—	630,332	—	—	630,627
Issuance of common stock in connection with the acquisition of Green for vested restricted stock units, net of 25,872 shares for taxes	497,594	5	—	—	12,479	—	—	12,484
Restricted stock units vested, net of 53,734 shares withheld to cover tax withholdings	226,581	2	—	—	(1,291)	—	—	(1,289)
Exercise of employee stock options, net of 13,709 shares withheld to cover taxes	211,246	2	—	—	2,389	—	—	2,391
Stock buyback	(2,349,103)	(23)	2,349,103	(58,764)	—	—	—	(58,787)
Stock based compensation	—	—	—	—	19,920	—	—	19,920
Reclassification of liability-classified awards to equity awards	—	—	—	—	1,403	—	—	1,403
Net income	—	—	—	—	—	61,688	—	61,688
Dividends paid	—	—	—	—	—	(20,312)	—	(20,312)
Other comprehensive income	—	—	—	—	—	—	26,767	26,767
<b>Balance at September 30, 2019</b>	<u>52,373,169</u>	<u>\$ 524</u>	<u>2,359,103</u>	<u>\$ (58,834)</u>	<u>\$ 1,114,659</u>	<u>\$ 125,344</u>	<u>\$ 23,837</u>	<u>\$ 1,205,530</u>

See accompanying Notes to Condensed Consolidated Financial Statements.



**VERITEX HOLDINGS, INC. AND SUBSIDIARIES**  
**Condensed Consolidated Statements of Cash Flows (Unaudited)**  
**For the Nine Months Ended September 30, 2020 and 2019**  
**(Dollars in thousands)**

	For the Nine Months Ended September 30,	
	2020	2019
<b>Cash flows from operating activities:</b>		
Net income	\$ 51,082	\$ 61,688
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of fixed assets and intangibles	11,910	12,372
Net accretion of time deposit premium, debt discount, and debt issuance costs	(1,208)	(6,495)
Provision for credit losses and unfunded commitments	64,767	18,021
Accretion of loan purchase discount	(11,407)	(20,241)
Stock-based compensation expense	5,881	19,920
Compensation expense, liability-classified awards	—	1,403
Excess tax (benefit) expense from stock compensation	(1,391)	94
Net amortization of premiums on debt securities	2,483	1,887
Unrealized gain on equity securities recognized in earnings	(512)	(377)
Change in cash surrender value and mortality rates of bank-owned life insurance	(1,451)	(1,506)
Net (gain) loss on sales of investment securities	(2,871)	1,414
Change in fair value of government guaranteed loans using fair value option	2,351	(215)
Gain on sales of mortgage loans held for sale	(923)	(394)
Gain on sales of government guaranteed loans	(3,242)	(3,933)
Originations of loans held for sale	(97,490)	(28,414)
Proceeds from sales of loans held for sale	101,494	28,926
Loss on sale of other real estate owned	83	—
Gain on sale of bank premises, furniture and equipment	(358)	—
Net loss on sale of branches	—	474
Increase in other assets	(35,012)	(687)
Increase (decrease) in accounts payable and other liabilities and accrued interest payable	9,700	(8,623)
Net cash provided by operating activities	93,886	75,502
<b>Cash flows from investing activities:</b>		
Cash received in excess of cash paid for the acquisition of Green	—	112,710
Cash settlement for sale of held for sale branches	—	7,153
Purchases of securities available for sale	(491,724)	(409,453)
Proceeds from sales of securities available for sale	90,897	254,397
Proceeds from maturities, calls and pay downs of available for sale securities	338,146	90,079
Purchases of securities held to maturity	—	(8,137)
Maturity, calls and paydowns of securities held to maturity	1,748	1,214
Purchases of other investments	(13,477)	(26,332)
Proceeds from sales of equity securities	21	—
Net loans originated	(842,847)	(103,790)
Proceeds from sale of Small Business Administration (“SBA”) loans	43,404	47,748
Net additions to bank premises, furniture and equipment	(2,433)	(6,395)
Proceeds from sales of bank premises, furniture and equipment	2,157	—
Proceeds from sales of other real estate owned	3,890	—
Net cash used in investing activities	(870,218)	(40,806)
<b>Cash flows from financing activities:</b>		
Net change in deposits	329,000	(213,005)
Net change in advances from Federal Home Loan Bank	404,886	424,888
Redemption of subordinated debt	(5,000)	—
Net change in securities sold under agreement to repurchase	(325)	(439)
Payments to tax authorities for stock-based compensation	(3,783)	(1,289)
Proceeds from exercise of employee stock options	4,068	2,391
Proceeds from exercise of stock warrants	109	—
Purchase of treasury stock	(49,557)	(58,787)
Dividends paid	(25,849)	(20,312)
Net cash provided by financing activities	653,549	133,447
Net (decrease) increase in cash and cash equivalents	(122,783)	168,143
Cash and cash equivalents at beginning of period	251,550	84,449
Cash and cash equivalents at end of period	\$ 128,767	\$ 252,592

See accompanying Notes to Condensed Consolidated Financial Statements.

**VERITEX HOLDINGS, INC. AND SUBSIDIARIES**  
**Notes to Condensed Consolidated Financial Statements**  
**(Dollars in thousands, except for per share amounts)**

**1. Summary of Significant Accounting Policies**

Nature of Organization

In this report, the words “Veritex”, “the Company,” “we,” “us,” and “our” refer to the combined entities of Veritex Holdings, Inc. and its subsidiaries, including Veritex Community Bank. The word “Holdco” refers to Veritex Holdings, Inc. The word “the Bank” refers to Veritex Community Bank.

Veritex is a Texas state banking organization, with corporate offices in Dallas, Texas, and currently operates 25 branches and one mortgage office located in the Dallas-Fort Worth metroplex, 12 branches in the Houston metropolitan area and one branch in Louisville, Kentucky. The Bank provides a full range of banking services to individual and corporate customers, which include commercial and retail lending, and the acceptance of checking and savings deposits. The Texas Department of Banking and the Board of Governors of the Federal Reserve System are the primary regulators of the Company and the Bank, and both perform periodic examinations to ensure regulatory compliance.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Veritex Holdings Holdings, Inc. and its subsidiaries, including Veritex Community Bank.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America (“GAAP”), but do not include all of the information and footnotes required for complete financial statements. Intercompany transactions and balances are eliminated in consolidation. In management’s opinion, these unaudited condensed consolidated financial statements include all adjustments of a normal recurring nature necessary for a fair statement of the Company’s condensed consolidated financial position at September 30, 2020 and December 31, 2019, condensed consolidated results of operations for the three and nine months ended September 30, 2020 and 2019, condensed consolidated stockholders’ equity for the three and nine months ended September 30, 2020 and 2019 and condensed consolidated cash flows for the nine months ended September 30, 2020 and 2019.

Accounting measurements at interim dates inherently involve greater reliance on estimates than at year end and the results for the interim periods shown herein are not necessarily indicative of results to be expected for the full year due in part to global economic and financial market conditions, interest rates, access to sources of liquidity, market competition and interruptions of business processes. These unaudited condensed consolidated financial statements have been prepared in accordance with GAAP for interim financial information and the instructions to Quarterly Reports on Form 10-Q adopted by the Securities and Exchange Commission (“SEC”). These unaudited condensed consolidated financial statements should be read in conjunction with the Company’s audited consolidated financial statements and notes thereto for the year ended December 31, 2019 included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2019, as filed with the SEC on February 28, 2020.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying notes. These estimates and assumptions may also affect 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 these estimates.

Segment Reporting

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

## Reclassifications

Certain items in the Company's prior year financial statements were reclassified to conform to the current presentation, including (i) the reclassification on the Condensed Consolidated Statement of Income from other noninterest income of \$109 and \$215 to government guaranteed loan income, net for the three and nine months ended September 30, 2019, respectively (ii) the reclassification on the Condensed Consolidated Statement of Income from net gain on sales of loans and other assets owned of \$821 and \$3,933 to government guaranteed loan income, net for the three and nine months ended September 30, 2019, respectively, (iii) the reclassification on the Condensed Consolidated Statement of Income from net gains on sales of loans and other assets owned to gain on sale of mortgage loans held for sale of \$32 and \$394 for the three and nine months ended September 30, 2019, respectively, (iv) the reclassification on the Condensed Consolidated Statement of Income from other income to rental income for \$274 and \$519 for the three and nine months ended September 30, 2019, respectively, and (v) the reclassification on the Condensed Consolidated Statement of Cash Flows from change in other assets to unrealized gain on equity securities recognized in earnings of \$377 for the nine months ended September 30, 2019.

## Earnings Per Share

Earnings per share ("EPS") are based upon the Company's weighted average shares outstanding. The table below sets forth the reconciliation between weighted average shares used for calculating basic and diluted EPS for the three and nine months ended September 30, 2020 and 2019:

	<u>Three Months Ended September 30,</u>		<u>Nine Months Ended September 30,</u>	
	<u>2020</u>	<u>2019</u>	<u>2020</u>	<u>2019</u>
<b>Earnings (numerator)</b>				
Net income	\$ 22,920	\$ 27,405	\$ 51,082	\$ 61,688
<b>Shares (denominator)</b>				
Weighted average shares outstanding for basic EPS	49,647	52,915	49,989	53,721
Dilutive effect of employee stock-based awards	128	953	188	912
Adjusted weighted average shares outstanding	49,775	53,868	50,177	54,633
<b>EPS:</b>				
Basic	\$ 0.46	\$ 0.52	\$ 1.02	\$ 1.15
Diluted	\$ 0.46	\$ 0.51	\$ 1.02	\$ 1.13

For the three and nine months ended September 30, 2020, there were 1,360 and 1,525 antidilutive shares excluded from the diluted EPS weighted average shares outstanding, respectively. For the three and nine months ended September 30, 2019, there were no antidilutive shares excluded from the diluted EPS weighted average shares outstanding.

## Adoption of New Accounting Standards

On January 1, 2020, the Company adopted Accounting Standard Update ("ASU") 2016-13 *Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, which replaces the incurred loss methodology with an expected loss methodology that is referred to as the current expected credit loss ("CECL") methodology. The measurement of expected credit losses under the CECL methodology is applicable to financial assets measured at amortized cost, including loan receivables and held-to-maturity debt securities. It also applies to off-balance sheet ("OBS") credit exposures not accounted for as insurance (loan commitments, standby letters of credit, financial guarantees, and other similar instruments) and net investments in leases recognized by a lessor in accordance with Topic 842 on leases. In addition, Accounting Standards Codification ("ASC") 326 made changes to the accounting for available-for-sale debt securities. One such change is to require credit losses to be presented as an allowance rather than as a write-down on available-for-sale debt securities management does not intend to sell or believes that it is more likely than not they will be required to sell.

The Company adopted ASC 326 using the modified retrospective method for all financial assets measured at amortized cost, net investments in leases and OBS credit exposures. Results for reporting periods beginning after January 1, 2020 are presented under ASC 326 while prior period amounts continue to be reported in accordance with previously applicable GAAP. The Company recorded a net decrease to retained earnings of \$15,505 as of January 1, 2020 for the cumulative effect of adopting ASC 326.

The Company adopted ASC 326 using the prospective transition approach for financial assets purchased with credit deterioration (“PCD”) that were previously classified as purchased credit impaired (“PCI”) and accounted for under ASC 310-30. In accordance with the standard, management did not reassess whether PCI assets met the criteria of PCD assets as of the date of adoption. On January 1, 2020, the amortized cost basis of the PCD assets were adjusted to reflect the addition of \$19,710 of the allowance for credit losses (“ACL”). The remaining noncredit discount will be accreted into interest income at the effective interest rate. As allowed by ASC 326, the Company elected to maintain pools of loans accounted for under ASC 310-30. In accordance with the standard, management did not reassess whether modifications to individual acquired financial assets accounted for in pools were troubled debt restructurings as of the date of adoption.

The following table illustrates the impact of ASC 326.

	January 1, 2020		
	As Reported Under ASC 326	Pre-ASC 326 Adoption	Impact of ASC 326 Adoption
<b>Assets:</b>			
Allowance for credit losses on debt securities held-to-maturity	\$ —	\$ —	\$ —
<b>Allowance for credit losses on loans</b>			
Construction and land	3,760	3,822	(62)
Farmland	65	61	4
1 - 4 family residential	6,002	1,378	4,624
Multi-family residential	2,593	1,965	628
Owner Occupied Commercial Real Estate	13,066	1,978	11,088
Non-Owner Occupied Commercial Real Estate	15,314	8,139	7,175
Commercial	27,729	12,369	15,360
Consumer	442	122	320
Allowance for credit losses on loans	\$ 68,971	\$ 29,834	\$ 39,137
<b>Liabilities:</b>			
Allowance for credit losses on OBS credit exposures	\$ 1,718	\$ 878	\$ 840

In January 2017, the FASB issued ASU 2017-04, *Intangibles - Goodwill and Other (Topic 350) - Simplifying the Test for Goodwill Impairment* (“ASU 2017-04”). ASU 2017-04 simplifies the accounting for goodwill impairment for all entities by requiring impairment charges to be based on the first step in the previous two-step impairment test. Under the new guidance, if a reporting unit’s carrying amount exceeds its fair value, an entity will record an impairment charge based on that difference. The impairment charge will be limited to the amount of goodwill allocated to that reporting unit. The standard eliminates the prior requirement to calculate a goodwill impairment charge using Step 2, which requires an entity to calculate any impairment charge by comparing the implied fair value of goodwill with its carrying amount. ASU 2017-04 was effective for the Company on January 1, 2020 and did not have a material impact on the Company’s financial statements.

In August 2018, the FASB issued ASU 2018-13, *Fair Value Measurement (Topic 820) - Changes to the Disclosure Requirements for Fair Value Measurement* (“ASU 2018-13”). ASU 2018-13 modifies the disclosure requirements on fair value measurements by requiring that Level 3 fair value disclosures include the range and weighted average of significant unobservable inputs used to develop those fair value measurements. For certain unobservable inputs, an entity may disclose other quantitative information in lieu of the weighted average if the entity determines that other quantitative information would be a more reasonable and rational method to reflect the distribution of unobservable inputs used to develop Level 3 fair value measurements. ASU 2018-13 was effective for the Company on January 1, 2020 and did not have a material impact on the Company’s financial statement disclosures.

In August 2018, the FASB issued ASU 2018-15, *Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40) - Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract* (“ASU 2018-15”). ASU 2018-15 aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain

internal-use software (and hosting arrangements that include an internal use software license). The accounting for the service element of a hosting arrangement that is a service contract is not affected by these amendments. ASU 2018-15 was effective for the Company on January 1, 2020 and did not have a material impact on the Company's financial statements.

On March 22, 2020, various regulatory agencies, including the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation, ("the agencies") issued an Interagency Statement on Loan Modifications and Reporting for Financial Institutions Working with Customers Affected by the Coronavirus. The interagency statement was effective immediately and impacted accounting for loan modification using ASC 310-40. The agencies confirmed with the staff of the FASB that short-term modifications made on a good faith basis in response to COVID-19 to borrowers who were current prior to any relief, are not to be considered troubled debt restructurings ("TDRs"). This includes short-term (e.g., six months) modifications such as payment deferrals, fee waivers, extensions of repayment terms, or other delays in payment that are insignificant. Borrowers considered current are those that are less than 30 days past due on their contractual payments at the time a modification program is implemented.

On March 27, 2020, the Coronavirus Aid, Relief and Economic Security ("CARES") Act was passed by Congress. Section 4013 of the CARES Act provides financial institutions with an option to suspend the application of ASC 310-40 to eligible loan restructurings. A loan restructuring is eligible under Section 4013 if the loan restructuring is related to COVID-19, if the loan was not more than 30 days past due as of December 31, 2019, and if the restructuring occurs between March 1, 2020 and the earlier of 60 days after the termination of the national emergency or December 31, 2020. If a loan restructuring is not eligible under Section 4013, or if the financial institution does not elect to avail itself of the optional relief in Section 4013, the financial institution should evaluate the loan restructuring under ASC 310-40 considering the guidance in the interagency statement.

For the nine months ended September 30, 2020, the Company had 741 modifications of loans with aggregate principal balances \$1.2 billion that qualified for temporary suspension of TDR requirements under Section 4013 of the CARES Act. The majority of these modifications allow 90-day deferment of principal and/or interest payments with the ability to request an extension to 180-day deferment of principal and/or interest payments in certain instances. As of October 15, 2020, the Company had \$155.5 million in loans with a remaining deferment.

### Debt Securities

Debt securities that the Company has both the positive intent and ability to hold to maturity are classified as held to maturity and are carried at amortized cost. Debt securities that the Company intends to hold for an indefinite period of time, but not necessarily to maturity, are classified as available for sale and are carried at fair value. Unrealized gains and losses on investment securities classified as available for sale have been accounted for as accumulated other comprehensive income (loss), net of taxes. Management determines the appropriate classification of investment securities at the time of purchase.

Interest income includes amortization of purchase premiums and discounts over the period to maturity using a level-yield method, except for premiums on callable debt securities, which are amortized to their earliest call date. Realized gains and losses are recorded on the sale of debt securities in noninterest income.

The Company has made a policy election to exclude accrued interest from the amortized cost basis of debt securities and report accrued interest separately in other assets on the condensed consolidated balance sheets. A debt security is placed on nonaccrual status at the time any principal or interest payments become more than 90 days delinquent or if full collection of interest or principal becomes uncertain. Accrued interest for a security placed on nonaccrual is reversed against interest income. There was no accrued interest related to debt securities reversed against interest income for the three and nine months ended September 30, 2020 and 2019.

### Allowance for Credit Losses – Available for Sale Securities

For available for sale debt securities in an unrealized loss position, the Company first assesses whether it intends to sell, or it is more likely than not that it will be required to sell the security before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the security's amortized cost basis is written down to fair value through income. For debt securities available for sale that do not meet the aforementioned criteria, the Company evaluates whether the decline in fair value has resulted from credit losses or other factors. In making this assessment, management considers the extent to which fair value is less than amortized cost, any changes to the rating of the security by a rating agency and adverse conditions specifically related to the security, among other factors. If this assessment indicates that a credit loss exists, the present value of cash flows expected to be collected from the security are compared to the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis, a credit loss exists and an ACL is recorded for the credit loss, limited by the amount that the fair value is less than the amortized cost basis. Any impairment that has not been recorded through an ACL is recognized in other comprehensive income.

Changes in the ACL are recorded as provision for (or reversal of) credit loss expense. Losses are charged against the allowance when management believes the uncollectibility of an available for sale security is confirmed or when either of the criteria regarding intent or requirement to sell is met. Accrued interest receivable on available for sale debt securities is excluded from the estimate of credit losses.

### Allowance for Credit Losses – Held to Maturity Securities

Management measures expected credit losses on held to maturity debt securities on a collective basis by major security type. The estimate of expected credit losses considers historical credit loss information that is adjusted for current conditions and reasonable and supportable forecasts. Accrued interest receivable on held to maturity debt securities is excluded from the estimate of credit losses.

Management classifies the held to maturity portfolio into the following major security types: mortgage-backed securities, collateralized mortgage obligations and municipal securities. All of the mortgage-backed securities and collateralized mortgage obligations held by the Company are issued by U.S. government entities and agencies. These securities are either explicitly or implicitly guaranteed by the U.S. government, are highly rated by major rating agencies and have a long history of no credit losses.

### Loans Held for Investment

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at amortized cost, net of the ACL. Amortized cost is the principal balance outstanding, net of purchase premiums and discounts, fair value hedge accounting adjustments, deferred loan fees and costs. The Company has made a policy election to exclude accrued interest from the amortized cost basis of loans and report accrued interest separately from the related loan balance in other assets on the condensed consolidated balance sheets.

Interest on loans is recognized using the effective-interest method on the daily balances of the principal amounts outstanding. Loan origination fees, net of certain direct origination costs, are deferred and recognized in interest income using the level-yield method without anticipating prepayments.

Loans are considered past due if the required principal and interest payments have not been received as of the date such payments were due in accordance with the terms of the loan agreement. The accrual of interest on loans is discontinued when, in management's opinion, the borrower may be unable to meet payment obligations as they come due, as well as when required by regulatory provisions. Loans may be placed on non-accrual status regardless of whether or not such loans are considered past due. When a loan is placed on non-accrual status, all interest accrued but not received for loans placed on nonaccrual is reversed against interest income. Interest received on such loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Under the cost-recovery method, interest income is not recognized until the loan balance is reduced to zero. Under the cash-basis method, interest income is recorded when the payment is received in cash. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

## Acquired Loans

Prior to January 1, 2020, loans acquired in a business combination that had evidence of deterioration of credit quality since origination and for which it was probable, at acquisition, that the Company would be unable to collect all contractually required payments receivable were considered purchased credit impaired (“PCI”). PCI loans were accounted for individually or aggregated into pools of loans based on common risk characteristics such as credit grade, loan type, and date of origination.

All loans considered to be PCI loans prior to January 1, 2020 were converted to PCD loans upon the Company’s adoption of ASC 326. The Company elected to maintain pools of loans that were previously accounted for under ASC 310-30 and will continue to account for these pools as a unit of account for all applicable areas of accounting which include credit loss measurement, interest income recognition, non-accrual determination, write-off determination and trouble debt restructuring identification. Loans are only removed from the existing pools if they are foreclosed, written off, paid off, or sold. Upon adoption of ASC 326, the ACL was determined for each loan or pool and added to the loan or pool’s carrying amount to establish a new amortized cost basis. The difference between the unpaid principal balance of the loan or pool and the new amortized cost basis is the noncredit premium or discount which will be accreted into interest income over the remaining life of the loan or pool. Changes to the ACL after adoption are recorded through provision expense.

Subsequent to January 1, 2020, loans acquired in a business combination that have experienced more-than-insignificant deterioration in credit quality since origination are considered PCD loans. At the acquisition date, an estimate of expected credit losses is made for groups of PCD loans with similar risk characteristics and individual PCD loans without similar risk characteristics. This initial ACL is allocated to individual PCD loans and added to the purchase price or acquisition date fair values to establish the initial amortized cost basis of the PCD loans. As the initial ACL is added to the purchase price, there is no credit loss expense recognized upon acquisition of a PCD loan. Any difference between the unpaid principal balance of PCD loans and the amortized cost basis is considered to relate to noncredit factors and results in a discount or premium. Discounts and premiums are recognized through interest income on a level-yield method over the life of the loans.

For acquired loans not deemed purchased credit deteriorated at acquisition, the differences between the initial fair value and the unpaid principal balance are recognized as interest income on a level-yield basis over the lives of the related loans. At the acquisition date, an initial allowance for expected credit losses is estimated and recorded as credit loss expense.

The subsequent measurement of expected credit losses for all acquired loans is the same as the subsequent measurement of expected credit losses for originated loans.

### Allowance for Credit Losses - Loans

The ACL is a valuation account that is deducted from the loans’ amortized cost basis to present the net amount expected to be collected on the loans.

The Company estimates the ACL on loans based on the underlying assets’ amortized cost basis, which is the amount at which the financing receivable is originated or acquired, adjusted for applicable accretion or amortization of premium, discount, and net deferred fees or costs, collection of cash, and charge-offs. In the event that collection of principal becomes uncertain, the Company has policies in place to reverse accrued interest in a timely manner. Therefore, the Company has made a policy election to exclude accrued interest from the measurement of ACL.

Expected credit losses are reflected in the ACL through a charge to credit loss expense. When the Company deems all or a portion of a financial asset to be uncollectible the appropriate amount is written off and the ACL is reduced by the same amount. The Company applies judgment to determine when a financial asset is deemed uncollectible; however, an asset will typically be considered uncollectible no later than when all efforts at collection have been exhausted. Subsequent recoveries, if any, are credited to the ACL when received.

The Company measures expected credit losses of financial assets on a collective (pool) basis, when the financial assets share similar risk characteristics. Depending on the nature of the pool of financial assets with similar risk characteristics, the Company uses a discounted cash flow (“DCF”) method or a loss-rate method to estimate expected credit losses. The Company will utilize a probability of default/loss given default (“PD/LGD”) model to estimate expected credit losses for our PCD loans and pools.

The Company’s methodologies for estimating the ACL take into account available relevant information about the collectability of cash flows, including information about past events, current conditions, and reasonable and supportable forecasts. The methodologies apply historical loss information, adjusted for asset-specific characteristics, economic conditions

at the measurement date, and forecasts about future economic conditions expected to exist through the contractual lives of the financial assets that are reasonable and supportable, to the identified pools of financial assets with similar risk characteristics for which the historical loss experience was observed.

The Company has identified the following pools of financial assets with similar risk characteristics for measuring expected credit losses:

Real Estate — This category of loans consists of the following loan types:

Construction and land — This category of loans consists of loans to finance the ground up construction, improvement and/or carrying for sale after the completion of construction of owner occupied and non-owner occupied residential and commercial properties, and loans secured by raw or improved land. The repayment of construction loans is generally dependent upon the successful completion of the improvements by the builder for the end user, or sale of the property to a third party. Repayment of land secured loans are dependent upon the successful development and sale of the property, the sale of the land as is, or the outside cash flow of the owners to support the retirement of the debt.

Farmland — These loans are principally loans to purchase farmland.

1-4 family residential — This category of loans includes both first and junior liens on residential real estate. Home equity revolving lines of credit and home equity term loans are included in this group of loans.

Multi-family residential — This category of loans is primarily secured by non-owner occupied apartment or multifamily residential buildings. Generally, these types of loans are thought to involve a greater degree of credit risk than owner occupied commercial real estate as they are more sensitive to adverse economic conditions.

Owner occupied commercial real estate (“OOCRE”) — This category of loans includes real estate loans for a variety of commercial property types and purposes. The repayment of real estate loans is generally largely dependent on the successful operation of the property securing the loans or the business conducted on the property securing the loan. Real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy. The properties securing the Company’s real estate portfolio are generally diverse in terms of type and geographic location, throughout the Dallas-Fort Worth metroplex and Houston metropolitan area. This diversity helps reduce the exposure to adverse economic events that may affect any single market or industry.

Non-owner occupied commercial real estate (“NOOCRE”) — This category of loans includes investment real estate loans that are primarily secured by office and industrial buildings, retail shopping centers and various special purpose properties. Generally, these types of loans are thought to involve a greater degree of credit risk than OOCRE as they are more sensitive to adverse economic conditions.

Commercial — This category of loans is for commercial, corporate and business purposes. The Company’s commercial business loan portfolio is comprised of loans for a variety of purposes and across a variety of industries. These loans include general commercial and industrial loans, loans to purchase capital equipment, agriculture operating loans and other business loans for working capital and operational purposes. Most commercial loans are secured by the assets being financed or other business assets, such as accounts receivable or inventory.

Mortgage warehouse - Mortgage warehouse facilities are provided to unaffiliated mortgage origination companies and are collateralized by 1-4 family residential loans. The originator closes new mortgage loans with the intent to sell these loans to third party investors for a profit. The Company provides funding to the mortgage companies for the period between the origination and their sale of the loan. The Company is repaid with the proceeds received from sale of the mortgage loan to the final investor.

Consumer — This category of loans is used for personal use typically for consumer purposes.

#### *Collateral Dependent Financial Assets*

Loans that do not share risk characteristics are evaluated on an individual basis. For collateral dependent financial assets where the Company has determined that foreclosure of the collateral is probable, or where the borrower is experiencing financial difficulty and the Company expects repayment of the financial asset to be provided substantially through the operation or sale of the collateral, the ACL is measured based on the difference between the fair value of the collateral and the amortized cost basis of the asset as of the measurement date. When repayment is expected to be from the operation of the collateral,



expected credit losses are calculated as the amount by which the amortized cost basis of the financial asset exceeds the present value of expected cash flows from the operation of the collateral. When repayment is expected to be from the sale of the collateral, expected credit losses are calculated as the amount by which the amortized costs basis of the financial asset exceeds the fair value of the underlying collateral less estimated cost to sell. The ACL may be zero if the fair value of the collateral at the measurement date exceeds the amortized cost basis of the financial asset.

For collateralized financial assets that are not collateral dependent, the Company will consider the nature of the collateral, potential future changes in collateral values, and historical loss information for financial assets secured with similar collateral to determine the ACL.

#### *Troubled-debt Restructurings (TDRs)*

From time to time, the Company may modify its loan agreement with a borrower. A modified loan is considered a TDR, using Accounting Standards Codification 310-40, “*Receivables – Troubled Debt Restructurings by Creditors*,” (“ASC 310-40”), when two conditions are met: (i) the borrower is experiencing financial difficulty and (ii) concessions are made by the Company that would not otherwise be considered for a borrower with similar credit risk characteristics. Modifications to loan terms may include a lower interest rate, a reduction of principal, or a longer term to maturity. The ACL on a TDR is measured using the same method as all other loans held for investment, except that the original interest rate is used to discount the expected cash flows, not the rate specified within the restructuring. In addition, when management has a reasonable expectation of executing a TDR the expected effect of the modification is included in the estimate of the ACL.

#### *Contractual Term*

The Company’s estimate of the ACL reflects losses expected over the remaining contractual life of the assets. The contractual term does not consider extensions, renewals or modifications unless the Company has identified an expected TDR.

#### *Discounted Cash Flow Method*

The Company uses the DCF method to estimate expected credit losses for the commercial real estate, construction, land development, land, 1-4 family residential, commercial (excluding liquid credit and premium finance), and consumer loan pools. For each of these loan segments, the Company generates cash flow projections at the instrument level wherein payment expectations are adjusted for estimated prepayment speeds, curtailments, time to recovery, probability of default and loss given default. The modeling of expected prepayment speeds, curtailment rates, and time to recovery are based on historical internal data.

The Company uses regression analysis of historical internal and peer data to determine suitable loss drivers to utilize when modeling lifetime probability of default and loss given default. This analysis also determines how expected probability of default and loss given default will react to forecasted levels of the loss drivers. For all loan pools utilizing the DCF method, management utilizes and forecasts Texas unemployment as a loss driver. Management also utilizes and forecasts either one-year percentage change in Texas gross domestic product or one-year percentage change in the commercial real estate property index as a second loss driver depending on the nature of the underlying loan pool and how well that loss driver correlates to expected future losses.

For all DCF models, management has determined that four quarters represents a reasonable and supportable forecast period and reverts back to a historical loss rate over four quarters on a straight-line basis as of the reporting period. Management leverages economic projections from a reputable and independent third party to inform its loss driver forecasts over the four-quarter forecast period. Other internal and external indicators of economic forecasts are also considered by management when developing the forecast metrics.

The combination of adjustments for credit expectations (default and loss) and timing expectations (prepayment, curtailment, and time to recovery) produces an expected cash flow stream at the instrument level. Instrument effective yield is calculated, net of the impacts of prepayment assumptions, and the instrument expected cash flows are then discounted at that effective yield to produce an instrument-level net present value of expected cash flows (“NPV”). An ACL is established for the difference between the instrument’s NPV and amortized cost basis. The ACL is further increased for qualitative loss factors based on management’s judgment of company, market, industry or business specific data, changes in underlying loan composition of specific portfolios, trends relating to credit quality, delinquency, non-performing and adversely rated loans, and reasonable and supportable forecasts of economic conditions.

### *Loss-Rate Method*

The Company uses a loss-rate method to estimate expected credit losses for its farmland and mortgage warehouse loan pool. For this loan segment, the Company applies an expected loss ratio based on internal and peer historical losses adjusted as appropriate for qualitative factors. Qualitative loss factors are based on management's judgment of company, market, industry or business specific data, changes in underlying loan composition of specific portfolios, trends relating to credit quality, delinquency, non-performing and adversely rated loans, and reasonable and supportable forecasts of economic conditions.

### *Probability of Default/Loss Given Default Method*

The Company uses the PD/LGD method to estimate expected credit losses for the construction and land, 1-4 family residential, OOCRE, NOOCRE, commercial and consumer PCD loan pools. For each of these loan segments, the Company generates cash flow projections at the instrument level wherein payment expectations are adjusted for estimated prepayment speeds, time to recovery, probability of default, and loss given default.

The combination of adjustments for credit expectations (default and loss) and timing expectations (prepayment and time to recovery) produces an expected cash flow stream at the instrument level. An ACL is established for the difference between the instrument's undiscounted cash flows and amortized cost basis. The ACL is further increased for qualitative loss factors based on management's judgment of company, market, industry or business specific data, changes in underlying loan composition of specific portfolios, trends relating to credit quality, delinquency, non-performing and adversely rated loans, and reasonable and supportable forecasts of economic conditions.

### Loan Commitments and Allowance for Credit Losses on Off-Balance Sheet Credit Exposures

Financial instruments include off-balance sheet credit instruments, such as commitments to make loans and standby letters of credit, issued to meet customer financing needs. The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for off-balance sheet loan commitments is represented by the contractual amount of those instruments. Such financial instruments are recorded when they are funded.

The Company records an ACL on off-balance sheet credit exposures, unless the commitments to extend credit are unconditionally cancellable, through a charge to provision for credit losses for unfunded commitments included in the Company's condensed consolidated statements of income. The ACL on off-balance sheet credit exposures is estimated by loan segment at each balance sheet date under the CECL model using the same methodologies as portfolio loans, taking into consideration the likelihood that funding will occur, and is included in accounts payable and other liabilities on the Company's condensed consolidated balance sheets.

### Derivative Financial Instruments (Not Designated as Accounting Hedges)

The Company has entered into certain derivative instruments pursuant to a customer accommodation program under which the Company enters into an interest rate swap, cap or collar agreement with a commercial customer and an agreement with offsetting terms with a correspondent bank. These derivative instruments are not designated as accounting hedges and the changes in net fair value are recognized in noninterest income or expense on the Company's condensed consolidated statements of income and the fair value amounts are included in other assets and accounts payable and other liabilities on the Company's condensed consolidated balance sheets.

### Derivative Financial Instruments (Designated as Cash Flow Hedges)

Cash flow hedge relationships mitigate exposure to the variability of future cash flows or other forecasted transactions. The Company uses interest rate swaps, floors, caps and collars to manage overall cash flow changes related to interest rate risk exposure on benchmark interest rate loans. The entire change in the fair value related to the derivative instrument is recognized as a component of other comprehensive income and subsequently reclassified into interest income when the forecasted transaction affects income.

The Company assesses the “effectiveness” of hedging derivatives on the date an arrangement was entered into and on a prospective basis at least quarterly. Hedge “effectiveness” is determined by the extent to which changes in the fair value of a derivative instrument offset changes in the fair value, cash flows or carrying value attributable to the risk being hedged. If the relationship between the change in the fair value of the derivative instrument and the change in the hedged item falls within a range considered to be the industry norm, the hedge is considered “highly effective” and qualifies for hedge accounting. A hedge is “ineffective” if the relationship between the changes falls outside the acceptable range. In that case, hedge accounting is discontinued on a prospective basis. The time value of the option is excluded from the assessment of effectiveness and is recognized in earnings using a straight-line amortization method over the life of the hedge arrangement. Gains or losses resulting from the termination or sale of a derivative accounted for as a cash flow hedge remain in other comprehensive income and are accreted or amortized to earnings over the remaining period of the former hedging relationship unless the forecasted transaction becomes probable of not occurring.

#### Fair Value Option

On a specific identification basis, the Company may elect the fair value option for certain financial instruments in the period the financial instrument was originated or acquired. As of September 30, 2020, the Company had held for sale government guaranteed loans and held for investment PPP loans that the Company had elected to carry at fair value. Changes in fair value for instruments using the fair value option are recorded in noninterest income. The Company had a change in fair value for loans the Company elected to carry at fair value of \$676 and \$2,351 for the three and nine months ended September 30, 2020, respectively, as compared to \$108 and \$215 for the three and nine months ended September 30, 2019, respectively, that was recorded in government guaranteed loan income, net on the Condensed Consolidated Statements of Income. In addition, the Company records upfront costs and fees as incurred that are related to items for which the fair value option is elected through noninterest income. For the three and nine months ended September 30, 2020, respectively, the Company recognized upfront fees of \$295 and \$12,811 and on PPP loans through government guaranteed loan income, net on the Condensed Consolidated Statements of Income. There were minimal fees recognized on loans electing the fair value option for the three and nine months ended September 30, 2019.

#### Gain on Sale of Guaranteed Portion of SBA Loans

The Company originates loans to customers under government guaranteed programs that generally provide for guarantees of 50% to 90% of each loan, subject to a maximum guaranteed amount. The Company can sell the guaranteed portion of the loan in an active secondary market and retains the unguaranteed portion in its portfolio.

All sales of government guaranteed loans are executed on a servicing retained basis, and the Company retains the rights and obligations to service the loans. The standard sale structure provides for the Company to retain a portion of the cash flow from the interest payment received on the loan. When a loan sale involves the transfer of an interest less than the entire loan, the controlling accounting method under Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 860, Transfers and Servicing, requires the seller to reallocate the carrying basis between the assets transferred and the assets retained based on the relative fair value of the respective assets as of the date of sale. The maximum gain on sale that can be recognized is the difference between the fair value of the assets sold and the reallocated basis of the assets sold. The gain on sale, which is recognized in government guaranteed loan income, net on the Condensed Consolidated Statements of Income, is the sum of the cash premium on the guaranteed loan and the fair value of the servicing assets recognized, less the discount recorded on the unguaranteed portion of the loan retained by the Company. For the three and nine months ended September 30, 2020, the Company recognized \$2,638 and \$3,242 of gain on sales of government guaranteed loans, respectively. For the same periods in 2019, the Company recognized \$822 and \$3,933 of gain on sales of government guaranteed loans, respectively.

## Goodwill

Goodwill resulting from a business combination represents the excess of the fair value of the consideration transferred over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill is not amortized but is reviewed for potential impairment annually on October 31 of each fiscal year or when a triggering event occurs. The Company may first assess qualitative factors to determine whether it is more likely than not (that is, a likelihood of more than 50%) that the fair value of a reporting unit is less than its carrying amount, including goodwill. The Company has an unconditional option to bypass the qualitative assessment for any reporting unit in any period and proceed directly to performing the quantitative goodwill impairment test, and the Company may resume performing the qualitative assessment in any subsequent period. If the Company determines that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, then the Company proceeds to perform the quantitative goodwill impairment test. The quantitative goodwill impairment test, used to identify both the existence of potential impairment and the amount of impairment loss, compares the fair value of a reporting unit with its carrying amount, including goodwill. If the carrying amount of a reporting unit exceeds its fair value, an impairment loss shall be recognized in an amount equal to that excess, limited to the total amount of goodwill allocated to that reporting unit. Any such adjustments to goodwill are reflected in the results of operations in the periods in which they become known.

During the second quarter of 2020, the Company observed a sustained decline in the market valuation of the Company's common stock as a result of continued economic disruption occurring after the first quarter of 2020 primarily due to the COVID-19 pandemic. As a result, the Company determined that it was more likely than not that the fair value of the Company's sole reporting unit was below its carrying value and proceeded to perform an interim quantitative impairment test. The Company determined the fair value of its reporting unit using a combination of a market and an income approach. Upon completion of quantitative evaluation, the Company determined that, as of June 30, 2020, the fair value of the Company's reporting unit exceeded its related carrying value, and therefore goodwill was not impaired. However, changing economic conditions that may adversely affect the Company's performance, the fair value of its assets and liabilities, or its stock price could result in future impairment, which could adversely affect earnings in future periods. During the third quarter of 2020, the Company determined that there was no triggering event that required an interim quantitative impairment assessment to determine if it was more likely than not that the fair value of the Company's sole reporting unit was below its carrying value. Management will continue to monitor events that could impact this conclusion in the future.

## **2. Supplemental Statement of Cash Flows**

Other supplemental cash flow information is presented below:

	Nine Months Ended September 30,	
	2020	2019
	(in thousands)	
<b>Supplemental Disclosures of Cash Flow Information:</b>		
Cash paid for interest	\$ 45,720	\$ 65,897
Cash paid for income taxes	32,590	13,400
<b>Supplemental Disclosures of Non-Cash Flow Information:</b>		
Setup of ROU asset and lease liability upon adoption of ASC 842	\$ —	\$ 9,380
Reclassification of deferred offering costs paid in 2018 from other assets to additional paid in capital	—	788
Reclassification of lease intangibles, cease-use liability and deferred rent liability to ROU asset upon adoption of ASC 842	—	(48)
Net foreclosure of other real estate owned and repossessed assets	4,100	4,625
Transfer of other real estate owned to other assets for losses incurred upon sale and expected to be collected from the SBA	327	—
Reclassification of branch assets held for sale to loans held for investment	—	26,171
Reclassification of branch liabilities held for sale to interest-bearing transaction and savings deposits	—	1,173
<b>Non-cash assets acquired in business combination</b>		
Investment securities	\$ —	\$ 660,792
Non-marketable equity securities	—	40,287
Loans held for sale	—	9,360
Loans held for investment	—	3,245,248
Accrued interest receivable	—	11,395
Bank-owned life insurance	—	56,841
Bank premises, furniture and equipment	—	36,855
Investment in trusts	—	666
Intangible assets, net	—	65,718
Goodwill	—	209,016
Other assets	—	12,649
Right of use asset	—	9,373
Deferred taxes	—	11,930
Current taxes	—	1,812
Assets held for sale	—	85,307
<b>Total assets</b>	<b>\$ —</b>	<b>\$ 4,457,249</b>
<b>Non-cash liabilities assumed in business combination</b>		
Non-interest-bearing deposits	\$ —	\$ 825,364
Interest-bearing deposits	—	1,300,825
Certificates and other time deposits	—	1,346,915
Accounts payable and accrued expenses	—	26,261
Lease liability	—	9,373
Accrued interest payable and other liabilities	—	5,181
Securities sold under agreements to repurchase	—	3,226
Advances from Federal Home Loan Bank	—	300,000
Subordinated debentures and subordinated notes	—	56,233
Liabilities held for sale	—	52,682
<b>Total liabilities</b>	<b>\$ —</b>	<b>\$ 3,926,060</b>

### 3. Share Transactions

On January 28, 2019, the Company's Board of Directors (the "Board") originally authorized a stock buyback program (the "Stock Buyback Program") pursuant to which the Company could, from time to time, purchase up to \$50,000 of its outstanding common stock in the aggregate. The Board authorized increases of \$50,000 on September 3, 2019 and \$75,000 on December 12, 2019, resulting in an aggregate authorization to purchase up to \$175,000 under the Stock Buyback Program. The Board also authorized an extension of the original expiration date of the Stock Buyback Program from December 31, 2019 to December 31, 2020. The shares may be repurchased in the open market or in privately negotiated transactions from time to time, depending upon market conditions and other factors, and in accordance with applicable regulations of the Securities and Exchange Commission. The Stock Buyback Program does not obligate the Company to purchase any share and the program may be terminated or amended by the Board at any time prior to its expiration.

During the three months ended September 30, 2020, there were no shares repurchased through the Stock Buyback Program. During the nine months ended September 30, 2020, 2,002,211 shares were repurchased through the Stock Buyback Program and held as treasury stock at an average price of \$24.78. During the three and nine months ended September 30, 2019, 1,177,241 and 2,349,103 shares were repurchased through the Stock Buyback Program and held as treasury stock at an average price of \$24.61 and \$25.03, respectively.

### 4. Securities

#### Equity Securities With a Readily Determinable Fair Value

The Company held equity securities with a fair value of \$11,605 and \$11,122 at September 30, 2020 and December 31, 2019, respectively. The Company realized a loss of \$8 on equity securities with a readily determinable fair value during the three and nine months ended September 30, 2020. The Company realized no gain or loss on equity securities with a readily determinable fair value during the and same periods in 2019. The gross unrealized gain recognized on equity securities with readily determinable fair values recorded in other noninterest income in the Company's condensed consolidated statements of income were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2020	2019	2020	2019
Unrealized gain recognized on equity securities with a readily determinable fair value	\$ 299	\$ 84	\$ 512	\$ 377

#### Equity Securities Without a Readily Determinable Fair Value

The Company held equity securities without a readily determinable fair values and measured at cost of \$3,575 as of September 30, 2020 and December 31, 2019.

#### Debt Securities

Debt securities have been classified in the condensed consolidated balance sheets according to management's intent. The amortized cost, related gross unrealized gains and losses, allowance for credit losses and the fair value of available for sale and held to maturity securities are as follows:

	September 30, 2020				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Allowance for Credit Losses	Fair Value
<b>Available for sale</b>					
Corporate bonds	\$ 166,655	\$ 5,322	\$ 1,556	\$ —	\$ 170,421
Municipal securities	113,553	8,149	66	—	121,636
Mortgage-backed securities	256,546	17,620	94	—	274,072
Collateralized mortgage obligations	414,430	22,552	40	—	436,942
Asset-backed securities	54,257	3,128	—	—	57,385
	<u>\$ 1,005,441</u>	<u>\$ 56,771</u>	<u>\$ 1,756</u>	<u>\$ —</u>	<u>\$ 1,060,456</u>

	September 30, 2020				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Allowance for Credit Losses
<b>Held to maturity</b>					
Mortgage-backed securities	\$ 7,022	\$ 866	\$ —	\$ 7,888	\$ —
Collateralized mortgage obligations	1,625	118	—	1,743	—
Municipal securities	22,337	2,255	—	24,592	—
	<u>\$ 30,984</u>	<u>\$ 3,239</u>	<u>\$ —</u>	<u>\$ 34,223</u>	<u>\$ —</u>

The Company did not transfer any securities from available for sale to held to maturity at fair value during the three and nine months ended September 30, 2020.

	December 31, 2019			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<b>Available for sale</b>				
Corporate bonds	\$ 76,997	\$ 1,974	\$ —	\$ 78,971
Municipal securities	74,956	3,724	—	78,680
Mortgage-backed securities	288,938	9,512	260	298,190
Collateralized mortgage obligations	431,276	6,465	1,503	436,238
Asset-backed securities	69,964	2,322	—	72,286
	<u>\$ 942,131</u>	<u>\$ 23,997</u>	<u>\$ 1,763</u>	<u>\$ 964,365</u>

<b>Held to maturity</b>				
Mortgage-backed securities	\$ 8,621	\$ 452	\$ —	\$ 9,073
Collateralized mortgage obligations	1,809	43	—	1,852
Municipal securities	22,535	1,350	—	23,885
	<u>\$ 32,965</u>	<u>\$ 1,845</u>	<u>\$ —</u>	<u>\$ 34,810</u>

The following tables disclose the Company's available for sale debt securities in an unrealized loss position for which an allowance for credit losses has not been recorded, aggregated by investment category and length of time that individual securities have been in a continuous loss position:

	September 30, 2020					
	Less Than 12 Months		12 Months or More		Totals	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
<b>Available for sale</b>						
Corporate bonds	\$ 57,195	\$ 1,556	\$ —	\$ —	\$ 57,195	\$ 1,556
Municipal securities	2,920	66	—	—	2,920	66
Mortgage-backed securities	18,453	95	4,603	39	23,056	134
	<u>\$ 78,568</u>	<u>\$ 1,717</u>	<u>\$ 4,603</u>	<u>\$ 39</u>	<u>\$ 83,171</u>	<u>\$ 1,756</u>

	December 31, 2019					
	Less Than 12 Months		12 Months or More		Totals	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
<b>Available for sale</b>						
Municipal securities	\$ 468	\$ 1	\$ —	\$ —	\$ 468	\$ 1
Mortgage-backed securities	28,883	370	—	—	28,883	370
Collateralized mortgage obligations	109,749	1,392	—	—	109,749	1,392
	<u>\$ 139,100</u>	<u>\$ 1,763</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 139,100</u>	<u>\$ 1,763</u>

Management evaluates available for sale debt securities in unrealized loss positions to determine whether the impairment is due to credit-related factors or noncredit-related factors. Consideration is given to (1) the extent to which the fair value is less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the security for a period of time sufficient to allow for any anticipated recovery in fair value.

The number of available for sale debt securities in an unrealized loss position totaled 15 and 11 at September 30, 2020 and December 31, 2019, respectively. Management does not have the intent to sell any of these securities and believes that it is more likely than not that the Company will not have to sell any such securities before a recovery of cost. The fair value is expected to recover as the securities approach their maturity date or repricing date or if market yields for such investments decline. Accordingly, as of September 30, 2020, management believes that the unrealized losses detailed in the previous table are due to noncredit-related factors, including changes in interest rates and other market conditions, and therefore no losses have been recognized in the Company's condensed consolidated statements of income.

The amortized costs and estimated fair values of securities available for sale, by contractual maturity, as of the dates indicated, are shown in the table below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Mortgage-backed securities, collateralized mortgage obligations and asset-backed securities typically are issued with stated principal amounts, and the securities are backed by pools of mortgage loans and other loans that have varying maturities. The terms of mortgage-backed securities, collateralized mortgage obligations and asset-backed securities thus approximates the terms of the underlying mortgages and loans and can vary significantly due to prepayments. Therefore, these securities are not included in the maturity categories below.

	September 30, 2020			
	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	\$ —	\$ —	\$ —	\$ —
Due from one year to five years	4,927	5,162	—	—
Due from five years to ten years	148,194	150,585	3,345	3,596
Due after ten years	127,087	136,310	18,992	20,996
	<u>280,208</u>	<u>292,057</u>	<u>22,337</u>	<u>24,592</u>
Mortgage-backed securities and collateralized mortgage obligations	670,976	711,014	8,647	9,631
Asset-backed securities	54,257	57,385	—	—
	<u>\$ 1,005,441</u>	<u>\$ 1,060,456</u>	<u>\$ 30,984</u>	<u>\$ 34,223</u>



	December 31, 2019			
	Available for Sale		Held to Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due from one year to five years	\$ 4,904	\$ 5,100	\$ —	\$ —
Due from five years to ten years	74,596	76,403	1,204	1,219
Due after ten years	72,453	76,148	21,331	22,666
	151,953	157,651	22,535	23,885
Mortgage-backed securities and collateralized mortgage obligations	720,214	734,428	10,430	10,925
Asset-backed securities	69,964	72,286	—	—
	<u>\$ 942,131</u>	<u>\$ 964,365</u>	<u>\$ 32,965</u>	<u>\$ 34,810</u>

Proceeds from sales of debt securities available for sale and gross gains and losses for the nine months ended September 30, 2020 and 2019 were as follows:

	Nine Months Ended September 30,	
	2020	2019
Proceeds from sales	\$ 90,897	\$ 254,397
Gross realized gains	2,879	522
Gross realized losses	—	1,936

As of September 30, 2020 and December 31, 2019, there were no holdings of securities of any one issuer, other than the U.S. government and its agencies, in an amount greater than 10% of shareholders' equity. There was a blanket floating lien on all debt securities held by the Company to secure FHLB advances as of September 30, 2020 and December 31, 2019.

## 5. Loans and Allowance for Credit Losses

### Loans Held for Investment

Loans held for investment in the accompanying condensed consolidated balance sheets are summarized as follows:

	September 30, 2020	December 31, 2019
<b>Loans held for investment, carried at amortized cost:</b>		
Real estate:		
Construction and land	\$ 623,496	\$ 629,374
Farmland	14,413	16,939
1 - 4 family residential	548,953	549,811
Multi-family residential	412,412	320,041
OOCRE	734,939	706,782
NOOCRE	1,817,013	1,784,201
Commercial	1,623,249	1,712,838
Mortgage warehouse	544,845	183,628
Consumer	14,127	17,457
	<u>6,333,447</u>	<u>5,921,071</u>
Deferred loan costs, net	691	134
Allowance for credit losses	(121,591)	(29,834)
Loans held for investment carried at amortized cost, net	6,212,547	5,891,371
<b>Loans held for investment, carried at fair value:</b>		
PPP loans	405,465	—
Total loans held for investment, net	<u>\$ 6,618,012</u>	<u>\$ 5,891,371</u>

Included in the net loan portfolio as of September 30, 2020 and December 31, 2019 was an accretible discount related to purchased performing and PCD loans, previously called PCI loans prior to the Company's adoption of ASU 2016-13, acquired within a business combination in the approximate amounts of \$18,119 and \$57,811, respectively. The discount is being accreted into income on a level-yield basis over the life of the loans. For the three and nine months ended September 30, 2020, the Company recognized \$2,180 and \$4,375, respectively, of accretion on PCD/PCI loans into interest income. For the nine months ended September 30, 2020 and 2019, the Company recognized \$11,407 and \$13,405, respectively, of accretion on PCD/PCI loans into interest income. In addition, included in the net loan portfolio as of September 30, 2020 and December 31, 2019 is a discount on retained loans from sale of originated SBA loans of \$3,233 and \$2,193, respectively.

Additionally, included in total loans held for investment, as of September 30, 2020, was \$405,465 of PPP loans, which are carried at fair value. During the three and nine months ended September 30, 2020, the Company recognized fee income of \$295 and \$12,811, respectively, which is included in government guaranteed loan income, net on the accompanying condensed consolidated statements of income. During the three and nine months ended September 30, 2020, the Company recognized a valuation discount of \$33 and \$2,038, respectively, which is included in government guaranteed loan income, net on the accompanying condensed consolidated statements of income and in change in fair value of government guaranteed loans using fair value option on the accompanying condensed consolidated statements of cash flows. These PPP loans were originated through the SBA as a result of the Coronavirus Aid, Relief, and Economic Security ("CARES") Act and are considered 100% forgiven if certain criteria are met by the borrowers. As of September 30, 2020, we do not believe any of the Company's PPP loans will not meet such criteria.

The majority of the Company's loan portfolio consists of loans to businesses and individuals in the Dallas-Fort Worth metroplex and the Houston metropolitan area. This geographic concentration subjects the loan portfolio to the general economic conditions within these areas. The risks created by this concentration have been considered by management in the determination of the adequacy of the ACL. Management believes the ACL was adequate to cover estimated losses on loans as of September 30, 2020 and December 31, 2019.

Allowance for Credit Losses

The Company's estimate of the ACL reflects losses expected over the remaining contractual life of the assets. The contractual term does not consider extensions, renewals or modifications unless the Company has identified an expected troubled debt restructuring. The activity in the ACL related to loans held for investment is as follows:

Three Months Ended September 30, 2020									
	Construction and Land	Farmland	Residential	Multifamily	OOCRE	NOOCRE	Commercial	Consumer	Total
Balance at beginning of year	\$ 9,021	\$ 63	\$ 10,777	\$ 6,428	\$ 13,886	\$ 36,067	\$ 38,577	\$ 546	\$ 115,365
Credit loss expense non-PCD loans	610	7	(142)	268	662	(85)	11,425	29	12,774
Credit loss expense PCD loans	(41)	—	(37)	—	(3,578)	(161)	(271)	6	(4,082)
Charge-offs	—	—	—	—	(2,421)	—	(68)	(11)	(2,500)
Recoveries	—	—	7	—	—	—	14	13	34
Ending Balance	<u>\$ 9,590</u>	<u>\$ 70</u>	<u>\$ 10,605</u>	<u>\$ 6,696</u>	<u>\$ 8,549</u>	<u>\$ 35,821</u>	<u>\$ 49,677</u>	<u>\$ 583</u>	<u>\$ 121,591</u>

Three Months Ended September 30, 2019									
	Construction and Land	Farmland	Residential	Multifamily	OOCRE	NOOCRE	Commercial	Consumer	Total
Balance at beginning of year	\$ 3,096	\$ 54	\$ 1,843	\$ 682	\$ 1,654	\$ 6,376	\$ 10,952	\$ 55	\$ 24,712
Credit Loss Expense	453	—	265	—	—	458	8,316	182	9,674
Charge-offs	—	—	—	—	—	—	(8,101)	(113)	(8,214)
Recoveries	—	—	—	—	—	—	71	—	71
Ending Balance	<u>\$ 3,549</u>	<u>\$ 54</u>	<u>\$ 2,108</u>	<u>\$ 682</u>	<u>\$ 1,654</u>	<u>\$ 6,834</u>	<u>\$ 11,238</u>	<u>\$ 124</u>	<u>\$ 26,243</u>

Nine Months Ended September 30, 2020									
	Construction and Land	Farmland	Residential	Multifamily	OOCRE	NOOCRE	Commercial	Consumer	Total
Balance at beginning of year	\$ 3,822	\$ 61	\$ 1,378	\$ 1,965	\$ 1,978	\$ 8,139	\$ 12,369	\$ 122	\$ 29,834
Impact of adopting ASC 326 non-PCD loans	(707)	4	3,716	628	3,406	5,138	7,025	217	19,427
Impact of adoption ASC 326 PCD loans	645	—	908	—	7,682	2,037	8,335	103	19,710
Credit loss expense non-PCD loans	6,393	5	4,955	4,103	3,177	17,294	22,853	3	58,783
Credit loss expense PCD loans	(563)	—	(360)	—	(5,273)	3,213	853	(13)	(2,143)
Charge-offs	—	—	—	—	(2,421)	—	(1,808)	(136)	(4,365)
Recoveries	—	—	8	—	—	—	50	287	345
Ending Balance	<u>\$ 9,590</u>	<u>\$ 70</u>	<u>\$ 10,605</u>	<u>\$ 6,696</u>	<u>\$ 8,549</u>	<u>\$ 35,821</u>	<u>\$ 49,677</u>	<u>\$ 583</u>	<u>\$ 121,591</u>

**Nine Months Ended September 30, 2019**

	Construction and Land	Farmland	Residential	Multifamily	OOCRE	NOOCRE	Commercial	Consumer	Total
Balance at beginning of year	\$ 2,186	\$ 58	\$ 1,614	\$ 361	\$ 1,393	\$ 5,070	\$ 8,554	\$ 19	\$ 19,255
Credit Loss Expense	1,363	(4)	589	321	261	1,764	13,491	236	18,021
Charge-offs	—	—	(157)	—	—	—	(10,898)	(217)	(11,272)
Recoveries	—	—	62	—	—	—	91	86	239
Ending Balance	<u>\$ 3,549</u>	<u>\$ 54</u>	<u>\$ 2,108</u>	<u>\$ 682</u>	<u>\$ 1,654</u>	<u>\$ 6,834</u>	<u>\$ 11,238</u>	<u>\$ 124</u>	<u>\$ 26,243</u>

The following table presents the amortized cost basis of collateral dependent loans, which are individually evaluated to determine expected credit losses, and the related ACL allocated to these loans as of September 30, 2020:

	Business Assets <sup>(1)</sup>	Real Property <sup>(1)</sup>	ACL Allocation
Real estate:			
Construction and land	\$ 785	\$ —	\$ —
1 - 4 family residential	—	2,366	—
OOCRE	2,530	2,779	49
NOOCRE	3,601	33,447	374
Commercial	16,521	25,662	18,419
Consumer	—	1,186	50
Total	<u>\$ 23,437</u>	<u>\$ 65,440</u>	<u>\$ 18,892</u>

<sup>(1)</sup> Loans reported exclude PCD loans that transitioned upon adoption of ASC 326 and accounted for on a pooled basis. Refer to Note 1 for further discussion.

The following table presents loans individually and collectively evaluated for impairment, as well as PCI loans, and their respective allowance for credit loss allocations as of December 31, 2019, as determined in accordance with ASC 310 prior to the Company's adoption of ASU 2016-13:

	December 31, 2019					
	Real Estate					
	Construction, Land and Farmland	Residential	Commercial Real Estate	Commercial	Consumer	Total
Loans individually evaluated for impairment	\$ 567	\$ 156	\$ 21,644	\$ 5,188	\$ 61	\$ 27,616
Loans collectively evaluated for impairment	641,799	865,927	2,372,485	1,869,259	17,267	5,766,737
PCD loans	3,947	3,769	96,854	22,019	129	126,718
Total	<u>\$ 646,313</u>	<u>\$ 869,852</u>	<u>\$ 2,490,983</u>	<u>\$ 1,896,466</u>	<u>\$ 17,457</u>	<u>\$ 5,921,071</u>
<b>ACL Allocations</b>						
Loans individually evaluated for impairment	\$ 128	\$ 37	\$ 395	\$ 1,042	\$ —	\$ 1,602
Loans collectively evaluated for impairment	3,755	3,306	9,702	10,754	122	27,639
PCD loans	—	—	20	573	—	593
Total	<u>\$ 3,883</u>	<u>\$ 3,343</u>	<u>\$ 10,117</u>	<u>\$ 12,369</u>	<u>\$ 122</u>	<u>\$ 29,834</u>

The following table presents information on impaired loans as of December 31, 2019, as determined in accordance with ASC 310 prior to the Company's adoption of ASU 2016-13:

	December 31, 2019 <sup>(1)</sup>					
	Unpaid Contractual Principal Balance	Recorded Investment with No Allowance	Recorded Investment with Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment YTD
Real estate:						
Construction and land	\$ 567	\$ —	\$ 567	\$ 567	\$ 128	\$ 1,793
Farmland	—	—	—	—	—	—
1 - 4 family residential	156	—	156	156	37	158
Multi-family residential	—	—	—	—	—	—
Commercial real estate	21,644	21,040	604	21,644	395	22,529
Commercial	5,188	2,011	3,177	5,188	1,042	8,546
Consumer	61	61	—	61	—	62
Total	\$ 27,616	\$ 23,112	\$ 4,504	\$ 27,616	\$ 1,602	\$ 33,088

<sup>(1)</sup> Loans reported exclude PCI loans.

#### Non-Accrual and Past Due Loans

Loans are considered past due if the required principal and interest payments have not been received as of the date such payments were due in accordance with the terms of the loan agreement. Loans are placed on non-accrual status when, in management's opinion, the borrower may be unable to meet payment obligations as they become due, as well as when required by regulatory provisions. Loans may be placed on non-accrual status regardless of whether or not such loans are considered past due. When interest accrual is discontinued, all unpaid accrued interest is reversed. Interest income is subsequently recognized only to the extent cash payments are received in excess of principal due. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Non-accrual loans aggregated by class of loans, as of September 30, 2020 and December 31, 2019, were as follows:

	September 30, 2020		December 31, 2019	
	Nonaccrual	Nonaccrual With No ACL	Nonaccrual	Nonaccrual With No ACL
Real estate:				
Construction and land	\$ 785	\$ 785	\$ 567	\$ —
Farmland	—	—	—	—
1 - 4 family residential	2,366	2,301	1,581	1,581
Multi-family residential	—	—	—	—
OOCRE	5,310	5,567	3,029	2,778
NOOCRE	37,048	35,939	18,876	18,876
Commercial	42,182	3,677	5,672	2,747
Mortgage warehouse	—	—	—	—
Consumer	1,186	122	54	54
Total	\$ 88,877	\$ 48,391	\$ 29,779	\$ 26,036

There were \$2,086 of PCD loans that are not accounted for on a pooled basis included in non-accrual loans at September 30, 2020. There were no PCD loans included in non-accrual loans at December 31, 2019.

During the three and nine months ended September 30, 2020, interest income not recognized on non-accrual loans was \$2,457 and \$2,993, respectively. During the three and nine months ended September 30, 2019, interest income not recognized on non-accrual loans, excluding PCI loans, was \$243 and \$530, respectively.

An age analysis of past due loans, aggregated by class of loans and including past due non-accrual loans, as of September 30, 2020 and December 31, 2019, is as follows:

September 30, 2020									
	30 to 59 Days	60 to 89 Days	90 Days or Greater	Total Past Due	Total Current	PCD	Total Loans	Total 90 Days Past Due and Still Accruing <sup>(1)</sup>	
Real estate:									
Construction and land	\$ 735	\$ —	\$ 785	\$ 1,520	\$ 619,291	\$ 2,685	\$ 623,496	\$ —	
Farmland	—	—	—	—	14,413	—	14,413	—	
1 - 4 family residential	630	175	3,791	4,596	540,090	4,267	548,953	1,569	
Multi-family residential	—	—	—	—	412,412	—	412,412	—	
OOCRE	1,124	3,064	462	4,650	690,616	39,673	734,939	—	
NOOCRE	—	—	17,697	17,697	1,746,641	52,675	1,817,013	—	
Commercial	3,225	7,656	16,707	27,588	1,573,296	22,365	1,623,249	75	
Mortgage warehouse	—	—	—	—	544,845	—	544,845	—	
Consumer	41	147	1,121	1,309	12,611	207	14,127	45	
<b>Total</b>	<b>\$ 5,755</b>	<b>\$ 11,042</b>	<b>\$ 40,563</b>	<b>\$ 57,360</b>	<b>\$ 6,154,215</b>	<b>\$ 121,872</b>	<b>\$ 6,333,447</b>	<b>\$ 1,689</b>	

<sup>(1)</sup> Loans 90 days past due and still accruing excludes \$33,188 of pooled PCD loans as of September 30, 2020 that transitioned upon adoption of ASC 326. Refer to Note 1 for further discussion.

December 31, 2019									
	30 to 59 Days	60 to 89 Days	90 Days or Greater	Total Past Due	Total Current	PCD	Total Loans	Total 90 Days Past Due and Still Accruing <sup>(1)</sup>	
Real estate:									
Construction and land	\$ —	\$ —	\$ —	\$ —	\$ 629,374	\$ 3,947	\$ 629,374	\$ 800	
Farmland	—	—	—	—	16,939	—	16,939	—	
1 - 4 family residential	2,595	520	1,155	4,270	541,772	3,769	549,811	959	
Multi-family residential	—	—	—	—	320,041	—	320,041	—	
Commercial real estate	12	3,834	868	4,714	2,389,415	96,854	2,490,983	511	
Commercial	3,572	1,707	1,497	6,776	1,684,043	22,019	1,712,838	1,317	
Mortgage warehouse	—	—	—	—	183,628	—	183,628	—	
Consumer	30	2,641	140	2,811	14,646	129	17,457	73	
<b>Total</b>	<b>\$ 6,209</b>	<b>\$ 8,702</b>	<b>\$ 3,660</b>	<b>\$ 18,571</b>	<b>\$ 5,779,858</b>	<b>\$ 126,718</b>	<b>\$ 5,921,071</b>	<b>\$ 3,660</b>	

<sup>(1)</sup> Loans 90 days past due and still accruing excludes \$41,328 of PCD loans accounted for on a pooled basis as of December 31, 2019.

Loans past due 90 days and still accruing were \$1,689 as of September 30, 2020. These loans are also considered well-secured, and are in the process of collection with plans in place for the borrowers to bring the notes fully current or to subsequently be renewed. The Company believes that it will collect all principal and interest due on each of the loans past due 90 days and still accruing.

#### *Troubled Debt Restructuring*

Modifications of terms for the Company's loans and their inclusion as TDRs are based on individual facts and circumstances. Loan modifications that are included as TDRs may involve a reduction of the stated interest rate of the loan, an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk, or deferral of principal payments, regardless of the period of the modification. The recorded investment in TDRs was \$29,659 and \$2,142 as of September 30, 2020 and December 31, 2019, respectively.

The following table presents the pre- and post-modification amortized cost of loans modified as TDRs during the nine months ended September 30, 2020. There were no new TDRs during the three and nine months ended September 30, 2019. The Company did not grant principal reductions or interest rate concessions on any TDRs during the three and nine months ended September 30, 2020.

	During the Three Months Ended September 30, 2020			
	Adjusted Payment Structure	Payment Deferrals	Total Modifications	Number of Loans
Commercial real estate	\$ 5,145	\$ 19,359	\$ 24,504	8
Total	\$ 5,145	\$ 19,359	\$ 24,504	8

	During the Nine Months Ended September 30, 2020			
	Adjusted Payment Structure	Payment Deferrals	Total Modifications	Number of Loans
Commercial real estate	\$ 5,145	\$ 19,359	\$ 24,504	8
Commercial	1,440	1,337	2,777	3
Total	\$ 6,585	\$ 20,696	\$ 27,281	11

There were no loans modified as TDR loans within the previous 12 months and for which there was a payment default during the three and nine months ended September 30, 2020 and 2019. A default for purposes of this disclosure is a TDR loan in which the borrower is 90 days past due or results in the foreclosure and repossession of the applicable collateral.

Interest income recorded during the three and nine months ended September 30, 2020 and 2019 on TDR loans and interest income that would have been recorded had the terms of the loans not been modified was minimal. As of September 30, 2020, there were seven TDR loans in compliance with modified terms with a balance of \$6,429. As of December 31, 2019, there were four TDR loans in compliance with modified terms with a balance of \$686.

The Company has not committed to lend additional amounts to customers with outstanding loans classified as TDRs as of September 30, 2020 or December 31, 2019.

#### *Credit Quality Indicators*

From a credit risk standpoint, the Company classifies its loans in one of the following categories: (i) pass, (ii) special mention, (iii) substandard or (iv) doubtful. Loans classified as loss are charged-off. Loans not rated special mention, substandard, doubtful or loss are classified as pass loans.

The classifications of loans reflect a judgment about the risks of default and loss associated with the loan. The Company reviews the ratings on criticized credits monthly. Ratings are adjusted to reflect the degree of risk and loss that is felt to be inherent in each credit as of each monthly reporting period. All classified credits are evaluated for impairment. If impairment is determined to exist, a specific reserve is established. The Company's methodology is structured so that specific reserves are increased in accordance with deterioration in credit quality (and a corresponding increase in risk and loss) or decreased in accordance with improvement in credit quality (and a corresponding decrease in risk and loss).

Credits rated special mention show clear signs of financial weaknesses or deterioration in credit worthiness, however, such concerns are generally not so pronounced that the Company expects to experience significant loss within the short-term. Such credits typically maintain the ability to perform within standard credit terms and credit exposure is not as prominent as credits with a lower rating.

Credits rated substandard are those in which the normal repayment of principal and interest may be, or has been, jeopardized by reason of adverse trends or developments of a financial, managerial, economic or political nature, or important weaknesses which exist in collateral. A protracted workout on these credits is a distinct possibility. Prompt corrective action is therefore required to strengthen the Company's position, and/or to reduce exposure and to assure that adequate remedial measures are taken by the borrower. Credit exposure becomes more likely in such credits and a serious evaluation of the secondary support to the credit is performed.

Credits rated doubtful are those in which full collection of principal appears highly questionable, and in which some degree of loss is anticipated, even though the ultimate amount of loss may not yet be certain and/or other factors exist which could affect collection of debt. Based upon available information, positive action by the Company is required to avert or minimize loss. Credits rated doubtful are generally also placed on non-accrual.

Credits classified as PCD are those that, at acquisition date, have experienced a more-than-insignificant deterioration in credit quality since origination. All loans considered to be PCI loans prior to January 1, 2020 were converted to PCD loans upon adoption of ASC 326. The Company elected to maintain pools of loans that were previously accounted for under ASC 310-30 and will continue to account for these pools as a unit of account. Loans are only removed from the existing pools if they are foreclosed, written off, paid off, or sold.

The Company considers the guidance in ASC 310-20 when determining whether a modification, extension or renewal of a loan constitutes a current period origination. Generally, current period renewals of credit are reunderwritten at the point of renewal and considered current period originations for purposes of the table below. Based on the most recent analysis performed, the risk category of loans by class of loans based on year of origination is as follows:

	Term Loans Amortized Cost Basis by Origination Year <sup>1</sup>						Revolving Loans Amortized Cost Basis	Revolving Loans Converted to Term	Total
	2020	2019	2018	2017	2016	Prior			
<b>As of September 30, 2020</b>									
<b>Construction and land:</b>									
Pass	\$ 75,351	\$ 254,891	\$ 209,706	\$ 14,652	\$ 11,642	\$ 29,461	\$ 20,589	\$ —	\$ 616,292
Special mention	—	222	2,657	—	—	—	—	—	2,879
Substandard	—	—	855	785	—	—	—	—	1,640
PCD	—	—	—	—	—	2,685	—	—	2,685
<b>Total construction and land</b>	<b>\$ 75,351</b>	<b>\$ 255,113</b>	<b>\$ 213,218</b>	<b>\$ 15,437</b>	<b>\$ 11,642</b>	<b>\$ 32,146</b>	<b>\$ 20,589</b>	<b>\$ —</b>	<b>\$ 623,496</b>
<b>Farmland:</b>									
Pass	\$ 552	\$ 973	\$ 3,367	\$ 3,926	\$ —	\$ 4,275	\$ 1,320	\$ —	\$ 14,413
<b>Total farmland</b>	<b>\$ 552</b>	<b>\$ 973</b>	<b>\$ 3,367</b>	<b>\$ 3,926</b>	<b>\$ —</b>	<b>\$ 4,275</b>	<b>\$ 1,320</b>	<b>\$ —</b>	<b>\$ 14,413</b>
<b>1 - 4 family residential:</b>									
Pass	\$ 112,975	\$ 86,456	\$ 98,312	\$ 53,987	\$ 37,532	\$ 119,792	\$ 24,514	\$ 2,998	\$ 536,566
Special mention	—	1,082	434	769	—	724	—	—	3,009
Substandard	10	—	143	1,023	—	3,010	925	—	5,111
PCD	—	—	—	—	—	4,267	—	—	4,267
<b>Total 1 - 4 family residential</b>	<b>\$ 112,985</b>	<b>\$ 87,538</b>	<b>\$ 98,889</b>	<b>\$ 55,779</b>	<b>\$ 37,532</b>	<b>\$ 127,793</b>	<b>\$ 25,439</b>	<b>\$ 2,998</b>	<b>\$ 548,953</b>
<b>Multi-family residential:</b>									
Pass	\$ 57,512	\$ 114,060	\$ 140,983	\$ 23,268	\$ 36,323	\$ 8,218	\$ 727	\$ —	\$ 381,091
Special mention	—	—	12,661	—	—	—	—	—	12,661
Substandard	—	18,660	—	—	—	—	—	—	18,660
<b>Total multi-family residential</b>	<b>\$ 57,512</b>	<b>\$ 132,720</b>	<b>\$ 153,644</b>	<b>\$ 23,268</b>	<b>\$ 36,323</b>	<b>\$ 8,218</b>	<b>\$ 727</b>	<b>\$ —</b>	<b>\$ 412,412</b>
<b>OOCRE:</b>									
Pass	\$ 93,273	\$ 63,349	\$ 84,361	\$ 77,012	\$ 82,610	\$ 198,213	\$ 7,447	\$ —	\$ 606,265
Special mention	—	2,697	24,623	3,698	13,046	4,341	1,992	—	50,397
Substandard	370	—	10,603	2,679	11,515	6,899	232	6,306	38,604
PCD	—	—	10,263	—	7,970	21,440	—	—	39,673



Total OOCRE	\$ 93,643	\$ 66,046	\$ 129,850	\$ 83,389	\$ 115,141	\$ 230,893	\$ 9,671	\$ 6,306	\$ 734,939
NOOCRE:									
Pass	\$ 220,048	\$ 268,223	\$ 441,601	\$ 99,787	\$ 193,174	\$ 321,236	\$ 13,553	\$ —	\$ 1,557,622
Special mention	101	30,115	37,444	19,399	26,125	37,979	493	—	151,656
Substandard	1,110	7,878	4,573	4,229	—	23,174	14,096	—	55,060
PCD	—	—	18,655	—	6,670	27,350	—	—	52,675
Total NOOCRE	\$ 221,259	\$ 306,216	\$ 502,273	\$ 123,415	\$ 225,969	\$ 409,739	\$ 28,142	\$ —	\$ 1,817,013
Commercial:									
Pass	\$ 182,768	\$ 178,850	\$ 139,191	\$ 64,018	\$ 27,149	\$ 44,087	\$ 794,733	\$ 13,815	\$ 1,444,611
Special mention	1,311	2,557	10,547	11,331	1,289	2,294	32,024	3,864	65,217
Substandard	—	4,742	34,363	3,523	7,980	2,378	32,727	5,343	91,056
PCD	—	—	—	3,287	4,280	14,798	—	—	22,365
Total commercial	\$ 184,079	\$ 186,149	\$ 184,101	\$ 82,159	\$ 40,698	\$ 63,557	\$ 859,484	\$ 23,022	\$ 1,623,249
Mortgage warehouse:									
Pass	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 544,845	\$ —	\$ 544,845
Total mortgage warehouse	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 544,845	\$ —	\$ 544,845
Consumer:									
Pass	\$ 2,170	\$ 1,695	\$ 1,153	\$ 4,209	\$ 934	\$ 478	\$ 1,610	\$ —	\$ 12,249
Special mention	—	—	—	45	30	234	5	—	314
Substandard	—	—	—	60	—	234	1,063	—	1,357
PCD	—	—	—	38	—	169	—	—	207
Total consumer	\$ 2,170	\$ 1,695	\$ 1,153	\$ 4,352	\$ 964	\$ 1,115	\$ 2,678	\$ —	\$ 14,127
Total Pass	\$ 744,649	\$ 968,497	\$ 1,118,674	\$ 340,859	\$ 389,364	\$ 725,760	\$ 1,409,338	\$ 16,813	\$ 5,713,954
Total Special Mention	1,412	36,673	88,366	35,242	40,490	45,572	34,514	3,864	286,133
Total Substandard	1,490	31,280	50,537	12,299	19,495	35,695	49,043	11,649	211,488
Total PCD	—	—	28,918	3,325	18,920	70,709	—	—	121,872
Total	\$ 747,551	\$ 1,036,450	\$ 1,286,495	\$ 391,725	\$ 468,269	\$ 877,736	\$ 1,492,895	\$ 32,326	\$ 6,333,447

<sup>1</sup> Term loans amortized cost basis by origination year excludes \$691 of deferred loan costs, net.

The following table summarizes the Company's internal ratings of its loans, including PCD loans, as of December 31, 2019:

December 31, 2019

	Pass	Special Mention	Substandard	Doubtful	PCD	Total
<b>Real estate:</b>						
Construction and land	\$ 618,773	\$ 3,965	\$ 2,689	\$ —	\$ 3,947	\$ 629,374
Farmland	16,939	—	—	—	—	16,939
1 - 4 family residential	541,787	795	3,460	—	3,769	549,811
Multi-family residential	320,041	—	—	—	—	320,041
Commercial real estate	2,332,357	23,494	38,278	—	96,854	2,490,983
Commercial	1,610,150	51,999	28,670	—	22,019	1,712,838
Mortgage warehouse	183,628	—	—	—	—	183,628
Consumer	17,106	40	182	—	129	17,457
<b>Total</b>	<b>\$ 5,640,781</b>	<b>\$ 80,293</b>	<b>\$ 73,279</b>	<b>\$ —</b>	<b>\$ 126,718</b>	<b>\$ 5,921,071</b>

Purchased Credit Impaired Loans (Prior to the Adoption of ASU 2016-13)

Loans acquired with evidence of credit quality deterioration at acquisition, for which it was probable that the Company would not be able to collect all contractual amounts due, were accounted for as PCI loans. The carrying amount of PCI loans included in the condensed consolidated balance sheets and the related outstanding balances at December 31, 2019 are set forth in the table below. The outstanding balance represents the total amount owed, including accrued but unpaid interest, and any amounts previously charged off.

	December 31, 2019
Carrying amount	\$ 126,125
Outstanding balance	157,417

Changes in the accretible yield for PCI loans for the three and nine months ended September 30, 2019 are included in table below.

	Three Months Ended	Nine Months Ended
	September 30, 2019	September 30, 2019
Balance at beginning of period	\$ 33,709	\$ 18,747
Additions	—	18,073
Reclassifications from nonaccretible	9,309	11,195
Accretion	(4,149)	(9,146)
<b>Balance at end of period</b>	<b>\$ 38,869</b>	<b>\$ 38,869</b>

During the three and nine months ended September 30, 2019, the Company received cash collections in excess of expected cash flows on PCI loans accounted for individually and not aggregated into loan pools of \$28 and \$441, respectively.

## Servicing Assets

The Company was servicing loans of approximately \$234,330 and \$241,733 as of September 30, 2020 and 2019, respectively. A summary of the changes in the related servicing assets are as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2020	2019	2020	2019
Balance at beginning of period	\$ 2,940	\$ 3,793	\$ 3,113	\$ 1,304
Servicing asset acquired through acquisition	—	—	—	2,382
Increase from loan sales	705	534	836	995
Recovery or (amortization/impairment) charged to income	140	(806)	(164)	(1,160)
Balance at end of period	\$ 3,785	\$ 3,521	\$ 3,785	\$ 3,521

The estimated fair value of the servicing assets approximated the carrying amount at September 30, 2020, December 31, 2019 and September 30, 2019. Fair value is estimated by discounting estimated future cash flows from the servicing assets using discount rates that approximate current market rates over the expected lives of the loans being serviced. A valuation allowance is recorded when the fair value is below the carrying amount of the asset.

The Company may also receive a portion of subsequent interest collections on loans sold that exceed the contractual servicing fees. In that case, the Company records an interest-only strip based on its relative fair market value and the other components of the loans. There was no interest-only strip receivable recorded at September 30, 2020 and December 31, 2019.

## 6. Fair Value

The following table summarizes assets measured at fair value on a recurring basis as of September 30, 2020 and December 31, 2019, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

	September 30, 2020			
	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
<b>Financial Assets:</b>				
Available for sale securities	\$ —	\$ 1,060,456	\$ —	\$ 1,060,456
Equity securities with a readily determinable fair value	11,605	—	—	11,605
PPP loans	—	405,465	—	405,465
Loans held for sale <sup>(1)</sup>	—	5,778	—	5,778
Interest rate swap designated as hedging instruments	—	6,621	—	6,621
Customer interest rate swaps not designated as hedging instruments	—	13,396	—	13,396
Correspondent interest rate caps and collars not designated as hedging instruments	—	2	—	2
<b>Financial Liabilities:</b>				
Interest rate swap designated as hedging instruments	—	3,373	—	3,373
Correspondent interest rate swaps not designated as hedging instruments	—	14,259	—	14,259
Customer interest rate caps and collars not designated as hedging instruments	—	2	—	2

<sup>(1)</sup> Represents loans held for sale elected to be carried at fair value upon origination or acquisition.

	December 31, 2019			
	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
<b>Financial Assets:</b>				
Available for sale securities	\$ —	\$ 964,365	\$ —	\$ 964,365
Equity securities with a readily determinable fair value	11,122	—	—	11,122
Loans held for sale <sup>(1)</sup>	—	10,068	—	10,068
Correspondent interest rate swaps	—	105	—	105
Customer interest rate swaps	—	4,393	—	4,393
Correspondent interest rate caps and collars	—	11	—	11
Commercial loan interest rate floor	—	3,353	—	3,353
<b>Financial Liabilities:</b>				
Correspondent interest rate swaps	—	4,736	—	4,736
Customer interest rate swaps	—	84	—	84
Customer interest rate caps and collars	—	11	—	11

<sup>(1)</sup> Represents loans held for sale elected to be carried at fair value upon origination or acquisition.

There were no transfers between Level 2 and Level 3 during the nine months ended September 30, 2020 and 2019.

The following table summarizes assets measured at fair value on a non-recurring basis as of September 30, 2020 and December 31, 2019, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

	Fair Value Measurements Using			Total Fair Value
	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	
<b>As of September 30, 2020</b>				
<b>Assets:</b>				
Collateral dependent loans with an allowance	\$ —	\$ —	\$ 40,486	\$ 40,486
<b>As of December 31, 2019</b>				
<b>Assets:</b>				
Impaired loans	—	—	4,504	4,504
Other real estate owned	—	—	5,995	5,995

At September 30, 2020, collateral dependent loans with an allowance had a recorded investment of \$40,486, with \$18,892 specific allowance for credit loss allocated. At December 31, 2019, impaired loans had a carrying value of \$4,504, with \$1,602 specific allowance for credit loss allocated.

Other real estate owned consisted of four properties recorded with a fair value of approximately \$5,995 at December 31, 2019.

There were no liabilities measured at fair value on a non-recurring basis as of September 30, 2020 or December 31, 2019.

#### Fair Value of Financial Instruments

The Company's methods of determining fair value of financial instruments in this Note are consistent with its methodologies disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2019. Please refer to Note 17 in the Company's Annual Report on Form 10-K for information on these methods.

The estimated fair values and carrying values of all financial instruments not measured at fair value on a recurring basis under current authoritative guidance as of September 30, 2020 and December 31, 2019 were as follows:

	Carrying Amount	Fair Value		
		Level 1	Level 2	Level 3
<b>September 30, 2020</b>				
Financial assets:				
Cash and cash equivalents	\$ 128,767	\$ —	\$ 128,767	\$ —
Held to maturity investments	30,984	—	34,223	—
Loans held for sale <sup>(1)</sup>	8,150	—	8,150	—
Loans held for investment <sup>(2)</sup>	6,334,138	—	—	6,371,257
Accrued interest receivable	28,205	—	28,205	—
Bank-owned life insurance	82,366	—	82,366	—
Servicing asset	3,785	—	3,654	—
Equity securities without a readily determinable fair value	3,575	N/A	N/A	N/A
Federal Home Loan Bank and Federal Reserve Bank stock	81,825	N/A	N/A	N/A
Financial liabilities:				
Deposits	\$ 6,222,556	\$ —	\$ 6,253,626	\$ —
Advances from FHLB	1,082,756	—	1,096,643	—
Accrued interest payable	3,444	—	3,444	—
Subordinated debentures and subordinated notes	140,158	—	140,158	—
Securities sold under agreement to repurchase	2,028	—	2,028	—
<b>December 31, 2019</b>				
Financial assets:				
Cash and cash equivalents	\$ 251,550	\$ —	\$ 251,550	\$ —
Held to maturity investments	32,965	—	34,810	—
Loans held for sale <sup>(1)</sup>	4,012	—	4,012	—
Loans held for investment <sup>(2)</sup>	5,921,205	—	—	5,899,945
Accrued interest receivable	19,508	—	19,508	—
Bank-owned life insurance	80,915	—	80,915	—
Servicing asset	3,113	—	3,113	—
Equity securities without a readily determinable fair value	3,575	N/A	N/A	N/A
Federal Home Loan Bank and Federal Reserve Bank stock	68,348	N/A	N/A	N/A
Financial liabilities:				
Deposits	\$ 5,894,350	\$ —	\$ 5,692,217	\$ —
Advances from FHLB	677,870	—	708,692	—
Accrued interest payable	5,893	—	5,893	—
Subordinated debentures and subordinated notes	145,571	—	145,571	—
Other borrowings	2,353	—	2,353	—

<sup>(1)</sup> Loans held for sale represent mortgage loans held for sale that are carried at lower of cost or market.

<sup>(2)</sup> Loans held for investment includes mortgage warehouse and is carried at amortized cost.

## 7. Derivative Financial Instruments

The Company primarily uses derivatives to manage exposure to market risk, including interest rate risk and credit risk and to assist customers with their risk management objectives. Management will designate certain derivatives as hedging instruments in a qualifying hedge accounting relationship. The Company's remaining derivatives consist of derivatives held for customer accommodation or other purposes.

The fair value of derivative positions outstanding is included in other assets and accounts payable and other liabilities on the accompanying condensed consolidated balance sheets and in the net change in each of these financial statement line items in the accompanying condensed consolidated statements of cash flows. For derivatives not designated as hedging instruments, gains and losses due to changes in fair value are included in other noninterest income and the operating section of the condensed consolidated statement of cash flows. For derivatives designated as hedging instruments, the entire change in the fair value related to the derivative instrument is recognized as a component of other comprehensive income and subsequently reclassified into interest income or interest expense when the forecasted transaction affects income. The notional amounts and estimated fair values as of September 30, 2020 and December 31, 2019 are as shown in the table below.

	September 30, 2020			December 31, 2019		
	Notional Amount	Estimated Fair Value		Notional Amount	Estimated Fair Value	
		Asset Derivative	Liability Derivative		Asset Derivative	Liability Derivative
<b>Derivatives designated as hedging instruments (cash flow hedges):</b>						
Interest rate swap on borrowing advances	\$ 500,000	\$ 6,621	\$ —	\$ —	\$ —	\$ —
Interest rate swap on money market deposit account payments	250,000	—	3,373	—	—	—
Commercial loan interest rate floor	—	—	—	275,000	3,353	—
<b>Total derivatives designated as hedging instruments</b>	<b>\$ 750,000</b>	<b>\$ 6,621</b>	<b>\$ 3,373</b>	<b>\$ 275,000</b>	<b>\$ 3,353</b>	<b>\$ —</b>
<b>Derivatives not designated as hedging instruments:</b>						
<b>Financial institution counterparty:</b>						
Interest rate swaps	\$ 296,322	\$ —	\$ 14,259	\$ 222,394	\$ 105	\$ 4,736
Interest rate caps and collars	73,094	2	—	90,093	11	—
<b>Commercial customer counterparty:</b>						
Interest rate swaps	296,322	13,396	—	222,394	4,393	84
Interest rate caps and collars	73,094	—	2	90,093	—	11
<b>Total derivatives not designated as hedging instruments</b>	<b>738,832</b>	<b>13,398</b>	<b>14,261</b>	<b>\$ 624,974</b>	<b>4,509</b>	<b>4,831</b>
<b>Offsetting derivative assets/liabilities</b>		<b>2</b>	<b>2</b>		<b>(2,895)</b>	<b>(2,895)</b>
<b>Total Derivatives</b>	<b>\$ 1,488,832</b>	<b>\$ 20,021</b>	<b>\$ 17,636</b>	<b>\$ 899,974</b>	<b>\$ 4,967</b>	<b>\$ 1,936</b>

Pre-tax gain (loss) included in the condensed consolidated statements of income and related to derivative instruments for the three and nine months ended September 30, 2020 and 2019 were as follows.

	For the Three Months Ended September 30, 2020			For the Three Months Ended September 30, 2019		
	Net gain (loss) recognized in other comprehensive income on derivative	Gain (loss) reclassified from accumulated other comprehensive income into income	Location of gain (loss) reclassified from accumulated other comprehensive income into income	Net gain recognized in other comprehensive income on derivative	Gain (loss) reclassified from accumulated other comprehensive income into income	Location of gain (loss) reclassified from accumulated other comprehensive income into income
Derivatives designated as hedging instruments (cash flow hedges):						
Interest rate swap on borrowing advances	\$ 4,096	\$ —	Interest Expense	\$ 413	\$ (334)	Interest Expense
Interest rate swap on money market deposit account payments	562	(194)	Interest Expense	—	—	Interest Income
Commercial loan interest rate floor	(553)	553	Interest Income	—	—	Interest Income
<b>Total</b>	<b>\$ 4,105</b>	<b>\$ 359</b>		<b>\$ 413</b>	<b>\$ (334)</b>	
			Gain recognized in other noninterest income			Loss recognized in other noninterest income
Derivatives not designated as hedging instruments:						
Interest rate swaps, caps and collars			\$ 1,651			\$ 604

	For the Nine Months Ended September 30, 2020			For the Nine Months Ended September 30, 2019		
	Net gain (loss) recognized in other comprehensive income on derivative	Gain (loss) reclassified from accumulated other comprehensive income into income	Location of gain (loss) reclassified from accumulated other comprehensive income into income	Net gain recognized in other comprehensive income on derivative	Loss reclassified from accumulated other comprehensive income into income	Location of gain or (loss) reclassified from accumulated other comprehensive income into income
Derivatives designated as hedging instruments (cash flow hedges):						
Interest rate swap on borrowing advances	\$ 6,621	\$ —	Interest Expense	\$ 2,033	\$ (473)	Interest Expense
Interest rate swap on money market deposit account payments	(3,373)	(409)	Interest Expense	—	—	Interest Expense
Commercial loan interest rate floor	(78)	1,384	Interest Income	—	—	Interest Income
<b>Total</b>	<b>\$ 3,170</b>	<b>\$ 975</b>		<b>\$ 2,033</b>	<b>\$ (473)</b>	

	Gain recognized in other noninterest income	Gain recognized in other noninterest income
Derivatives not designated as hedging instruments:		
Interest rate swaps, caps and collars	\$ 575	\$ 474

### Cash Flow Hedges

Cash flow hedge relationships mitigate exposure to the variability of future cash flows or other forecasted transactions. The Company uses interest rate swaps, floors, caps and collars to manage overall cash flow changes related to interest rate risk exposure on benchmark interest rate loans.

In March 2020, the Company entered into an interest rate swap for a notional amount of \$500,000 to hedge the variability of cash flow payments attributable to changes in interest rates in regards to forecasted issuances of three-month term debt arrangements every three months from March 2022 through March 2032. These forecasted borrowings can be sourced from an FHLB advance, repurchase agreement, brokered certificate of deposit or some combination.

In March 2020, the Company entered into an interest rate swap for a notional amount of \$250,000 to hedge the variability of cash flow payments attributable to changes in interest rates in regards to forecasted money market account borrowings from March 2020 through March 2025.

In May 2019, the Company entered into a \$275,000 notional interest rate floor for commercial loans with a two-year term. The interest rate floor had a purchased floor strike of 2.43%. In February 2020, the Company terminated this interest rate floor. The gain resulting from the termination of the interest rate floor will remain in other comprehensive income (loss) and will be accreted into earnings over the remaining period of the former hedging relationship unless the forecasted transaction becomes probable of not occurring.



### Interest Rate Swap, Floor, Cap and Collar Agreements Not Designated as Hedging Derivatives

In order to accommodate the borrowing needs of certain commercial customers, the Company has entered into interest rate swap or cap agreements with those customers. These interest rate derivative contracts effectively allow the Company's customers to convert a variable rate loan into a fixed rate loan. In order to offset the exposure and manage interest rate risk, at the time an agreement was entered into with a customer, the Company entered into an interest rate swap or cap with a correspondent bank counterparty with offsetting terms. These derivative instruments are not designated as accounting hedges and changes in the net fair value are recognized in noninterest income or expense. Because the Company acts as an intermediary for its customers, changes in the fair value of the underlying derivative contracts substantially offset each other and do not have a material impact on the Company's results of operations. The fair value amounts are included in other assets and other liabilities.

The following is a summary of the interest rate swaps, caps and collars outstanding as of September 30, 2020 and December 31, 2019.

	September 30, 2020				
	Notional Amount	Fixed Rate	Floating Rate	Maturity	Fair Value
Non-hedging derivative instruments:					
Customer interest rate derivatives:					
Interest rate swaps - receive fixed/pay floating	\$ 296,322	3.140 - 8.470%	LIBOR 1 month + — % - 5.00% PRIME H15 - 0.250%	Wtd. Avg. 3.8 years	\$ (14,259)
Interest rate caps and collars	\$ 73,094	2.500% / 3.100%	LIBOR 1 month + — %	Wtd. Avg. 1.2 years	\$ 2
Correspondent interest rate derivatives:					
Interest rate swaps - pay fixed/receive floating	\$ 296,322	3.140 - 8.470%	LIBOR 1 month + — % - 5.00% PRIME H15 - 0.250%	Wtd. Avg. 3.8 years	\$ 13,396
Interest rate caps and collars	\$ 73,094	3.000% / 5.000%	LIBOR 1 month + — % - 2.50%	Wtd. Avg. 1.2 years	\$ (2)
	December 31, 2019				
	Notional Amount	Fixed Rate	Floating Rate	Maturity	Fair Value
Non-hedging derivative instruments:					
Customer interest rate derivatives:					
Interest rate swaps - receive fixed/pay floating	\$ 222,394	2.944 - 8.470%	LIBOR 1 month + — % - 5.00% PRIME H15 - 0.250%	Wtd. Avg. 3.3 years	\$ (4,632)
Interest rate caps and collars	\$ 90,093	2.430% / 5.800%	LIBOR 1 month + — % - 3.75%	Wtd. Avg. 1.5 years	\$ 11
Correspondent interest rate derivatives:					
Interest rate swaps - pay fixed/receive floating	\$ 222,394	2.944 - 8.470%	LIBOR 1 month + — % - 5.00% PRIME H15 - 0.250%	Wtd. Avg. 3.3 years	\$ 4,309
Interest rate caps and collars	\$ 90,093	3.000% / 5.800%	LIBOR 1 month + — % - 3.75%	Wtd. Avg. 1.5 years	\$ (11)

## 8. Off-Balance Sheet Loan Commitments

The Company is a 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. Those instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the condensed consolidated balance sheets.

The Company's exposure to credit loss in the event of nonperformance by the other party to a financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

The following table sets forth the approximate amounts of these financial instruments as of September 30, 2020 and December 31, 2019:

	September 30, 2020	December 31, 2019
Commitments to extend credit	\$ 2,127,728	\$ 1,744,989
Mortgage warehouse commitments	280,444	205,361
Standby and commercial letters of credit	43,363	27,196
Total	<u>\$ 2,451,535</u>	<u>\$ 1,977,546</u>

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments may expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Management evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the borrower.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Standby letters of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Company's policy for obtaining collateral and the nature of such collateral is substantially the same as that involved in making commitments to extend credit.

Mortgage warehouse commitments are unconditionally cancellable and represent the unused capacity on mortgage warehouse facilities the Company has approved. The Company reserves the right to refuse to buy any mortgage loans offered for sale by a customer, for any reason, at the Company's sole and absolute discretion.

The table below presents the activity in the allowance for unfunded commitment credit losses related to those financial instruments discussed above. This allowance is recorded in accounts payable and other liabilities on the condensed consolidated balance sheets:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2020	2019	2020	2019
Beginning balance for allowance for unfunded commitments	\$ 8,398	\$ 878	\$ 878	\$ 878
Impact of CECL adoption	—	—	840	—
Provision for unfunded commitments	1,447	—	8,127	—
Ending balance of allowance for unfunded commitments	<u>\$ 9,845</u>	<u>\$ 878</u>	<u>\$ 9,845</u>	<u>\$ 878</u>

## 9. Stock-Based Awards

### Veritex 2010 Stock Option and Equity Incentive Plan (“2010 Incentive Plan”)

The Company recognized no stock compensation expense related to the 2010 Incentive Plan for the three and nine months ended September 30, 2020. The Company recognized no stock compensation expense related to the 2010 Incentive Plan during the three months ended September 30, 2019 and stock compensation of \$2 for the nine months ended September 30, 2019.

A summary of option activity under the 2010 Incentive Plan for the nine months ended September 30, 2020 and 2019, and changes during the periods then ended, is presented below:

	2010 Incentive Plan			
	Non-Performance Based Stock Options			
	Shares Underlying Options	Weighted Exercise Price	Weighted Average Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2019	275,000	\$ 10.12	2.39 years	
Exercised	(17,500)	10.24		
Outstanding and exercisable at September 30, 2019	257,500	\$ 10.28	1.62 years	
Outstanding at January 1, 2020	257,500	\$ 10.28	1.37 years	\$ 4,971
Exercised	(207,500)	10.14		
Outstanding and exercisable at September 30, 2020	50,000	\$ 10.84	1.91 years	\$ 377

As of September 30, 2020, December 31, 2019 and September 30, 2019 there was no unrecognized stock compensation expense related to non-performance based stock options.

A summary of the fair value of the Company’s stock options exercised under the 2010 Incentive Plan for the nine months ended September 30, 2020 and 2019 is presented below:

	Fair Value of Options Exercised as of September 30,	
	2020	2019
Non-performance based stock options exercised	5,851	454

### 2019 Amended Plan and Green Acquired Omnibus Plans

#### *2020 Grants of Restricted Stock Units*

During the nine months ending September 30, 2020, the Company granted non-performance-based and performance-based restricted stock units (“RSUs”) under the 2019 Amended and Restated Omnibus Incentive Plan, which amended and restated the 2014 Omnibus Incentive Plan (“2019 Amended Plan”), and the Veritex (Green) 2014 Omnibus Equity Incentive Plan (“Veritex (Green) 2014 Plan”). The majority of the non-performance-based RSUs granted to employees during the nine months ending September 30, 2020 cliff vest after three to five years from the grant date. There were also non-performance-based RSUs granted to the Company’s directors that vest in four equal quarterly installments from the grant date.

The performance-based RSUs granted in January 2020 are subject to “cliff” vesting, with a vesting date of January 1, 2023, based on a performance period starting on December 31, 2019 and ending on December 31, 2022. The vesting percentage is determined based on the Company’s total shareholder return (“TSR”) relative to the TSR of 15 peer companies (“Peer Group”) over the performance period. Below is a table showing the range of vesting percentages for the performance-based RSUs based on the Company’s TSR percentile rank.

	<b>Vesting %</b>
Below the 24.9 <sup>th</sup> percentile of Peer Group TSR	—%
Within the 25 <sup>th</sup> to 49.9 <sup>th</sup> percentile of Peer Group TSR	50%
Within the 50 <sup>th</sup> the 74.9 <sup>th</sup> percentile of Peer Group TSR	100%
At or above the 75 <sup>th</sup> percentile of Peer Group TSR	150%

A Monte Carlo simulation was used to estimate the fair value of performance-based RSUs on the grant date that include a market condition based on the Company's TSR relative to its Peer Group, which determines the eligible number of RSUs to vest.

#### *2020 Grant of Stock Options*

In January 2020, the Company granted non-performance-based options under the 2019 Amended Plan and the Veritex (Green) 2014 Plan, which vest over three years in equal installments on each anniversary of the grant date.

The fair value of each option award is estimated on the grant date using the Black-Scholes option-pricing model with the following assumptions used for the grants for the nine months ended September 30, 2020:

	<b>Nine Months Ended September 30, 2020</b>
Expected life	5 to 6.51 years
Expected volatility	27.49% to 38.88%
Dividend yield	2.33% to 5.14%
Risk-free interest rate	0.36% to 1.76%

The expected life is based on the amount of time that options being valued are expected to remain outstanding. The expected volatility is based on historical volatility of the Company. The dividend yield assumption is based on the Company's dividend history. The risk-free interest rates are based upon yields of U.S. Treasury issues with a term equal to the expected life of the option being valued.

#### *Stock Compensation Expense and Liability Award Compensation Expense*

Stock compensation expense for equity awards under the 2019 Amended Plan was approximately \$1,588 and \$4,468 for the three and nine months ended September 30, 2020, respectively. For the three and nine months ended September 30, 2019, the Company recognized \$1,054 and \$1,691 in stock compensation expense, respectively.

Stock compensation expense for options and RSUs granted under the Veritex (Green) 2014 Plan was approximately \$490 and \$1,413 for the three and nine months ended September 30, 2020, respectively. Stock compensation expense for options and RSUs granted under the Veritex (Green) 2014 Plan was approximately \$376 and \$1,147 for the three and nine months ended September 30, 2019, respectively.

There was no compensation expense for liability-classified awards under the 2019 Amended Plan during the three and nine months ended September 30, 2020. There was no compensation expense for liability-classified awards for the three months ended September 30, 2019 and \$1,403 for the nine months ended September 30, 2019.

2019 Amended Plan

A summary of the status of the Company's stock options under the 2019 Amended Plan as of September 30, 2020 and 2019, and changes during the nine months then ended, is as follows:

	2019 Amended Plan							
	Non-performance Based Stock Options							
	Equity Awards				Liability Awards			
	Shares Underlying Options	Weighted Exercise Price	Weighted Average Contractual Term	Aggregate Intrinsic Value	Shares Underlying Options	Weighted Exercise Price	Weighted Average Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2019	449,520	\$ 24.47	8.24 years		—	\$ —		
Granted	166,971	23.91			253,633	21.38		
Conversion to equity awards	253,633	21.38			(253,633)	21.38		
Forfeited	(28,240)	25.82			—	—		
Exercised	(12,610)	15.42			—	—		
Outstanding at September 30, 2019	829,274	\$ 23.50	8.42 years		—	\$ —		—
Options exercisable at September 30, 2019	417,183	\$ 24.59	7.53 years		—	\$ —		
Outstanding at January 1, 2020	849,768	\$ 23.61	8.24 years	\$ 4,687	—	\$ —		
Granted	170,025	27.31			—	—		
Forfeited	(23,735)	27.70			—	—		
Exercised	(33,439)	19.19			—	—		
Outstanding at September 30, 2020	962,619	\$ 24.32	7.77 years	\$ (7,018)	—	\$ —		\$ —
Options exercisable at September 30, 2020	492,204	\$ 24.23	6.94 years	\$ (5,147)	—	\$ —		
Weighted average fair value of options granted during the period		\$ 27.31				\$ —		

As of September 30, 2020, December 31, 2019 and September 30, 2019, there was \$2,801, \$2,948 and \$1,296 of total unrecognized compensation expense related to equity options awarded under the 2019 Amended Plan, respectively. As of September 30, 2020, there was no unrecognized compensation expense related to liability options awarded under the 2019 Amended Plan. The unrecognized compensation expense at September 30, 2020 is expected to be recognized over the remaining weighted average requisite service period of 1.88 years.

A summary of the status of the Company's non-performance-based RSUs under the 2019 Amended Plan as of September 30, 2020 and 2019, and changes during the nine months then ended, is as follows:

	2019 Amended Plan			
	Non-performance-Based RSUs			
	Equity Awards		Liability Awards	
	Units	Weighted Average Grant Date Fair Value	Units	Weighted Average Grant Date Fair Value
Outstanding at January 1, 2019	133,455	\$ 19.67	—	\$ —
Granted	104,827	23.09	165,739	21.38
Conversion to equity awards	165,739	21.38	(165,739)	21.38
Vested into shares	(229,031)	22.06		
Outstanding at September 30, 2019	174,990	\$ 21.55	—	\$ —
Outstanding at January 1, 2020	175,688	\$ 21.65	—	\$ —
Granted	436,818	26.92	—	—
Vested into shares	(82,683)	23.24	—	—
Forfeited	(470)	29.13	—	—
Outstanding at September 30, 2020	529,353	\$ 25.16	—	\$ —

A summary of the status of the Company's performance-based RSUs under the 2019 Amended Plan as of September 30, 2020 and 2019, and changes during the nine months then ended, is as follows:

	2019 Amended Plan			
	Performance-Based RSUs			
	Equity Awards		Liability Awards	
	Units	Weighted Average Grant Date Fair Value	Units	Weighted Average Grant Date Fair Value
Outstanding at January 1, 2019	63,988	\$ 21.28	—	\$ —
Granted	38,360	22.47	32,249	21.38
Conversion to equity awards	32,249	21.38	(32,249)	21.38
Vested into shares	(51,284)	25.31	—	—
Forfeited	(17,827)	21.38	—	—
Outstanding at September 30, 2019	65,486	\$ 22.73	—	\$ —
Outstanding at January 1, 2020	63,727	\$ 22.76	—	\$ —
Granted	39,398	29.13	—	—
Vested into shares	(1,841)	26.65	—	—
Outstanding at September 30, 2020	101,284	\$ 25.22	—	\$ —

As of September 30, 2020, December 31, 2019 and September 30, 2019 there was \$9,098, \$4,329 and \$2,484 of total unrecognized compensation related to equity RSUs awarded under the 2019 Amended Plan, respectively. As of September 30, 2020, there was no of unrecognized compensation related to liability RSUs awarded under the 2019 Amended Plan. The unrecognized compensation expense at September 30, 2020 is expected to be recognized over the remaining weighted average requisite service period of 2.9 years.

A summary of the fair value of the Company's stock options exercised and RSUs vested under the 2019 Amended Plan during the nine months ended September 30, 2020 and 2019 is presented below:

	Fair Value of Options Exercised or RSUs Vested in the Nine Months Ended September 30,	
	2020	2019
Non-performance-based stock options exercised	943	335
Non-performance-based RSUs vested	2,225	5,669
Performance-based RSUs vested	36	1,089

#### Veritex (Green) 2014 Plan

A summary of the status of the Company's stock options under the Veritex (Green) 2014 Plan as of September 30, 2020 and 2019, and changes during the nine months then ended, is as follows:

	Veritex (Green) 2014 Plan			
	Non-performance Based Stock Options			
	Shares Underlying Options	Weighted Exercise Price	Weighted Average Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2019	—	\$ —		
Converted in acquisition of Green	304,778	15.41		
Granted	211,793	21.38		
Forfeited	(10,217)	12.21		
Exercised	(82,451)	12.43		
Outstanding at September 30, 2019	423,903	\$ 18.85	8.01 years	
Options exercisable at September 30, 2019	213,427	\$ 16.36	6.89 years	
Outstanding at January 1, 2020	386,969	\$ 19.30	7.86 years	\$ 3,800
Granted	31,075	29.13		
Forfeited	(28,736)	21.38		
Exercised	(34,476)	19.54		
Outstanding at September 30, 2020	354,832	\$ 19.95	7.34 years	\$ (1,039)
Options exercisable at September 30, 2020	212,676	\$ 17.84	6.46 years	\$ (546)
Weighted average fair value of options granted during the period		\$ 29.13		

As of September 30, 2020, December 31, 2019 and September 30, 2019, there was \$759, \$1,062, and \$1,198 of total unrecognized compensation expense related to options awarded under the Veritex (Green) 2014 Plan, respectively. The unrecognized compensation expense at September 30, 2020 is expected to be recognized over the remaining weighted average requisite service period of 1.4 years.

A summary of the status of the Company's non-performance-based RSUs under the Veritex (Green) 2014 Plan as of September 30, 2020 and 2019 and changes during the nine months then ended, is as follows:

	Veritex (Green) 2014 Plan Non-performance-Based RSUs	
	Units	Weighted Average Grant Date Fair Value
Outstanding at January 1, 2019	—	\$ —
Granted	116,250	21.38
Outstanding at September 30, 2019	116,250	\$ 21.38
Outstanding at January 1, 2020	116,250	\$ 21.38
Granted	93,918	21.36
Vested into shares	(38,744)	29.13
Forfeited	(4,402)	29.13
Outstanding at September 30, 2020	167,022	\$ 22.69

A summary of the status of the Company's performance-based RSUs under the Veritex (Green) 2014 Plan as of September 30, 2020 and 2019 and changes during the nine months then ended, is as follows:

	Veritex (Green) 2014 Plan Performance-Based RSUs	
	Units	Weighted Average Grant Date Fair Value
Outstanding at January 1, 2019	—	\$ —
Granted	26,145	\$ 21.38
Forfeited	(508)	\$ 21.38
Outstanding at September 30, 2019	25,637	\$ 21.38
Outstanding at January 1, 2020	25,320	\$ 21.38
Granted	8,531	29.13
Outstanding at September 30, 2020	33,851	\$ 23.33

As of September 30, 2020, December 31, 2019 and September 30, 2019, there was \$2,842, \$1,991, and \$2,243, respectively, of total unrecognized compensation related to outstanding performance-based RSUs awarded under the Veritex (Green) 2014 Plan to be recognized over a remaining weighted average requisite service period of 2.3 years.



A summary of the fair value of the Company's stock options exercised and RSUs vested under the Veritex (Green) 2014 Plan during the nine months ended September 30, 2020 and 2019 presented below:

	Fair Value of Options Exercised or RSUs Vested in the Nine Months Ended September 30,	
	2020	2019
Non-performance-based stock options exercised	\$ 1,001	\$ 2,088
Non-performance-based RSUs vested	828	—

*Green Bancorp Inc. 2010 Stock Option Plan and Green Bancorp Inc. 2006 Stock Option Plan*

In addition to the Veritex (Green) 2014 Plan discussed earlier in this Note, the Company assumed two stock and incentive plans in the Green acquisition, the Green Bancorp Inc. 2010 Stock Option Plan ("Green 2010 Plan") and the Green Bancorp Inc. 2006 Stock Option Plan ("Green 2006 Plan"). For the Green 2010 Plan and the Green 2006 Plan, 768,628 and 11,850 of stock options, respectively, were converted in the acquisition of Green during the nine months ended September 30, 2019. No stock options or restricted stock units were awarded from these plans during the nine months ended September 30, 2020 or 2019. During the nine months ended September 30, 2020, 440,652 stock options granted under the Green 2010 Plan were exercised and no stock options granted under the Green 2006 Plan were exercised. As of September 30, 2020, 126,284 exercisable stock options remain outstanding in the Green 2010 Plan and no exercisable stock options remain outstanding in the Green 2006 Plan.

## 10. Income Taxes

Income tax expense for the three and nine months ended September 30, 2020 and 2019 was as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2020	2019	2020	2019
Income tax expense for the period	\$ 6,198	\$ 7,595	\$ 9,501	\$ 16,953
Effective tax rate	21.3 %	21.7 %	15.7 %	21.6 %

For the three and nine months ended September 30, 2020, the Company had an effective tax rate of 21.3% and 15.7%. The decrease in the effective tax rate during the nine months ended September 30, 2020 was primarily due to a net discrete tax benefit of \$1,799 as a result of the Company amending a prior year Green Bancorp, Inc. ("Green") tax return to carry back a net operating loss ("NOL") incurred by Green on January 1, 2019. The Company was allowed to carry back this NOL as result of a provision in the Coronavirus Aid, Relief, and Economic Security Act (the "CARES" Act) which permits NOLs generated in tax years 2018, 2019 or 2020 to be carried back five years. In addition to this, the Company recognized a net discrete tax expense of \$32 and a net discrete tax benefit of \$1,391 primarily associated with the recognition of excess tax expense/benefit realized on share-based payment awards during the three and nine months ended September 30, 2020, respectively. Excluding these discrete tax items, the Company had an effective tax rate of 21.2% and 21.0% for the three and nine months ended September 30, 2020.

## 11. Legal Contingencies

### Litigation

The Company may from time to time be involved in legal actions arising from normal business activities. In the opinion of management, there are no claims for which it is reasonably possible that an adverse outcome would have a material effect on the Company's financial position, liquidity or results of operations. The Company is not aware of any material unasserted claims.

## 12. Capital Requirements and Restrictions on Retained Earnings

The Company, on a consolidated basis, and the Bank are subject to various regulatory capital requirements administered by federal banking agencies. Failure to meet minimum capital requirements can lead to the initiation of certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company must meet specific capital guidelines that involve quantitative measures of the Company's assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The Company's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

In the first quarter of 2020, U.S. federal regulatory authorities issued an interim final rule that provides banking organizations that adopt CECL during the 2020 calendar year with the option to delay for two years the estimated impact of CECL on regulatory capital relative to regulatory capital determined under the prior incurred loss methodology, followed by a three-year transition period to phase out the aggregate amount of the capital benefit provided during the initial two-year delay (i.e., a five-year transition in total). In connection with our adoption of CECL on January 1, 2020, we have elected to utilize the five-year CECL transition.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios (set forth in the table below) of total, CET1 and Tier 1 capital (as defined in the regulations) to risk weighted assets (as defined), and of Tier 1 capital (as defined) to average assets (as defined). Management believes, as of September 30, 2020 and December 31, 2019, that the Company and the Bank met all capital adequacy requirements to which they were subject.

As of September 30, 2020 and December 31, 2019, the Company's and the Bank's capital ratios exceeded those levels necessary to be categorized as "well capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well capitalized," the Company and the Bank must maintain minimum total risk-based, CET1, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the table below. There are no conditions or events since September 30, 2020 that management believes have changed the Company's categorization as "well capitalized."

A comparison of the Company's and Bank's actual capital amounts and ratios to required capital amounts and ratios is presented in the following table:

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of September 30, 2020						
Total capital (to risk-weighted assets)						
Company	\$ 980,761	12.70 %	\$ 617,802	8.0 %	n/a	n/a
Bank	954,317	12.37 %	617,182	8.0 %	\$ 771,477	10.0 %
Tier 1 capital (to risk-weighted assets)						
Company	776,108	10.05 %	463,348	6.0 %	n/a	n/a
Bank	859,634	11.14 %	462,999	6.0 %	617,331	8.0 %
Common equity tier 1 to risk-weighted assets						
Company	746,937	9.67 %	347,592	4.5 %	n/a	n/a
Bank	859,634	11.14 %	347,249	4.5 %	501,582	6.5 %
Tier 1 capital (to average assets)						
Company	776,108	9.54 %	325,412	4.0 %	n/a	n/a
Bank	859,634	10.57 %	325,311	4.0 %	406,639	5.0 %
As of December 31, 2019						
Total capital (to risk-weighted assets)						
Company	\$ 917,939	13.10 %	\$ 560,573	8.0 %	n/a	n/a
Bank	870,838	12.44 %	560,024	8.0 %	\$ 700,031	10.0 %
Tier 1 capital (to risk-weighted assets)						
Company	771,679	11.02 %	420,152	6.0 %	n/a	n/a
Bank	840,126	12.00 %	420,063	6.0 %	560,084	8.0 %
Common equity tier 1 to risk-weighted assets						
Company	742,675	10.60 %	315,287	4.5 %	n/a	n/a
Bank	840,126	12.00 %	315,047	4.5 %	455,068	6.5 %
Tier 1 capital (to average assets)						
Company	771,679	10.17 %	303,512	4.0 %	n/a	n/a
Bank	840,126	11.07 %	303,569	4.0 %	379,461	5.0 %

**Dividend Restrictions** — Dividends paid by the Bank are subject to certain restrictions imposed by regulatory agencies. The Basel III Capital Rules further limit the amount of dividends that may be paid by the Bank. There are no dividend payment limitations by the Bank if the Bank's capital conservation buffer is greater than 2.5%. The Bank had a capital conservation buffer of 4.37% as of September 30, 2020. Dividends of \$20,000 and \$65,000 were paid by the Bank to the Holdco during the three and nine months ended September 30, 2020, respectively. Dividends of \$37,000 and \$56,750 were paid by the Bank to the Holdco during the three and nine months ended September 30, 2019, respectively.

Dividends of \$8,558, or \$0.17, and \$25,849, or \$0.51, were paid by the Company during the three and nine months ended September 30, 2020, respectively. Dividends of \$6,713, or \$0.125, and \$20,312, or \$0.38, were paid by the the Company during the three and nine months ended September 30, 2019, respectively.

### 13. Subsequent Events

On October 27, 2020, the Company announced that its Board of Directors declared a regular cash dividend of \$0.17 per share on its outstanding common stock, payable on or after November 19, 2020 to shareholders of record as of November 5, 2020.

Also on October 27, 2020, the Company announced that its Board of Directors authorized an extension of the Stock Buyback Program from December 31, 2020 to March 31, 2021.

On October 5, 2020, the Company completed the issuance and sale of \$125,000 in aggregate principal amount of its 4.125% Fixed-to-Floating Rate Subordinated Debt due in 2030 (the "Subordinated Notes"). The Subordinated Notes will bear interest: (i) from and including the date of issuance to, but excluding, October 15, 2025, at a rate of 4.125% per year and (ii) from and including October 15, 2025 to, but excluding, the maturity date (unless redeemed prior to such date), at a floating rate per year equal to the Benchmark (which is expected to be Three-Month Term Secured Overnight Funding Rate) plus 399.5 basis points. The Company has the right, subject to certain circumstances and the receipt of any required approval of the Federal Reserve Board, to redeem the Subordinated Notes at the Company's option, in whole or in part, on any interest payment date on or after October 15, 2025. The Company intends to use the net proceeds from the offering of Subordinated Notes for general corporate purposes, including the potential repayment of outstanding indebtedness, and supporting capital levels of the Bank.

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

*The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and notes thereto appearing in Item 1 of Part I of this Quarterly Report on Form 10-Q (this “Report”) as well as with our consolidated financial statements and notes thereto appearing in our Annual Report on Form 10-K for the year ended December 31, 2019. Except where the content otherwise requires or when otherwise indicated, the terms “Veritex”, “Company,” “we,” “us,” “our,” and “our business” refer to the combined entities of Veritex Holdings, Inc. and its subsidiaries, including Veritex Community Bank.*

*This discussion and analysis contains forward-looking statements that are subject to certain risks and uncertainties and are based on certain assumptions that we believe are reasonable but may prove to be inaccurate. Certain risks, uncertainties and other factors, including those set forth under “Special Cautionary Notice Regarding Forward-Looking Statements,” may cause actual results to differ materially from the projected results discussed in the forward-looking statements appearing in this discussion and analysis. We assume no obligation to update any of these forward-looking statements. For additional information concerning forward-looking statements, please read “Special Cautionary Notice Regarding Forward-Looking Statements” below.*

### Overview

Veritex is a Texas corporation and bank holding company headquartered in Dallas, Texas. Through our wholly owned subsidiary, Veritex Community Bank (the “Bank”), a Texas state chartered bank, we provide relationship-driven commercial banking products and services tailored to meet the needs of small to medium-sized businesses and professionals. Beginning at our operational inception in 2010, we initially targeted customers and focused our acquisitions primarily in the Dallas metropolitan area, which we consider to be Dallas and the adjacent communities in North Dallas. Our current primary market now includes the broader Dallas-Fort Worth metroplex and the Houston metropolitan area. As we continue to grow, we may expand to other metropolitan banking markets in Texas.

Our business is conducted through one reportable segment, community banking, where we generate the majority of our revenues from interest income on loans, customer service and loan fees, gains on sale of Small Business Administration (“SBA”) guaranteed loans and mortgage loans and interest income from securities. We incur interest expense on deposits and other borrowed funds and noninterest expense, such as salaries and employee benefits and occupancy expenses. We analyze our ability to maximize income generated from interest earning assets and expense of our liabilities through net interest margin. Net interest margin is a ratio calculated as net interest income divided by average interest-earning assets. Net interest income is the difference between interest income on interest-earning assets, such as loans and securities, and interest expense on interest-bearing liabilities, such as deposits and borrowings, which are used to fund those assets.

Changes in the market interest rates and interest rates we earn on interest-earning assets or pay on interest-bearing liabilities, as well as the volume and types of interest-earning assets, and interest-bearing and noninterest-bearing liabilities, are usually the largest drivers of periodic changes in net interest spread, net interest margin and net interest income. Fluctuations in market interest rates are driven by many factors, including governmental monetary policies, inflation, deflation, macroeconomic developments, changes in unemployment, the money supply, political and international conditions and conditions in domestic and foreign financial markets. Periodic changes in the volume and types of loans in our loan portfolio are affected by, among other factors, economic and competitive conditions in Texas and, specifically, in the Dallas-Fort Worth metroplex and Houston metropolitan area, as well as developments affecting the real estate, technology, financial services, insurance, transportation, manufacturing and energy sectors within our target market and throughout the state of Texas.

## Recent Developments

### Impact of COVID-19

The novel coronavirus (“COVID-19”) pandemic has created a global public health crisis that has resulted in unprecedented uncertainty, volatility and disruption in financial markets and in governmental, commercial and consumer activity in the United States and globally, including the markets that we serve. Governmental responses to the pandemic have included orders closing businesses not deemed essential and directing individuals to observe social distancing and shelter in place. These actions, together with responses to the pandemic by businesses and individuals, have resulted in rapid decreases in commercial and consumer activity, temporary closures of many businesses that have led to a loss of revenues and a rapid increase in unemployment, material decreases in business valuations, disrupted global supply chains, market downturns and volatility, changes in consumer behavior related to pandemic fears, related emergency response legislation and an expectation that the policy of the Board of Governors of the Federal Reserve (the “Federal Reserve”) will maintain a low interest rate environment for the foreseeable future.

We have taken deliberate actions to ensure that we have the balance sheet strength to serve our clients and communities during the COVID-19 pandemic, including increasing our liquidity and reserves supported by a strong capital position. Our commercial and consumer customers are experiencing varying degrees of financial distress due to the pandemic and related governmental actions taken in response to the pandemic. In order to protect the health of our customers and employees, and to comply with applicable governmental directives, we have implemented our operational response and preparedness plan, which includes dispersion of critical operation processes, increased monitoring focused on higher risk operations, enhanced remote access security and further restricted internet access, enhanced security around wire transfer execution and flexible scheduling provided to employees who are unable to work from home.

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security (“CARES”) Act was enacted. The CARES Act contains substantial tax and spending provisions intended to address the impact of the COVID-19 pandemic, including the SBA Paycheck Protection Program (“PPP”), a nearly \$350 billion program designed to aid small- and medium-sized businesses through federally guaranteed, forgivable loans distributed through banks. These loans are intended to guarantee eight weeks of payroll and other costs to help those businesses remain viable and allow their workers to pay their bills. We partnered with a web-based commercial and SBA lending software platform that manages the origination, processing, closing and monitoring of SBA loans and have provided our customers the ability to apply and qualify for PPP loans through this platform. On April 16, 2020, the SBA announced that all available funds had been exhausted and applications were no longer being accepted. On April 24, 2020, the President signed into law the Paycheck Protection Program and Health Care Enhancement Act (“PPHCE Act”), which provided an additional \$310 billion for the PPP and supplements certain other programs. The Company believes that the majority of these loans will ultimately be forgiven by the SBA in accordance with the terms of the program. The deadline for loan applications was August 8, 2020. If a loan is fully forgiven, SBA will repay the lending bank in full. If a loan is partially forgiven or not forgiven at all, a bank must look to the borrower for repayment of unforgiven principal and interest. If the borrower defaults, the loan is guaranteed by SBA. In order to obtain loan forgiveness, a PPP borrower must submit a forgiveness application to us, which we must review and forward to the SBA. The SBA began approving forgiveness applications on October 2, 2020. As of September 30, 2020, we had funded approvals for approximately 2,199 clients totaling approximately \$405.5 million in PPP loans carried at fair value.

In response to the COVID-19 pandemic, we have also implemented a loan deferment program to provide temporary payment relief to certain of our borrowers who meet the program's qualifications. This program allows for a deferral of principal and/or interest payments for 90 days (“Round 1 Deferments”), which we may extend for an additional 90 days (“Round 2 Deferments”), for a maximum of 180 days on a cumulative basis. The deferred payments along with interest accrued during the deferral period are due and payable on the maturity date of the existing loan. For the nine months ended September 30, 2020, the Company had 741 modifications of loans with aggregate principal balances \$1.2 billion that qualified for temporary suspension of troubled debt restructuring requirements under Section 4013 of the CARES Act. As of October 22, 2020, we had \$155.5 million in loans with remaining deferments.

Significant uncertainties as to future economic conditions exist, and we have taken deliberate actions in response to these uncertainties, including increased levels of on balance sheet liquidity and increased capital ratio levels. Additionally, the economic pressures, coupled with our implementation in January 2020 of the current expected credit loss (“CECL”) methodology for determining our provision for credit losses, have contributed to an increased provision for credit losses for the three and nine months ended September 30, 2020 compared to the same period in 2019. We continue to monitor the impact of COVID-19 closely, as well as any effects that may result from the CARES Act; however, the extent to which the COVID-19 pandemic will impact our operations and financial results during the remainder of 2020 is highly uncertain.

## *Financial position and results of operations*

COVID-19 had a material impact on our allowance for credit losses during 2020. While we have not yet experienced any charge-offs related to COVID-19, our allowance for credit losses calculation and resulting provision for credit losses were significantly impacted by the change in the Texas economic forecasts used in the CECL model throughout 2020 to reflect the expected impact of COVID-19. Given that forecasted economic scenarios have deteriorated significantly since the pandemic was declared in early March, our need for additional reserve for credit loss increased significantly. Refer to our further discussion of the allowance for credit losses below as well as in Note 1, “Summary of Significant Accounting Policies,” and Note 5, “Loans and Allowance for Credit Losses,” in the accompanying notes to the condensed consolidated financial statements. Should economic conditions worsen, we could experience further increases in our allowance for credit losses and record additional credit loss expense. We could also see an increase in our ratio of past due loans to total loans, although the execution of our loan deferment program might temporarily improve this ratio. It is possible that our asset quality measures could worsen at future measurement periods if the effects of COVID-19 are further prolonged.

Our fee income could be reduced due to COVID-19. In keeping with guidance from regulators, we are working with customers affected by COVID-19 to waive fees from a variety of sources, including, but not limited to, insufficient funds and overdraft fees, ATM fees and account maintenance fees. These reductions in fees are thought, at this time, to be temporary in conjunction with the length of the expected COVID-19 related economic crisis. At this time, we are unable to project the materiality of such an impact, but recognize the breadth of the economic impact is likely to impact our fee income in future periods.

Our interest income could also be reduced due to COVID-19. In keeping with guidance from regulators, we are actively working with borrowers affected by COVID-19 to defer their payments, interest, and fees. While interest and fees will still accrue to income, should eventual credit losses on these deferred payments emerge, our interest income and fees accrued would need to be reversed. In such a scenario, interest income in future periods could be negatively impacted. At this time, we are unable to project the materiality of such an impact, but recognize the breadth of the economic impact may affect our borrowers’ ability to repay in future periods.

## *Capital and liquidity*

As of September 30, 2020, all of our capital ratios, and the Bank’s capital ratios, were in excess of all regulatory requirements. While we believe that we have sufficient capital to withstand an extended economic recession brought about by COVID-19, our reported and regulatory capital ratios could be adversely impacted by further credit losses. We rely on cash on hand as well as dividends from the Bank to service our debt. If our capital deteriorates such that the Bank is unable to pay dividends to us for an extended period of time, we may not be able to service our debt.

We maintain access to multiple sources of liquidity. Wholesale funding markets have remained open to us, but rates for short term funding have recently been volatile. If funding costs are elevated for an extended period of time, it could have an adverse effect on our net interest margin. If an economic recession caused large numbers of our deposit customers to withdraw their funds, we might become more reliant on volatile or more expensive sources of funding.

## *Asset valuation*

Currently, we do not expect COVID-19 to affect our ability to account timely for the assets on our balance sheet; however, this could change in future periods. While certain valuation assumptions and judgments will change to account for pandemic-related circumstances such as widening credit spreads, we do not anticipate significant changes in methodology used to determine the fair value of assets measured in accordance with generally accepted accounting principles in the United States (“GAAP”).

During the second quarter of 2020, we observed a sustained decline in the market valuation of the Company's common shares as a result of continued economic disruption occurring after the first quarter of 2020 primarily due to the COVID-19 pandemic. As a result, the Company determined that it was more likely than not that the fair value of the Company's sole reporting unit was below its carrying value and proceeded to perform an interim quantitative impairment test. The Company determined the fair value of its reporting unit using a combination of a market and an income approach. The fair value of our reporting unit exceeded its related carrying value by approximately 26%. The effects of the COVID-19 pandemic could cause a further and sustained economic disruption. This could result in additional decline in our stock price or further impact to our business operations, which could result in the determination that another interim quantitative impairment assessment is necessary in a future period. In the event that we conclude that all or a portion of our goodwill is impaired, a non-cash charge for the amount of such impairment would be recorded to earnings. Such a charge would have no impact on tangible capital or regulatory capital. During the third quarter of 2020, the Company determined that there was no triggering event that required an interim quantitative impairment assessment to determine if it was more likely than not that the fair value of the Company's sole reporting unit was below its carrying value. As of September 30, 2020, we did not have any impairment with respect to our intangible assets, premises and equipment, equity investments or other long-lived assets. It is possible that the lingering effects of the COVID-19 pandemic could cause the occurrence of what management would deem to be a triggering event that could, under certain circumstances, cause us to perform an intangible asset impairment test and result in an impairment charge being recorded for that period. In the event that we conclude that all or a portion of our intangible assets are impaired, a non-cash charge for the amount of such impairment would be recorded to earnings. Such a charge would have no impact on tangible capital or regulatory capital. At September 30, 2020, we had intangible assets of \$64.7 million, representing approximately 5.5% of equity.

#### *Credit*

The following loan portfolios represent our material at-risk portfolios identified by management impacted by the COVID-19 pandemic as of September 30, 2020:

#### Hospitality Exposure

The Company's exposure to hospitality at September 30, 2020 was \$356.5 million, or 6.2% of total loans held for investment, excluding mortgage warehouse and PPP loans. 33% of the Company's hospitality borrowers are top tier hotels, 46% are national brands, 19% are luxury boutique hotels and 2% are no flag hotels. The weighted average loan to value for this portfolio was 60.0% at origination date.

#### Retail Commercial Real Estate ("CRE") Exposure

The Company's exposure to retail CRE at September 30, 2020 was \$455.7 million, or 7.9% of total loans held for investment, excluding mortgage warehouse and PPP loans. The weighted average loan to value for this portfolio was 58.0% at origination date.

#### Restaurant Exposure

The Company's exposure to restaurants at September 30, 2020 was \$122.8 million, or 2.1% of total loans held for investment, excluding mortgage warehouse and PPP loans. 63% of the Company's restaurant borrowers are quick service restaurants and 37% are full service restaurants. A total of 80% of the portfolio is secured by real estate assets with an average loan to value of 60.0% at origination date.

#### **Adoption of New Accounting Standard for Allowance for Credit Losses**

On January 1, 2020, the Company adopted Accounting Standards Update 2016-13, *Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments* ("ASU 2016-13"), which replaces the incurred loss methodology with an expected loss methodology that is referred to as CECL. The measurement of expected credit losses under the CECL methodology is applicable to financial assets measured at amortized cost, including loan receivables and held-to-maturity debt securities. It also applies to off-balance sheet ("OBS") credit exposures not accounted for as insurance (loan commitments, standby letters of credit, financial guarantees, and other similar instruments) and net investments in leases recognized by a lessor. In addition, ASU 2016-13 made changes to the accounting for available-for-sale debt securities. One such change is to require credit losses to be presented as an allowance rather than as a write-down on available-for-sale debt securities management does not intend to sell or believes that it is more likely than not they will be required to sell.



A summary of the impact of the adoption of ASU 2016-13 on our financial statements is as follows:

- Net decrease in retained earnings of \$15.5 million as of January 1, 2020 for the cumulative effect of adopting ASC 326.
- On January 1, 2020, the amortized cost basis of assets purchased with credit deterioration were adjusted to reflect the addition of \$19.7 million to the allowance for credit losses. The remaining noncredit discount (based on the adjusted amortized cost basis) will be accreted into interest income at the effective interest rate as of January 1, 2020.
- Increase in the allowance for credit losses of \$39.1 million as of January 1, 2020.
- Increase in our allowance for unfunded commitments of \$840 thousand as of January 1, 2020. The allowance for unfunded commitments is recorded in accounts payable and other liabilities in the condensed consolidated balance sheets.

## Results of Operations for the Nine Months Ended September 30, 2020 and 2019

### *General*

Net income for the nine months ended September 30, 2020 was \$51.1 million, a decrease of \$10.6 million, or 17.2%, from net income of \$61.7 million for the nine months ended September 30, 2019.

Basic earnings per share (“EPS”) for the nine months ended September 30, 2020 was \$1.02, a decrease of \$0.13 from \$1.15 for the nine months ended September 30, 2019. Diluted EPS for the nine months ended September 30, 2020 was \$1.02, a decrease of \$0.11 from \$1.13 for the nine months ended September 30, 2019.

### *Net Interest Income*

For the nine months ended September 30, 2020, net interest income before provisions for credit losses totaled \$199.0 million and net interest margin and net interest spread were 3.42% and 3.10%, respectively. For the nine months ended September 30, 2019, net interest income totaled \$215.2 million and net interest margin and net interest spread were 4.02% and 3.53%, respectively. The decrease in net interest income of \$16.2 million was primarily due to a \$41.4 million decrease in interest income on loans, partially offset by a \$21.0 million decrease in interest expense on transaction and savings deposits during the nine months ended September 30, 2020 compared to the nine months ended September 30, 2019. The decrease in interest income on loans was due to lower loan yields. The \$30.5 million decrease in interest expense on deposit accounts was due to lower rates on deposit accounts. Net interest margin decreased 60 basis points from the nine months ended September 30, 2019 primarily due to a decrease in yields earned on loan balances, partially offset by decreases in the average rate paid on interest-bearing demand and savings deposits in the nine months ended September 30, 2020 and an unfavorable shift in the mix of earning assets compared to the nine months ended September 30, 2019. As a result, the average cost of interest-bearing deposits decreased 77 basis points to 0.97% for the nine months ended September 30, 2020 from 1.74% for the nine months ended September 30, 2019.

For the nine months ended September 30, 2020, interest expense totaled \$44.7 million and the average rate paid on interest-bearing liabilities was 1.09%. For the nine months ended September 30, 2019, interest expense totaled \$71.8 million and the average rate paid on interest-bearing liabilities was 1.84%. The decrease in interest expense of \$27.1 million was due to a \$21.0 million decrease in the average rate paid on interest-bearing demand and savings deposits and a \$9.5 million decrease in the average rate paid on time deposits, partially offset by a \$3.4 million increase in interest paid on borrowings.

The following table presents, for the periods indicated, an analysis of net interest income by each major category of interest-earning assets and interest-bearing liabilities, the average amounts outstanding and the interest earned or paid on such amounts. The table also sets forth the average rate earned on interest-earning assets, the average rate paid on interest-bearing liabilities, and the net interest margin on average total interest-earning assets for the same periods. Interest earned on loans that are classified as non-accrual is not recognized in income; however, the balances are reflected in average outstanding balances for the period. For the nine months ended September 30, 2020, interest income not recognized on non-accrual loans was \$3.0 million. For the nine months ended September 30, 2019, interest income not recognized on non-accrual loans was \$288 thousand. Any non-accrual loans have been included in the table as loans carrying a zero yield.

	For the Nine Months Ended September 30,					
	2020			2019		
	Average Outstanding Balance	Interest Earned/ Interest Paid	Average Yield/ Rate	Average Outstanding Balance	Interest Earned/ Interest Paid	Average Yield/ Rate
(Dollars in thousands)						
<b>Assets</b>						
Interest-earning assets:						
Loans <sup>(1)</sup>	\$ 5,779,469	\$ 208,889	4.83 %	\$ 5,731,902	\$ 253,247	5.91 %
Loans held for investment, mortgage warehouse	275,890	6,318	3.06	152,617	5,097	4.47
PPP loans	236,778	1,779	1.00	—	—	—
Investment securities	1,086,185	23,074	2.84	968,616	22,316	3.08
Interest-bearing deposits in other banks	283,108	1,122	0.53	242,119	4,255	2.35
Other investments	102,185	2,568	3.36	56,438	2,129	5.04
Total interest-earning assets	7,763,615	243,750	4.19	7,151,692	287,044	5.37
Allowance for credit losses	(90,633)			(22,173)		
Noninterest-earning assets	776,790			799,509		
Total assets	\$ 8,449,772			\$ 7,929,028		
<b>Liabilities and Stockholders' Equity</b>						
Interest-bearing liabilities:						
Interest-bearing demand and savings deposits	\$ 2,680,925	\$ 11,128	0.55 %	\$ 2,657,195	\$ 32,152	1.62 %
Certificates and other time deposits	1,579,114	19,759	1.67	2,067,032	29,220	1.89
Advances from FHLB	1,070,856	8,387	1.05	427,306	7,323	2.29
Subordinated debentures and subordinated notes	143,387	5,444	5.07	75,298	3,116	5.53
Total interest-bearing liabilities	5,474,282	44,718	1.09	5,226,831	71,811	1.84
Noninterest-bearing liabilities:						
Noninterest-bearing deposits	1,763,289			1,459,904		
Other liabilities	57,737			42,853		
Total liabilities	7,295,308			6,729,588		
Stockholders' equity	1,154,464			1,199,440		
Total liabilities and stockholders' equity	\$ 8,449,772			\$ 7,929,028		
Net interest rate spread <sup>(2)</sup>			3.10 %			3.53 %
Net interest income		\$ 199,032			\$ 215,233	
Net interest margin <sup>(3)</sup>			3.42 %			4.02 %

<sup>(1)</sup> Includes average outstanding balances of loans held for sale of \$16,448 and \$8,127 for the nine months ended September 30, 2020 and September 30, 2019, respectively, and average balances of loans held for investment, excluding mortgage warehouse.

<sup>(2)</sup> Net interest rate spread is equal to the average yield on interest-earning assets minus the average rate on interest-bearing liabilities.

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

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

	For the Nine Months Ended September 30, 2020 vs. 2019		
	Increase (Decrease) Due to Change in		
	Volume	Rate	Total
	(In thousands)		
<b>Interest-earning assets:</b>			
Loans	\$ 2,104	\$ (46,462)	\$ (44,358)
Loans held for investment, mortgage warehouse	4,125	(2,904)	1,221
PPP loans	1,779	—	1,779
Securities	2,711	(1,953)	758
Interest-bearing deposits in other banks	721	(3,854)	(3,133)
Other investments	1,726	(1,287)	439
Total increase in interest income	<u>13,166</u>	<u>(56,460)</u>	<u>(43,294)</u>
<b>Interest-bearing liabilities:</b>			
Interest-bearing demand and savings deposits	287	(21,311)	(21,024)
Certificates and other time deposits	(6,904)	(2,557)	(9,461)
Advances from FHLB	11,039	(9,975)	1,064
Subordinated debentures and subordinated notes	2,820	(492)	2,328
Total increase in interest expense	<u>7,242</u>	<u>(34,335)</u>	<u>(27,093)</u>
Increase in net interest income	<u>\$ 5,924</u>	<u>\$ (22,125)</u>	<u>\$ (16,201)</u>

#### *Provision for Credit Losses*

Our provision for credit losses is a charge to income in order to bring our allowance for credit losses to a level deemed appropriate by management. For a description of the factors taken into account by management in determining the allowance for credit losses see “—Financial Condition —Allowance for Credit Losses on Loans Held for Investment.” The provision for credit losses was \$56.6 million for the nine months ended September 30, 2020, compared to \$18.0 million for the same period in 2019, an increase of \$38.6 million, or 214.3%. The increase in the recorded provision for credit losses for the nine months ended September 30, 2020 was primarily attributable to the implementation of CECL on January 1, 2020 which resulted in a required increase in our provision of \$19.4 million. Subsequent to implementation, the increase was further due to changes in the Texas economic forecasts used in the CECL model during the nine months ended September 30, 2020 to reflect the expected impact of the COVID-19 pandemic. In the nine months ended September 30, 2020, we also recorded an \$8.1 million provision for unfunded commitments, which was also attributable to the change in the economic forecasts as a result of the COVID-19 pandemic. Allowance for credit losses as a percentage of loans held for investment, excluding mortgage warehouse and PPP loans, was 2.10%, 2.01% and 0.46% of total loans at September 30, 2020, June 30, 2020 and September 30, 2019, respectively.

## Noninterest Income

The following table presents, for the periods indicated, the major categories of noninterest income:

	For the Nine Months Ended September 30,		Increase (Decrease)
	2020	2019	
(In thousands)			
<b>Noninterest income:</b>			
Service charges and fees on deposit accounts	\$ 9,732	\$ 10,606	\$ (874)
Loan fees	5,027	5,861	(834)
Gain (loss) on sales of investment securities	2,871	(1,414)	4,285
Gain on sales of mortgage loans	922	394	528
Government guaranteed loan income, net	13,702	4,148	9,554
Rental income	1,600	1,629	(29)
Other	4,478	1,724	2,754
<b>Total noninterest income</b>	<b>\$ 38,332</b>	<b>\$ 22,948</b>	<b>\$ 15,384</b>

Noninterest income for the nine months ended September 30, 2020 increased \$15.4 million, or 67.0%, to \$38.3 million compared to noninterest income of \$22.9 million for the same period in 2019. The primary drivers of the increase were as follows:

*Gain (loss) on sales of investment securities.* The increase of \$4.3 million in gain on sales of investment securities was primarily due to a decrease in market interest rates below coupon rates for securities sold during the nine months ended September 30, 2020 as compared to \$1.4 million loss on sales of investment securities during the nine months ended September 30, 2019 as a result of a repositioning strategy following the acquisition of Green Bancorp, Inc.

*Government guaranteed loan income, net.* Government guaranteed loan income, net includes non-interest income earned on PPP loans as well as income related to the sales of SBA loans. The increase in government guaranteed loan income, net of \$9.6 million was primarily due to the increase in PPP loans originated and the impact of the fair value option election on these loans during the nine months ended September 30, 2020. The Company earned fee income of 5%, \$7.0 million, on PPP loans with balances under \$350 thousand, 3%, or \$4.4 million, on PPP loans with balances between \$350 thousand and \$2 million and 1%, or \$1.1 million, on PPP loans with balances greater than \$2 million. This income was recognized upon origination as the Company elected the fair value option for PPP loan income. The increase in government guaranteed loan income, net was partially offset by a \$2.6 million change in fair value for SBA and PPP loans elected to be accounted for under the fair value option and a decrease on gains on sale of non-PPP SBA loans of \$291 thousand.

*Other.* The increase in other noninterest income of \$2.8 million in nine months ended September 30, 2020 as compared to the same period in 2019 was primarily driven by an increase in derivative income of \$943 thousand, gain on sale of bank premises, furniture and equipment of \$358 thousand, and an insurance reimbursement on branch premises, furniture and equipment of \$214 thousand.

## Noninterest Expense

The following table presents, for the periods indicated, the major categories of noninterest expense:

	For the Nine Months Ended September 30,		Increase (Decrease)
	2020	2019	2020 vs. 2019
	(In thousands)		
Salaries and employee benefits	\$ 59,442	\$ 53,874	\$ 5,568
Non-staff expenses:			
Occupancy and equipment	12,247	12,187	60
Professional and regulatory fees	8,151	8,982	(831)
Data processing and software expense	6,975	6,485	490
Marketing	2,706	2,288	418
Amortization of intangibles	8,232	8,191	41
Telephone and communications	972	1,381	(409)
Merger and acquisition expense	—	38,042	(38,042)
COVID expenses	1,377	—	1,377
Other	11,912	10,089	1,823
Total noninterest expense	<u>\$ 112,014</u>	<u>\$ 141,519</u>	<u>\$ (29,505)</u>

Noninterest expense for the nine months ended September 30, 2020 decreased \$29.5 million, or 20.8%, to \$112.0 million compared to noninterest expense of \$141.5 million for the nine months ended September 30, 2019. The most significant components of the decrease were as follows:

*Salaries and employee benefits.* Salaries and employee benefits include payroll expense, the cost of incentive compensation, benefit plans, health insurance and payroll taxes. These expenses are impacted by the amount of direct loan origination costs, which are required to be deferred in accordance with ASC 310-20 (formerly FAS91). Salaries and employee benefits were \$59.4 million for the nine months ended September 30, 2020, an increase \$5.6 million, or 10.3%, compared to the same period in 2019. The increase was primarily attributable to increased incentive costs of \$3.8 million due to increased loan production due to PPP loans origination during the nine months ended September 30, 2020. The increase is also due to an increase in compensation costs of \$2.7 million due to the hiring of several new officers increasing officer salaries by \$1.5 million and increased severance costs of \$678.

*Merger and acquisition expense.* This category includes legal, professional, audit, regulatory, severance and change-in-control payments, stock-based compensation, conversion related data processing and software expense and other expenses incurred in connection with a merger or acquisition. No merger and acquisition expenses were incurred in the nine months ended September 30, 2020, as our acquisition of Green Bancorp, Inc. ("Green") was completed in 2019. These expenses incurred in the nine months ended September 30, 2019 were primarily driven by a \$17.1 million increase in stock-based compensation due to the accelerated vesting of outstanding restricted stock units and stock options related to the Green acquisition, a \$9.0 million increase in severance and change-in-control payments, a \$3.1 million increase in professional services expenses and a \$1.6 million increase in data processing expense as a result of our system conversions in connection with our acquisition of Green.

*COVID expenses.* This category of expenses includes expenses related to the COVID-19 pandemic such as PPP incentive compensation of \$500 thousand, CRA donations of \$471 thousand, employee salaries of \$273 thousand and increased cleaning expenses of \$30 thousand.

*Other noninterest expense.* This category includes loan operations and collections, supplies and printing, automatic teller and online expenses and other miscellaneous expenses. Other noninterest expense was \$11.9 million for the nine months ended September 30, 2020 compared to \$10.1 million for the same period in 2019, an increase \$1.8 million, or 18.1%. This increase was primarily due to an increase in bank service charges resulting from pre-payment fees on FHLB advances paid off early of \$1.6 million during the nine months ended September 30, 2020. The increase was also driven by an increase in loan appraisal fees of \$232 thousand and problem loan fees of \$229 thousand during the nine months ended September 30, 2020 as compared to the same period in 2019.

#### *Income Tax Expense*

Income tax expense is a function of our pre-tax income, tax-exempt income and other nondeductible expenses. Deferred tax assets and liabilities reflect current statutory income tax rates in effect for the period in which the deferred tax assets and liabilities are expected to be realized or settled. As changes in tax laws or statutory tax rates are enacted, deferred tax assets and liabilities are adjusted through the provision of income taxes. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized. As of September 30, 2020, we did not believe a valuation allowance was necessary.

For the nine months ended September 30, 2020, income tax expense totaled \$9.5 million, a decrease of \$7.5 million, or 44.0%, compared to a income tax expense of \$17.0 million for the same period in 2019. The effective tax rate for the nine months ended September 30, 2020 was 15.7%, a decrease as compared to the effective tax rate of 21.6% for the same period in 2019. The decrease in income tax expense was primarily attributable to the decrease in net income from operations to \$60.6 million for the nine months ended September 30, 2020 from \$78.6 million for the same period in 2019. The decrease in income tax expense and effective tax rate was also driven by a net discrete tax benefit of \$1.8 million as a result of the Company amending a prior year Green tax return to carry back a net operating loss ("NOL") incurred by Green Bancorp, Inc. on January 1, 2019 and a net discrete tax benefit of \$1.4 million primarily associated with the recognition of excess tax benefit realized on share-based payment awards during the nine months ended September 30, 2020. Excluding these discrete tax items, the Company had an effective tax rate of 21.0% for the nine months ended September 30, 2020.

## Results of Operations for the Three Months Ended September 30, 2020 and 2019

### General

Net income for the three months ended September 30, 2020 was \$22.9 million, a decrease of \$4.5 million, or 16.4%, from net income of \$27.4 million for the three months ended September 30, 2019.

Basic EPS for the three months ended September 30, 2020 was \$0.46, a decrease of \$0.06 from \$0.52 for the three months ended September 30, 2019. Diluted EPS for the three months ended September 30, 2020 was \$0.46, a decrease of \$0.05 from \$0.51 for the three months ended September 30, 2019.

### Net Interest Income

For the three months ended September 30, 2020, net interest income totaled \$65.9 million and net interest margin and net interest spread were 3.32% and 3.05%, respectively. For the three months ended September 30, 2019, net interest income totaled \$70.9 million and net interest margin and net interest spread were 3.90% and 3.40%, respectively. The decrease in net interest income was primarily due to a \$17.1 million decrease in interest income on loans, partially offset by an \$8.3 million decrease in interest expense on transaction and savings deposits during the three months ended September 30, 2020 compared to the three months ended September 30, 2019. Net interest margin decreased 58 basis points from the three months ended September 30, 2019 primarily due to a decrease in yields earned on loan balances, partially offset by decreases in the average rate paid on interest-bearing demand and savings deposits and certificate and other time deposits in the three months ended September 30, 2020. As a result, the average cost of interest-bearing deposits decreased to 0.67% for the three months ended September 30, 2020 from 1.79% for the three months ended September 30, 2019.

For the three months ended September 30, 2020, interest expense totaled \$11.6 million and the average rate paid on interest-bearing liabilities was 0.85%. For the three months ended September 30, 2019, interest expense totaled \$24.8 million and the average rate paid on interest-bearing liabilities was 1.86%. The decrease in interest expense of \$13.2 million was primarily due to a decrease in yields earned on loan balances, and decreases in the average rate paid on interest-bearing demand and savings deposits in the three months ended September 30, 2020. As a result, the average cost of interest-bearing deposits decreased to 0.67% for the three months ended September 30, 2020 from 1.79% for the three months ended September 30, 2019.

The following table presents, for the periods indicated, an analysis of net interest income by each major category of interest-earning assets and interest-bearing liabilities, the average amounts outstanding and the interest earned or paid on such amounts. The table also sets forth the average rate earned on interest-earning assets, the average rate paid on interest-bearing liabilities, and the net interest margin on average total interest-earning assets for the same periods. Interest earned on loans that are classified as non-accrual is not recognized in income; however, the balances are reflected in average outstanding balances for the period. For the three months ended September 30, 2020, interest income not recognized on non-accrual loans was \$2.5 million. For the three months ended September 30, 2019, interest income not recognized on non-accrual loans was \$243 thousand. Any non-accrual loans have been included in the table as loans carrying a zero yield.



**For the Three Months Ended September 30,**

	2020			2019		
	Average Outstanding Balance	Interest Earned/ Interest Paid	Average Yield/ Rate	Average Outstanding Balance	Interest Earned/ Interest Paid	Average Yield/ Rate
<b>(Dollars in thousands)</b>						
<b>Assets</b>						
Interest-earning assets:						
Loans <sup>(1)</sup>	\$ 5,753,859	\$ 64,958	4.49 %	\$ 5,702,696	\$ 84,022	5.85 %
Loans held for investment, mortgage warehouse	358,248	2,705	3.00	182,793	1,789	3.88
PPP loans	407,112	1,022	1.00	—	—	—
Securities	1,101,469	7,852	2.84	1,022,289	7,687	2.98
Interest-earning deposits in other banks	175,201	65	0.15	234,087	1,329	2.25
Other investments	103,948	827	3.17	71,901	816	4.50
Total interest-earning assets	7,899,837	77,429	3.90	7,213,766	95,643	5.26
Allowance for credit losses	(116,859)			(22,539)		
Noninterest-earning assets	802,948			818,150		
Total assets	\$ 8,585,926			\$ 8,009,377		
<b>Liabilities and Stockholders' Equity</b>						
Interest-bearing liabilities:						
Interest-bearing demand and savings deposits	\$ 2,735,170	\$ 2,105	0.31 %	\$ 2,621,701	\$ 10,381	1.57 %
Certificates and other time deposits	1,459,046	5,004	1.36	1,953,084	10,283	2.09
Advances from FHLB	1,067,771	2,707	1.01	632,754	3,081	1.93
Subordinated debentures and subordinated debt	142,432	1,743	4.87	74,869	1,024	5.43
Total interest-bearing liabilities	5,404,419	11,559	0.85	5,282,408	24,769	1.86
Noninterest-bearing liabilities:						
Noninterest-bearing deposits	1,937,921			1,467,127		
Other liabilities	65,704			49,695		
Total liabilities	7,408,044			6,799,230		
Stockholders' equity	1,177,882			1,210,147		
Total liabilities and stockholders' equity	\$ 8,585,926			\$ 8,009,377		
Net interest rate spread <sup>(2)</sup>			3.05 %			3.40 %
Net interest income		\$ 65,870			\$ 70,874	
Net interest margin <sup>(3)</sup>			3.32 %			3.90 %

<sup>(1)</sup> Includes average outstanding balances of loans held for sale of \$15,404 and \$8,525 for the three months ended September 30, 2020 and September 30, 2019, respectively, and average balances of loans held for investment, excluding mortgage warehouse.

<sup>(2)</sup> Net interest rate spread is equal to the average yield on interest-earning assets minus the average rate on interest-bearing liabilities.

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

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

	For the Three Months Ended September 30, 2020 vs. 2019		
	Increase (Decrease) Due to Change in		
	Volume	Rate	Total
	(In thousands)		
<b>Interest-earning assets:</b>			
Loans	\$ 752	\$ (19,816)	\$ (19,064)
Loans held for investments, mortgage warehouse	1,711	(795)	916
PPP loans	1,022	—	1,022
Securities	593	(428)	165
Other investments	(333)	(931)	(1,264)
Interest-bearing deposits in other banks	362	(351)	11
Total increase in interest income	<u>4,107</u>	<u>(22,321)</u>	<u>(18,214)</u>
<b>Interest-bearing liabilities:</b>			
Interest-bearing demand and savings deposits	448	(8,724)	(8,276)
Certificates and other time deposits	(2,594)	(2,685)	(5,279)
Advances from FHLB	2,112	(2,486)	(374)
Subordinated debentures and subordinated notes	922	(203)	719
Total increase in interest expense	<u>888</u>	<u>(14,098)</u>	<u>(13,210)</u>
Increase in net interest income	<u>\$ 3,219</u>	<u>\$ (8,223)</u>	<u>\$ (5,004)</u>

#### *Provision for Credit Losses*

The provision for credit losses was \$8.7 million for the three months ended September 30, 2020, compared to \$9.7 million for the same period in 2019, a decrease of \$1.0 million, or 10.2%. On January 1, 2020, the Company implemented CECL which transitioned our estimate of the provision for credit losses from an incurred loss model to an expected loss model. The decreased provision for credit losses was driven by relatively minimal change to the Texas economic indicators that the Company forecasts to calculate expected losses under CECL. Prior to the three months ended September 30, 2020, significant deterioration in these forecasted Texas economic indicators was brought on by the projected economic impact of COVID on the reasonable and supportable forecast period. At September 30, 2020, changes to the forecasted Texas economic indicators changed minimally as management's expectations for these Texas economic indicators did not change materially from June 30, 2020. We recorded a \$13.2 million increase in specific reserves on certain lending relationships that moved onto nonaccrual status during the three months ended September 30, 2020 which was slightly offset by a \$2.4 million charge-off and resulting \$1.7 million recovery of a previously recorded specific reserves and changes to the forecasted Texas economic indicators resulting in a \$404 thousand decrease in our provision for credit losses. For the three months ended September 30, 2019, the provision for credit losses was primarily attributable to a \$6.1 million charge-off of a commercial loan relationship acquired from Sovereign Bancshares, Inc. in 2017. The acquired commercial loan relationship was a loan to an independent oil and gas exploration company that filed for bankruptcy protection in 2018 and entered into a sales process pursuant to Section 363 of the Bankruptcy Code during the third quarter of 2019. Changes to loss factors under the incurred loss allowance methodology had an insignificant impact on provision for credit losses for the third quarter of 2019. In the third quarter of 2020, we also recorded a \$1.4 million provision for unfunded commitments, which was also attributable to the change in the economic forecasts as a result of the COVID-19 pandemic.

## Noninterest Income

The following table presents, for the periods indicated, the major categories of noninterest income:

	For the Three Months Ended September 30,		Increase
	2020	2019	(Decrease)
(In thousands)			
<b>Noninterest income:</b>			
Service charges and fees on deposit accounts	\$ 3,130	\$ 3,667	\$ (537)
Loan fees	1,787	2,252	(465)
Gain (loss) on sales of investment securities	(8)	—	(8)
Gain on sales of mortgage loans	472	32	440
Government guaranteed loan income, net	2,257	930	1,327
Rental income	502	643	(141)
Other	1,655	906	749
<b>Total noninterest income</b>	<b>\$ 9,795</b>	<b>\$ 8,430</b>	<b>\$ 1,365</b>

Noninterest income for the three months ended September 30, 2020 increased \$1.4 million, or 16.2%, to \$9.8 million compared to noninterest income of \$8.4 million for the same period in 2019. The primary components of the increase were as follows:

*Government guaranteed loan income, net.* Government guaranteed loan income, net includes income earned on PPP loans as well as income related to the sales of SBA loans. The increase in government guaranteed fee income was primarily due to the increase in government guaranteed loans, specifically non-PPP SBA loans, originated and sold during the three months ended September 30, 2020.

## Noninterest Expense

The following table presents, for the periods indicated, the major categories of noninterest expense:

	For the Three Months Ended September 30,		Increase (Decrease)
	2020	2019	2020 vs. 2019
(In thousands)			
Salaries and employee benefits	\$ 20,553	\$ 17,530	\$ 3,023
<b>Non-staff expenses:</b>			
Occupancy and equipment	3,980	4,044	(64)
Professional and regulatory fees	3,159	2,750	409
Data processing and software expense	2,452	2,252	200
Marketing	1,062	708	354
Amortization of intangibles	2,840	2,712	128
Telephone and communications	345	361	(16)
Merger and acquisition expense	—	1,035	(1,035)
COVID expenses	132	—	132
Other	1,885	3,238	(1,353)
<b>Total noninterest expense</b>	<b>\$ 36,408</b>	<b>\$ 34,630</b>	<b>\$ 1,778</b>

Noninterest expense for the three months ended September 30, 2020 increased \$1.8 million, or 5.1%, to \$36.4 million compared to noninterest expense of \$34.6 million for the three months ended September 30, 2019. The most significant components of the increase were as follows:

*Salaries and employee benefits.* Salaries and employee benefits include payroll expense, the cost of incentive compensation, benefit plans, health insurance and payroll taxes. These expenses are impacted by the amount of direct loan origination costs, which are required to be deferred in accordance with ASC 310-20 (formerly FAS91). Salaries and employee benefits were \$20.6 million for the three months ended September 30, 2020, an increase of \$3.0 million, or 17.2%, compared to the same period in 2019. The increase was primarily attributable to increased employee compensation of \$1.7 million, mainly attributed to an increase in officer salaries due to several new officer hires, and an increase in stock-based compensation costs of \$649 thousand, in the three months ended September 30, 2020 as compared to the same period in 2019.

*Merger and acquisition expense.* This category includes legal, professional, audit, regulatory, severance and change-in-control payments, stock-based compensation, conversion related data processing and software expense and other expenses incurred in connection with a merger or acquisition. No merger and acquisition expenses were incurred in the three months ended September 30, 2020, as our acquisition of Green Bancorp, Inc. ("Green") was completed in 2019.

*Other noninterest expense.* This category includes loan and collection expenses, supplies and printing, postage, automatic teller and online expenses and other miscellaneous expenses. Other noninterest expense was \$1.9 million for the three months ended September 30, 2020 compared to \$3.2 million for the same period in 2019, a decrease of \$1.4 million, or 41.8%. This decrease was primarily due to a decrease in problem loan fees of \$565 thousand and a decrease in auto and travel expense of \$241 thousand during the three months ended September 30, 2020 due to COVID.

#### *Income Tax Expense*

For the three months ended September 30, 2020, income tax expense totaled \$6.2 million, a decrease of \$1.4 million, or 18.4%, compared to \$7.6 million for the same period in 2019. The effective tax rate for the three months ended September 30, 2020 was 21.3% compared to 21.7% for the same period in 2019. The decrease in income tax expense was primarily attributable to the decrease in net income from operations to \$29.1 million for the three months ended September 30, 2020 from \$35.0 million the same period in 2019. The decrease was slightly offset by a net discrete tax expense of \$32 thousand primarily associated with the recognition of an excess tax expense realized on share-based payment awards during the three months ended September 30, 2020. Excluding this discrete tax item, the Company had an effective tax rate of 21.2% for the three months ended September 30, 2020.

#### **Financial Condition**

Our total assets increased \$747.4 million, or 9.4%, from \$8.0 billion as of December 31, 2019 to \$8.7 billion as of September 30, 2020. Our asset growth was due to the continued execution of our strategy to establish deep relationships in the Dallas-Fort Worth metroplex and the Houston metropolitan area as well as our PPP loan portfolio, with which we serve small businesses impacted by COVID-19. We believe these relationships will continue to bring in new customer accounts and grow balances from existing loan and deposit customers.

#### *Loan Portfolio*

Our primary source of income is interest on loans to individuals, professionals, small to medium-sized businesses and commercial companies located in the Dallas-Fort Worth metroplex and Houston metropolitan area. Our loan portfolio consists primarily of commercial loans and real estate loans secured by commercial real estate properties located in our primary market area. Our loan portfolio represents the highest yielding component of our earning asset base.

As of September 30, 2020, total loans held for investment, excluding allowance for credit losses ("ACL"), was \$6.8 billion, an increase of \$818.2 million, or 13.8%, compared to \$5.9 billion as of December 31, 2019. The increase was the result of the continued execution and success of our loan growth strategy as well as our PPP loan portfolio, with which we serve our small businesses impacted by COVID-19. In addition to these amounts, \$13.9 million and \$14.1 million in loans were classified as held for sale as of September 30, 2020 and December 31, 2019, respectively.

Total loans held for investment, excluding mortgage warehouse and PPP, as a percentage of deposits were 93.0% and 97.3% as of September 30, 2020 and December 31, 2019, respectively. Total loans excluding mortgage warehouse and PPP as a percentage of deposits were 93.0% and 93.5% as of September 30, 2020 and December 31, 2019, respectively. Total loans as a percentage of assets were 72.8% and 74.4% as of September 30, 2020 and December 31, 2019, respectively.

The following table summarizes our loan portfolio by type of loan as of the dates indicated:

	As of September 30, 2020		As of December 31, 2019	
	Total	Percent	Total	Percent
(Dollars in thousands)				
Commercial	\$ 1,623,249	25.6 %	\$ 1,712,838	28.9 %
Mortgage warehouse	544,845	8.6 %	183,628	3.1 %
Real estate:				
Owner Occupied CRE (“OOCRE”)	734,939	11.6 %	706,782	11.8 %
Non-owner Occupied CRE (“NOOCRE”)	1,817,013	28.7 %	1,784,201	30.1 %
Construction and land	623,496	9.8 %	629,374	10.6 %
Farmland	14,413	0.2 %	16,939	0.3 %
1-4 family residential	548,953	8.7 %	549,811	9.3 %
Multifamily	412,412	6.5 %	320,041	5.4 %
Consumer	14,127	0.3 %	17,457	0.3 %
Total loans held for investment, carried at amortized cost	<u>\$ 6,333,447</u>	<u>100.0 %</u>	<u>\$ 5,921,071</u>	<u>100.0 %</u>
Held for investment PPP loans, carried at fair value	<u>\$ 405,465</u>	<u>100.0 %</u>	<u>\$ —</u>	<u>— %</u>
Total loans held for sale	<u>\$ 13,928</u>	<u>100.0 %</u>	<u>\$ 14,080</u>	<u>100.0 %</u>

## Nonperforming Assets

The following table presents information regarding nonperforming assets at the dates indicated:

	As of September 30, 2020	As of December 31, 2019
(Dollars in thousands)		
Non-accrual loans	\$ 88,877	\$ 29,779
Accruing loans 90 or more days past due	1,689	3,660
<b>Total nonperforming loans</b>	<b>90,566</b>	<b>33,439</b>
Other real estate owned:		
Commercial and Industrial	4,831	4,242
Commercial real estate, construction, land and land development	—	1,087
Residential real estate	965	666
Total other real estate owned	5,796	5,995
<b>Total nonperforming assets</b>	<b>\$ 96,362</b>	<b>\$ 39,434</b>
Restructured loans—non-accrual	23,230	1,457
Restructured loans—accruing	6,429	686
Ratio of nonperforming loans to total loans	1.56 %	0.56 %
Ratio of nonperforming assets to total assets	1.11 %	0.50 %

The following table presents information regarding non-accrual loans by category as of the dates indicated:

	As of September 30, 2020	As of December 31, 2019
(In thousands)		
Commercial	\$ 42,182	\$ 5,672
Real estate:		
OOCRE	5,310	3,029
NOOCRE	37,048	18,876
Construction and land	785	567
1-4 family residential	2,366	1,581
Consumer	1,186	54
<b>Total</b>	<b>\$ 88,877</b>	<b>\$ 29,779</b>

Potential Problem Loans

The following tables summarize our internal ratings of our loans as of the dates indicated.

	September 30, 2020					
	Pass	Special Mention	Substandard	Doubtful	PCD	Total
Real estate:						
Construction and land	\$ 616,292	\$ 2,879	\$ 1,640	\$ —	\$ 2,685	\$ 623,496
Farmland	14,413	—	—	—	—	14,413
1 - 4 family residential	536,566	3,009	5,111	—	4,267	548,953
Multi-family residential	381,091	12,661	18,660	—	—	412,412
Commercial real estate	2,163,887	202,053	93,664	—	92,348	2,551,952
Commercial	1,444,611	65,217	91,056	—	22,365	1,623,249
Mortgage warehouse	544,845	—	—	—	—	544,845
Consumer	12,249	314	1,357	—	207	14,127
Total	<u>\$ 5,713,954</u>	<u>\$ 286,133</u>	<u>\$ 211,488</u>	<u>\$ —</u>	<u>\$ 121,872</u>	<u>\$ 6,333,447</u>

	December 31, 2019					
	Pass	Special Mention	Substandard	Doubtful	PCD	Total
Real estate:						
Construction and land	\$ 618,773	\$ 3,965	\$ 2,689	\$ —	\$ 3,947	\$ 629,374
Farmland	16,939	—	—	—	—	16,939
1 - 4 family residential	541,787	795	3,460	—	3,769	549,811
Multi-family residential	320,041	—	—	—	—	320,041
Commercial real estate	2,332,357	23,494	38,278	—	96,854	2,490,983
Commercial	1,610,150	51,999	28,670	—	22,019	1,712,838
Mortgage warehouse	183,628	—	—	—	—	183,628
Consumer	17,106	40	182	—	129	17,457
Total	<u>\$ 5,640,781</u>	<u>\$ 80,293</u>	<u>\$ 73,279</u>	<u>\$ —</u>	<u>\$ 126,718</u>	<u>\$ 5,921,071</u>

ACL on loans held for investment

The ACL is an allowance of estimated credit losses at each balance sheet date in accordance with GAAP that is deducted from the loans' amortized cost basis to present the net amount expected to be collected on the loans. When the Company deems all or a portion of a loan to be uncollectible, the appropriate amount is written off and the ACL is reduced by the same amount. Subsequent recoveries, if any, are credited to the ACL when received. See Note 1 – "Summary of Significant Accounting Policies" in the notes to the condensed consolidated financial statements included elsewhere in this report for discussion of our ACL methodology on loans.

The following table presents, as of and for the periods indicated, an analysis of the allowance for credit losses and other related data:

	As of September 30, 2020		As of December 31, 2019	
	Amount	Percent of Total	Amount	Percent of Total
(Dollars in thousands)				
Real estate:				
Construction and land	\$ 9,590	7.9	\$ 3,822	12.8 %
Farmland	70	0.1	61	0.2
1 - 4 family residential	10,605	8.7	1,378	4.6
Multi-family residential	6,696	5.5	1,965	6.6
OOCRE	8,549	7.0	1,978	6.6
NOOCRE	35,821	29.5	8,139	27.3
Total real estate	\$ 71,331	58.7 %	\$ 17,343	58.1 %
Commercial	49,677	40.9	12,369	41.5
Consumer	583	0.4	122	0.4
Total allowance for credit losses	\$ 121,591	100.0 %	\$ 29,834	100.0 %

The ACL increased \$91.8 million, or 307.6%, as of September 30, 2020 from December 31, 2019. Upon adoption of ASU 2016-13 on January 1, 2020, the Company recorded an increase of \$39.1 million to the ACL. The primary reasons for the increase in required ACL are the Company's adoption of CECL on January 1, 2020 and significant projected deterioration of the loss drivers that the Company forecasts to calculate expected losses. This deterioration was brought on by the projected economic impact of COVID-19 on the Company's loss drivers over the reasonable and supportable forecast period and created the need for additional ACL.

The Company uses the discounted cash flow (DCF) method to estimate ACL for non-PCD owner occupied and non-owner occupied commercial real estate, construction and land development, 1-4 family residential, commercial and consumer loan pools. The Company leverages economic projections from a reputable and independent third party to include in its loss driver forecasts. Other internal and external indicators of economic forecasts are also considered by the Company when developing the forecast metrics. See Note 1 – "Summary of Significant Accounting Policies" in the notes to the condensed consolidated financial statements included elsewhere in this report for discussion of our DCF methodology and economic projections.

Consistent forecasts of the loss drivers are used across the loan segments. For all DCF models at September 30, 2020, the Company has determined that four quarters represents a reasonable and supportable forecast period and the Company will revert back to a historical loss rate over an additional four quarters on a straight-line basis. At September 30, 2020, the Company forecasted increased Texas unemployment and a year over year percentage decrease in Texas gross domestic product growth for a one year forecast period over historical averages. The Company projected gradual improvement in these loss drivers over the next four quarters with these loss drivers remaining below historical trends over the past several years.



The following table provides an analysis of the provisions for loan losses, net charge-offs and recoveries and the effects of those items on our ACL:

	Nine Months Ended September 30, 2020	Nine Months Ended September 30, 2019
	(Dollars in thousands)	
Average loans outstanding <sup>(1)</sup>	\$ 6,055,359	\$ 5,884,519
Amortized costs of loans outstanding at end of period excluding mortgage warehouse and PPP loans <sup>(1)</sup>	5,789,293	5,737,577
Amortized costs of loans outstanding at end of period <sup>(1)</sup>	6,334,829	5,654,161
Allowance for credit losses at beginning of period	29,834	19,255
Impact of adopting ASC 326	39,137	—
Provision for credit losses	56,640	18,021
Charge-offs:		
Real estate:		
Residential	—	(157)
Commercial Real Estate	(2,421)	—
Commercial	(1,808)	(10,898)
Consumer	(136)	(217)
Total charge-offs	(4,365)	(11,272)
Recoveries:		
Real estate:		
Residential	8	62
Commercial	50	91
Consumer	287	86
Total recoveries	345	239
Net charge-offs	(4,020)	(11,033)
Allowance for credit losses at end of period	\$ 121,591	\$ 26,243
Ratio of allowance to end of period loans excluding mortgage warehouse and PPP loans	2.10 %	0.46 %
Ratio of net charge-offs to average loans	0.07 %	0.19 %

<sup>(1)</sup> Excludes loans held for sale.

We believe the successful execution of our growth strategy through key acquisitions and organic growth is demonstrated by the upward trend in loan balances from December 31, 2019 to September 30, 2020. Total loan balances increased from \$5.9 billion as of December 31, 2019 to \$6.8 billion as of September 30, 2020. Net charge-offs represented 0.07% and 0.19% of average loan balances for the nine months ended September 30, 2020 and 2019, respectively.

#### Equity Securities

As of September 30, 2020, we held equity securities with a readily determinable fair value of \$11.6 million compared to \$11.1 million as of December 31, 2019. These equity securities primarily represent investments in a publicly traded Community Reinvestment Act fund and are subject to market pricing volatility, with changes in fair value recorded in earnings.

The Company held equity securities without a readily determinable fair values and measured at cost of \$3.6 million at September 30, 2020 and December 31, 2019, respectively. The Company measures equity securities that do not have readily determinable fair values at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer.

#### FHLB Stock and FRB Stock

As of September 30, 2020, we held FHLB Stock and FRB Stock of \$81.8 million compared to \$68.3 million as of December 31, 2019. The Bank is a member of its regional FRB and of the FHLB system. FHLB members are required to own a

certain amount of stock based on the level of borrowings and other factors, and may invest in additional amounts. Both FRB and FHLB stock are carried at cost, restricted for sale, and periodically evaluated for impairment based on ultimate recovery of par value. Both cash and stock dividends are reported as income. Other non-marketable equity securities are carried at their cost, which approximates fair value.

### *Debt Securities*

We use our debt securities portfolio, which includes both available for sale and held to maturity debt securities, to provide a source of liquidity, provide an appropriate return on funds invested, manage interest rate risk, meet collateral requirements and meet regulatory capital requirements. As of September 30, 2020, the carrying amount of debt securities totaled \$1.1 billion, an increase of \$94.1 million, or 9.4%, compared to \$997.3 million as of December 31, 2019. The increase was primarily due to purchases of debt securities of \$491.7 million and net unrealized gains \$32.8 million, offset by sales of \$90.9 million and maturities, calls, and paydowns of \$339.9 million. Debt securities represented 12.5% and 12.5% of total assets as of September 30, 2020 and December 31, 2019, respectively.

All of our mortgage-backed securities and collateralized mortgage obligations are issued and/or guaranteed by U.S. government agencies or U.S. government-sponsored entities. We do not hold any Fannie Mae or Freddie Mac preferred stock, corporate equity, collateralized debt obligations, collateralized loan obligations, structured investment vehicles, private label collateralized mortgage obligations, subprime, Alt-A, or second lien elements in our investment portfolio. As of September 30, 2020, our investment portfolio did not contain any securities that are directly backed by subprime or Alt-A mortgages.

Management evaluates available for sale debt securities in unrealized loss positions to determine whether the impairment is due to credit-related factors or noncredit-related factors. Consideration is given to (1) the extent to which the fair value is less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the security for a period of time sufficient to allow for any anticipated recovery in fair value. As of September 30, 2020, management believes that available for sale securities in a unrealized loss position are due to noncredit-related factors, including changes in interest rates and other market conditions, and therefore no allowance for credit losses have been recognized in the Company's condensed consolidated balance sheets. The Company also recorded no allowance for credit losses for its held to maturity debt securities as of September 30, 2020.

As of September 30, 2020 and December 31, 2019, we did not own securities of any one issuer other than U.S. government agency securities for which aggregate cost exceeded 10.0% of our stockholders' equity as of such respective dates.

### *Deposits*

Total deposits as of September 30, 2020 were \$6.2 billion, an increase of \$328.2 million, or 5.6%, compared to \$5.9 billion as of December 31, 2019. The increase from December 31, 2019 was primarily the result of increases of \$167.0 million and \$364.2 million in interest-bearing transaction and savings deposits and noninterest-bearing demand deposits, respectively, partially offset by a decrease in certificates and other time deposits of \$203.0 million.

### *Borrowings*

We utilize short-term and long-term borrowings to supplement deposits to fund our lending and investment activities, each of which is discussed below.

### *Subordinated Debentures and Subordinated Notes*

*Subordinated Notes* - In connection with our acquisition of Green, on January 1, 2019, we assumed \$35.0 million of 8.50% Fixed-to-Floating Rate Subordinated Notes (the "Fixed-to-Floating Notes") that mature on December 15, 2026. The Fixed-to-Floating Notes, which qualify as Tier 2 capital under the Federal Reserve's capital guidelines, have an interest rate of 8.50% per annum during the fixed-rate period from date of issuance through December 15, 2021. Interest is payable semi-annually on each June 15 and December 15 through December 15, 2021.

During the floating rate period from December 15, 2021, to but excluding the maturity date or date of earlier redemption, the Fixed-to-Floating Notes will bear interest at a rate per annum equal to three-month LIBOR for the related interest period plus 6.685%, payable quarterly on each March 15, June 15, September 15 and December 15. The Fixed-to-Floating Notes are subordinated in right of payment to all of our senior indebtedness and effectively subordinated to all existing and future debt and all other liabilities of the Bank. We may elect to redeem the Fixed-to-Floating Notes (subject to regulatory approval), in whole or in part, on any early redemption date, which is any interest payment date on or after December 15, 2021 at a redemption price equal to 100% of the principal amount plus any accrued and unpaid interest. We may also redeem (subject to regulatory approval), in whole but not in part, the Fixed-to Floating Notes prior to an early redemption date upon the occurrence of certain events at a redemption price equal to 100% of the principal amount plus any accrued and unpaid interest. Other than on an early redemption date, the Fixed-to-Floating Notes cannot be accelerated except in the event of bankruptcy or the occurrence of certain other events of bankruptcy, insolvency or reorganization.

A summary of pertinent information related to our issues of subordinated notes outstanding at the dates indicated is set forth in the table below:

	September 30, 2020	December 31, 2019
	(In thousands)	
Subordinated notes	\$ 110,000	\$ 114,878
Unamortized debt premium	1,298	2,081
Debt issuance costs	(1,329)	(1,411)
Total subordinated notes	<u>\$ 109,969</u>	<u>\$ 115,548</u>

We are currently monitoring the actions of LIBOR's regulator and the implementation of alternative reference rates in advance of the expected discontinuation of LIBOR after 2021 to determine any potential impact on the subordinated notes.

*Subordinated Debentures Trust Preferred Securities.* The following subordinated debentures trust preferred securities were outstanding at the dates indicated in the table below:

	September 30, 2020	December 31, 2019
	(In thousands)	
Subordinated debentures	\$ 33,868	\$ 33,868
Debt discount	(3,679)	(3,845)
Total subordinated debentures	<u>\$ 30,189</u>	<u>\$ 30,023</u>

A summary of pertinent information related to our issues of subordinated debentures outstanding at September 30, 2020 is set forth in the table below:

Description	Subordinated Debt Owed to Trusts	Interest Rate <sup>(1)</sup> (Dollars in thousands)	Maturity Date
Parkway National Capital Trust I	\$ 3,093	3-month LIBOR +1.85%	December 2036
SovDallas Capital Trust I	8,609	3-month LIBOR +4.0%	July 2038
Patriot Bancshares Capital Trust I	5,155	3-month LIBOR +1.85%, not to exceed 11.90%	April 7, 2036
Patriot Bancshares Capital Trust II	17,011	3-month LIBOR +1.80%, not to exceed 11.90%	September 15, 2037
<b>Total subordinated debentures</b>	<b>\$ 33,868</b>		

<sup>(1)</sup> The 3-month LIBOR in effect as of September 30, 2020 was 0.2%.

Each of the trusts is a capital trust organized for the sole purpose of issuing trust securities and investing the proceeds in our junior subordinated debentures. The preferred trust securities of each trust represent preferred beneficial interests in the assets of the respective trusts and are subject to mandatory redemption upon payment of the junior subordinated debentures held by the trust. The common securities of each trust are wholly owned by us. Each trust's ability to pay amounts due on the trust preferred securities is solely dependent upon our making payment on the related junior subordinated debentures. The debentures, which are the only assets of each trust, are subordinate and junior in right of payment to all of our present and future senior indebtedness. We have fully and unconditionally guaranteed each trust's obligations under the trust securities issued by such trust to the extent not paid or made by each trust, provided such trust has funds available for such obligations.

Under the provisions of each issue of the debentures, we have the right to defer payment of interest on the debentures at any time, or from time to time, for periods not exceeding five years. If interest payments on either issue of the debentures are deferred, the distributions on the applicable trust preferred securities and common securities will also be deferred.

We are currently monitoring the actions of LIBOR's regulator and the implementation of alternative reference rates in advance of the expected discontinuation of LIBOR after 2021 to determine any potential impact on the subordinated notes.

#### *FHLB Advances*

The FHLB allows us to borrow on a blanket floating lien status collateralized by certain securities and loans. As of each of September 30, 2020 and December 31, 2019, total borrowing capacity of \$322.9 million and \$752.7 million, respectively, was available under this arrangement and \$1.1 billion and \$677.9 million, respectively, was outstanding with a weighted average interest rate of 0.993% for the nine months ended September 30, 2020 and 1.99% for the year ended December 31, 2019. FHLB has also issued standby letters of credit to the Company for \$557.9 million and \$481.7 million as of each of September 30, 2020 and December 31, 2019, respectively. Our current FHLB advances mature within fifteen years. Other than FHLB borrowings, we had no other short-term borrowings at the dates indicated.

#### *Federal Reserve Bank of Dallas.*

The Federal Reserve Bank of Dallas has an available borrower in custody arrangement, which allows us to borrow on a collateralized basis. Certain securities and commercial and consumer loans are pledged under this arrangement. We maintain this borrowing arrangement to meet liquidity needs pursuant to our contingency funding plan. As of September 30, 2020 and December 31, 2019, \$729.0 million and \$843.9 million, respectively, were available under this arrangement based on collateral values of pledged commercial and consumer loans. As of September 30, 2020 and December 31, 2019, no borrowings were outstanding under this arrangement.

## Liquidity and Capital Resources

### Liquidity

Liquidity involves our ability to raise funds to support asset growth and acquisitions or reduce assets to meet deposit withdrawals and other payment obligations, to maintain reserve requirements and otherwise to operate on an ongoing basis and manage unexpected events. For the nine months ended September 30, 2020 and the year ended December 31, 2019, our liquidity needs were primarily met by core deposits, wholesale borrowings, security and loan maturities and amortizing investment and loan portfolios. Use of brokered deposits, purchased funds from correspondent banks and overnight advances from the FHLB and the Federal Reserve Bank are available and have been utilized to take advantage of the cost of these funding sources. We maintained five lines of credit with commercial banks that provide for extensions of credit with an availability to borrow up to an aggregate of \$175.0 million and \$150.0 million as of September 30, 2020 and December 31, 2019, respectively. There were no advances under these lines of credit outstanding as of September 30, 2020 and December 31, 2019.

In addition, \$407.5 million was available in conjunction with the Paycheck Protection Program Liquidity Facility ("PPPLF") which is a lending facility offered by the FRB to facilitate lending to small businesses under the PPP. As of September 30, 2020, we have not utilized the PPPLF.

The following table illustrates, during the periods presented, the mix of our funding sources and the average assets in which those funds are invested as a percentage of our average total assets for the period indicated. Average assets totaled \$8.4 billion for the nine months ended September 30, 2020 and \$8.0 billion for the year ended December 31, 2019.

	For the Nine Months Ended September 30, 2020	For the Year Ended December 31, 2019
<b>Sources of Funds:</b>		
Deposits:		
Noninterest-bearing	20.9 %	18.6 %
Interest-bearing	31.7	33.3
Certificates and other time deposits	18.7	25.1
Advances from FHLB	12.7	6.3
Other borrowings	1.7	1.1
Other liabilities	0.6	0.6
Stockholders' equity	13.7	15.0
Total	<u>100.0 %</u>	<u>100.0 %</u>
<b>Uses of Funds:</b>		
Loans	73.7 %	73.6 %
Securities available-for-sale	12.7	12.3
Interest-bearing deposits in other banks	3.3	0.8
Other noninterest-earning assets	10.2	13.3
Total	<u>99.9 %</u>	<u>100.0 %</u>
Average noninterest-bearing deposits to average deposits	29.3 %	35.9 %
Average loans to average deposits	104.5 %	96.1 %
Average loans, excluding PPP and MW, to average deposits	96.0 %	93.4 %

Our primary source of funds is deposits, and our primary use of funds is loans. We do not expect a change in the primary source or use of our funds in the foreseeable future. Our average loans held for investment increased 6.9% for the nine months ended September 30, 2020 compared to the year ended December 31, 2019. We invest excess deposits in interest-bearing deposits at other banks, the Federal Reserve or liquid investments securities until these monies are needed to fund loan growth.

As of September 30, 2020, we had \$2.1 billion in outstanding commitments to extend credit, \$280.4 million in unconditionally cancellable mortgage warehouse commitments and \$43.4 million in commitments associated with outstanding standby and commercial letters of credit. As of December 31, 2019, we had \$1.7 billion in outstanding commitments to extend credit, \$205.4 million in mortgage warehouse commitments and \$27.2 million in commitments associated with outstanding standby and commercial letters of credit. Since commitments associated with letters of credit and commitments to extend credit may expire unused, the total outstanding may not necessarily reflect the actual future cash funding requirements.

As of September 30, 2020, we had cash and cash equivalents of \$128.8 million compared to \$251.6 million as of December 31, 2019.

#### *Analysis of Cash Flows*

	For the Nine Months Ended September 30, 2020	For the Nine Months Ended September 30, 2019
(In thousands)		
Net cash provided by operating activities	\$ 93,886	\$ 75,502
Net cash used in investing activities	(870,218)	(40,806)
Net cash provided by financing activities	653,549	133,447
Net change in cash and cash equivalents	<u>\$ (122,783)</u>	<u>\$ 168,143</u>

#### *Cash Flows Provided by Operating Activities*

For the nine months ended September 30, 2020, net cash provided by operating activities increased by \$18.4 million when compared to the same period in 2019. The increase in cash from operating activities was primarily related to the Company having no merger and acquisition expenses in the nine months ended September 30, 2020 as compared to \$38.0 million of merger and acquisition expenses in the nine months ending September 30, 2019.

#### *Cash Flows Used in Investing Activities*

For the nine months ended September 30, 2020, net cash used in investing activities increased by \$829.4 million when compared to the same period in 2019. The increase in cash used in investing activities was primarily attributable to a \$739.1 million increase in originations of net loans held for investment and \$112.7 million of cash received in excess of cash paid for the acquisition of Green during 2019 with no corresponding cash received in excess of cash paid in 2020 for the nine months ending September 30, 2019, slightly offset by \$248.1 million increase of maturities of securities available for sale.

#### *Cash Flows Provided by Financing Activities*

For the nine months ended September 30, 2020, net cash provided by financing activities increased by \$520.1 million when compared to the same period in 2019. The increase in cash provided by financing activities was primarily attributable to a \$542.0 million increase in deposits and a decrease in share repurchases of \$9.2 million, slightly offset by a \$20.0 million decrease in advances from the FHLB for the nine months ending September 30, 2019.

As of the nine months ended September 30, 2020 and 2019, we had no exposure to future cash requirements associated with known uncertainties or capital expenditures of a material nature.

#### *Share Repurchases*

On January 28, 2019, the Company's Board of Directors (the "Board") originally authorized a stock buyback program (the "Stock Buyback Program") pursuant to which the Company could, from time to time, purchase up to \$50 million of its outstanding common stock in the aggregate. The Board authorized increases of \$50 million on September 3, 2019 and \$75 million on December 12, 2019, resulting in an aggregate authorization to purchase up to \$175 million under the Stock Buyback Program. The Board also authorized an extension of the original expiration date of the Stock Buyback Program from December 31, 2019 to December 31, 2020 and recently authorized a further extension to March 31, 2021. The shares may be repurchased in the open market or in privately negotiated transactions from time to time, depending upon market conditions and other factors, and in accordance with applicable regulations of the Securities and Exchange Commission ("SEC"). The Stock

Buyback Program does not obligate the Company to purchase any shares, and the program may be terminated or amended by the Board at any time prior to its expiration. On March 16, 2020, Veritex suspended its stock buyback program.

During the nine months ended September 30, 2020, 2,002,211 shares were repurchased through the Stock Buyback Program and held as treasury stock at an average price of \$24.78. All of these shares were purchased prior to the suspension of the Stock Buyback Program in March 2020. During the nine months ended September 30, 2019, 2,349,103 shares were repurchased through the Stock Buyback Program and held as treasury stock at an average price of \$25.03.

On October 27, 2020, the Board authorized an extension to the expiration date of the Stock Buyback Program from December 31, 2020 to March 31, 2021.

#### Capital Resources

Total stockholders' equity decreased to \$1.2 billion as of September 30, 2020, compared to \$1.191 billion as of December 31, 2019, a decrease of \$5.5 million, or 0.5%. The decrease from December 31, 2019 to September 30, 2020 was primarily the result of \$49.6 million in stock buybacks, \$25.8 million in dividends declared and paid and \$15.5 million in CECL transition during the nine months ended September 30, 2020.

By comparison, total stockholders' equity increased to \$1.2 billion as of September 30, 2019, compared to \$530.6 million as of December 31, 2018, an increase of \$674.9 million, or 127.2%. The increase from December 31, 2018 to September 30, 2019 was primarily the result of the acquisition of Green, net income of \$61.7 million and \$58.8 million in stock buybacks during the nine months ended September 30, 2019.

Capital management consists of providing equity to support our current and future operations. The bank regulators view capital levels as important indicators of an institution's financial soundness. As a general matter, FDIC-insured depository institutions and their holding companies are required to maintain minimum capital relative to the amount and types of assets they hold. We are subject to regulatory capital requirements at the bank holding company and bank levels. See Note 12 – "Capital Requirements and Restrictions on Retained Earnings" in the notes to our condensed consolidated financial statements for additional discussion regarding the regulatory capital requirements applicable to us and the Bank. As of September 30, 2020 and December 31, 2019, the Company and the Bank were in compliance with all applicable regulatory capital requirements, and the Bank was classified as "well capitalized" for purposes of the prompt corrective action regulations. As we employ our capital and continue to grow our operations, our regulatory capital levels may decrease depending on our level of earnings. However, we expect to monitor and control our growth in order to remain in compliance with all regulatory capital standards applicable to us.

The following table presents the actual capital amounts and regulatory capital ratios for us and the Bank as of the dates indicated.

	As of September 30, 2020		As of December 31, 2019	
	Amount	Ratio	Amount	Ratio
(Dollars in thousands)				
<b>Veritex Holdings, Inc.</b>				
Total capital (to risk-weighted assets)	\$ 980,761	12.70 %	\$ 917,939	13.10 %
Tier 1 capital (to risk-weighted assets)	776,108	10.05	771,679	11.02
Common equity tier 1 (to risk-weighted assets)	746,937	9.67	742,675	10.60
Tier 1 capital (to average assets)	776,108	9.54	771,679	10.17
<b>Veritex Community Bank</b>				
Total capital (to risk-weighted assets)	\$ 954,317	12.37 %	\$ 870,838	12.44 %
Tier 1 capital (to risk-weighted assets)	859,634	11.14	840,126	12.00
Common equity tier 1 (to risk-weighted assets)	859,634	11.14	840,126	12.00
Tier 1 capital (to average assets)	859,634	10.57	840,126	11.07

### *Contractual Obligations*

In the ordinary course of the Company's operations, the Company enters into certain contractual obligations, such as future cash payments associated with its contractual obligations pursuant to its FHLB advance, non-cancelable future operating leases and qualified affordable housing investment and other borrowed funds. The Company believes that it will be able to meet its contractual obligations as they come due through the maintenance of adequate cash levels. The Company expects to maintain adequate cash levels through profitability, loan and securities repayment and maturity activity and continued deposit gathering activities. The Company has in place various borrowing mechanisms for both short-term and long-term liquidity needs.

Other than normal changes in the ordinary course of business and changes discussed within "Financial Condition—Borrowings," there have been no significant changes in the types of contractual obligations or amounts due as of September 30, 2020 since December 31, 2019 as reported in our Annual Report on Form 10-K for the year ended December 31, 2019.

### *Off-Balance Sheet Items*

In the normal course of business, the Company enters into various transactions, which, in accordance with GAAP, are not included in its condensed consolidated balance sheets. However, the Company has only limited off-balance sheet arrangements that have, or are reasonably likely to have, a current or future material effect on the Company's financial condition, revenues, expenses, results of operations, liquidity, capital expenditures or capital resources. The Company enters into these transactions to meet the financing needs of its customers. These transactions include commitments to extend credit and issue standby letters of credit, which involve, to varying degrees, elements of credit risk and interest rate risk in excess of the amounts recognized in the condensed consolidated balance sheets.

The Company's commitments to extend credit, mortgage warehouse commitments and outstanding standby letters of credit were \$2.1 billion, \$280.4 million and \$43.4 million, respectively, as of September 30, 2020. Since commitments associated with letters of credit and commitments to extend credit may expire unused, the amounts shown do not necessarily reflect the actual future cash funding requirements. The Company manages the Company's liquidity in light of the aggregate amounts of commitments to extend credit and outstanding standby letters of credit in effect from time to time to ensure that the Company will have adequate sources of liquidity to fund such commitments and honor drafts under such letters of credit.

### *Commitments to Extend Credit*

The Company enters into contractual commitments to extend credit, normally with fixed expiration dates or termination clauses, at specified rates and for specific purposes. Substantially all of the Company's commitments to extend credit are contingent upon customers maintaining specific credit standards at the time of loan funding. The Company minimizes its exposure to loss under these commitments by subjecting them to credit approval and monitoring procedures.

### *Mortgage warehouse commitments*

Mortgage warehouse commitments are unconditionally cancellable and represent the unused capacity on mortgage warehouse facilities the Company has approved. The Company reserves the right to refuse to buy any mortgage loans offered for sale by a customer, for any reason, at the Company's sole and absolute discretion.

### *Standby Letters of Credit*

Standby letters of credit are written conditional commitments that the Company issues 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, the Company would be required to fund the commitment. The maximum potential amount of future payments the Company could be required to make is represented by the contractual amount of the commitment. If the commitment is funded, the customer is obligated to reimburse the Company for the amount paid under this standby letter of credit.

### *Impact of Inflation*

Our condensed consolidated financial statements and related notes included elsewhere herein have been prepared in accordance with GAAP. These require the measurement of financial position and operating results in terms of historical dollars, without considering changes in the relative value of money over time due to inflation or recession.



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

#### *Subsequent Events*

On October 27, 2020, we announced that our Board of Directors declared a regular cash dividend of \$0.17 per share on our outstanding common stock, payable on or after November 19, 2020 to shareholders of record as of November 5, 2020.

Also on October 27, 2020, the Board authorized an extension to the expiration date of the Stock Buyback Program from December 31, 2020 to March 31, 2021.

On October 5, 2020, the Company completed the issuance and sale of \$125.0 million in aggregate principal amount of its 4.125% Fixed-to-Floating Rate Subordinated Notes (the "Subordinated Notes") due in 2030. The Subordinated Notes will bear interest: (i) from and including the date of issuance to, but excluding, October 15, 2025, at a rate of 4.125% per year and (ii) from and including October 15, 2025 to, but excluding, the maturity date (unless redeemed prior to such date), at a floating rate per year equal to the Benchmark (which is expected to be Three-Month Term Secured Overnight Funding Rate) plus 399.5 basis points. The Company has the right, subject to certain circumstances and the receipt of any required approval of the Federal Reserve Board, to redeem the Subordinated Notes at the Company's option, in whole or in part, on any interest payment date on or after October 15, 2025. The Company intends to use the net proceeds from the offering of Subordinated Notes for general corporate purposes, including the potential repayment of outstanding indebtedness, and supporting capital levels of the Bank.

#### *LIBOR Transition*

On July 27, 2017, the Financial Conduct Authority of the United Kingdom ("FCA"), which regulates the London Interbank Offered Rate ("LIBOR"), announced that it will no longer persuade or require banks to submit rates for the calculation of LIBOR after 2021. Given LIBOR's extensive use across financial markets, the transition away from LIBOR presents various risks and challenges to financial markets and institutions, including to the Company. The Company's commercial and consumer businesses issue, trade and hold various products that are currently indexed to LIBOR. As of September 30, 2020, the Company had approximately \$1.4 billion of loans indexed to LIBOR that mature after 2021. The Company's products that are indexed to LIBOR are significant, and if not sufficiently planned for, the discontinuation of LIBOR could result in financial, operational, legal, reputational or compliance risks to the Company.

The Alternative Reference Rates Committee ("ARRC") has proposed the Secured Overnight Financing Rate ("SOFR") as its preferred rate as an alternative to LIBOR. In 2019 and 2020, the ARRC released final recommended fallback contract language for new issuances of LIBOR indexed bilateral business loans, syndicated loans, floating rate notes, securitizations, and adjustable rate mortgage loans and private student loans. The ARRC also has published other recommendations relating to the spread adjustment between LIBOR and SOFR and other transition matters. The International Swaps and Derivatives Association, Inc. released fallback provisions for derivative instruments in October that will take effect in January 2021 where the parties have agreed to adhere to the ISDA language.

Due to the uncertainty surrounding the future of LIBOR, it is expected that the transition will span several reporting periods through the end of 2021. One of the major identified risks is inadequate fallback language in various existing instruments' contracts that may result in issues establishing the alternative index and adjusting the margin as applicable. The Company continues to monitor this activity and evaluate the related risks to its business.

## Critical Accounting Policies

Our accounting policies are fundamental to understanding our management's discussion and analysis of our results of operations and financial condition. We have identified certain significant accounting policies that 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 loans and allowance for credit losses, business combinations, investment securities, and loans held for sale. On January 1, 2020, we adopted ASU 2016-13, *Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments* ("ASU 2016-13"). The impact of adopting this standard resulted in an increase in our allowance for credit losses of \$39.1 million. Since December 31, 2019, there have been no other changes in critical accounting policies as described under "Management's Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies" in our Annual Report on Form 10-K for the year ended December 31, 2019, except for those updates discussed in Note 1 - "Summary of Significant Accounting Policies" in the accompanying notes to the condensed consolidated financial statements included in this report.

### Goodwill

Goodwill resulting from a business combination represents the excess of the fair value of the consideration transferred over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill is not amortized but is reviewed for potential impairment annually on October 31 of each fiscal year or when a triggering event occurs.

We may first assess qualitative factors to determine whether it is more likely than not (that is, a likelihood of more than 50%) that the fair value of a reporting unit is less than its carrying amount, including goodwill. We have an unconditional option to bypass the qualitative assessment for any reporting unit in any period and proceed directly to performing the quantitative goodwill impairment test, and we may resume performing the qualitative assessment in any subsequent period. If we determine that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, then we perform the quantitative goodwill impairment test. The quantitative goodwill impairment test, used to identify both the existence of potential impairment and the amount of impairment loss, involves estimating the fair value of a reporting unit and comparing these estimated fair values with its carrying amount. If the carrying amount of a reporting unit exceeds its fair value, an impairment loss shall be recognized in an amount equal to that excess, limited to the total amount of goodwill allocated to that reporting unit. Any such adjustments to goodwill are reflected in the results of operations in the periods in which they become known.

Estimating the fair values of a reporting unit involves the use of significant assumptions, estimates and judgments with respect to a variety of factors, including revenues, capital expenditures, cash flows and the selection and use of an appropriate discount rate and market values and multiples of earnings and revenues of similar public companies. Projected sales and capital expenditures are based on our annual business plan or other forecasted results. Discount rates reflect market-based estimates of the risks associated with the projected cash flows of the reporting unit.

The use of different assumptions, estimates or judgments in the goodwill impairment testing process, including with respect to the estimated future cash flows of our reporting unit, the discount rate used to discount such estimated cash flows to their net present value, and the reasonableness of the resultant implied control premium relative to our market capitalization, could materially increase or decrease the fair value of the reporting unit and/or its net assets and, accordingly, could materially increase or decrease any related impairment charge.

During the second quarter of 2020, the Company observed a sustained decline in the market valuation of the Company's common stock as a result of continued economic disruption occurring after the first quarter of 2020 primarily due to the COVID-19 pandemic. As a result, the Company determined that it was more likely than not that the fair value of the Company's sole reporting unit was below its carrying value and proceeded to perform an interim quantitative impairment test. The Company determined the fair value of its reporting unit using a combination of a market and an income approach. Upon completion of quantitative evaluation, the Company determined that, as of June 30, 2020, the fair value of the Company's reporting unit exceeded its related carrying value, and therefore goodwill was not impaired. However, changing economic conditions that may adversely affect the Company's performance, the fair value of its assets and liabilities, or its stock price could result in future impairment, which could adversely affect earnings in future periods. During the third quarter of 2020, the Company determined that there was no triggering event that required an interim quantitative impairment assessment to determine if it was more likely than not that the fair value of the Company's sole reporting unit was below its carrying value. Management will continue to monitor events that could impact this conclusion in the future.

## Special Cautionary Notice Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q includes “forward-looking statements” within the meaning of Private Securities Litigation Reform Act of 1995. Forward-looking statements are based on various facts and derived utilizing assumptions, current expectations, estimates and projections and are subject to known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Forward-looking statements include, without limitation, statements relating to the expected payment date of our quarterly cash dividend, impact of certain changes in our accounting policies, standards and interpretations, the effects of the COVID-19 pandemic and actions taken in response thereto, our future financial performance, business and growth strategy, projected plans and objectives, as well as other projections based on macroeconomic and industry trends, which are inherently unreliable due to the multiple factors that impact broader economic and industry trends, and any such variations may be material. Statements preceded by, followed by or that otherwise include the words “believes,” “expects,” “anticipates,” “intends,” “projects,” “estimates,” “plans” and similar expressions or future or conditional verbs such as “will,” “should,” “would,” “may” and “could” are generally forward-looking in nature and not historical facts, although not all forward-looking statements include the foregoing words. You should understand that the following important factors could affect our future results and cause actual results to differ materially from those expressed in the forward-looking statements:

- risks related to the concentration of our business in Texas, and specifically within the Dallas-Fort Worth metroplex and the Houston metropolitan area, including risks associated with any downturn in the real estate sector and risks associated with a decline in the values of single family homes in the Dallas-Fort Worth metroplex and the Houston metropolitan area;
- uncertain market conditions and economic trends nationally, regionally and particularly in the Dallas-Fort Worth metroplex and Texas, including as a result of the COVID-19 pandemic
- risks related to the impact of the COVID-19 pandemic on our business and operations
- possible additional loan losses and impairment of the collectibility of loans, particularly as a result of the COVID-19 pandemic and the programs implemented by the CARES Act, including its automatic loan forbearance provisions, and our PPP lending activities;
- the effects of regional or national civil unrest;
- changes in market interest rates that affect the pricing of our loans and deposits and our net interest income;
- risks related to our strategic focus on lending to small to medium-sized businesses;
- the sufficiency of the assumptions and estimates we make in establishing reserves for potential loan losses;
- our ability to implement our growth strategy, including identifying and consummating suitable acquisitions;
- our ability to recruit and retain successful bankers that meet our expectations in terms of customer relationships and profitability;
- changes in our accounting policies, standards and interpretations;
- our ability to retain executive officers and key employees and their customer and community relationships;
- risks associated with our commercial real estate and construction loan portfolios, including the risks inherent in the valuation of the collateral securing such loans;
- risks associated with our commercial loan portfolio, including the risk for deterioration in value of the general business assets that generally secure such loans;
- our level of nonperforming assets and the costs associated with resolving problem loans, if any, and complying with government-imposed foreclosure moratoriums;
- potential changes in the prices, values and sales volumes of commercial and residential real estate securing our real estate loans;
- risks related to the significant amount of credit that we have extended to a limited number of borrowers and in a limited geographic area;
- our ability to maintain adequate liquidity (including in compliance with the finalized Basel III capital standards and the effect of the transition to the CECL methodology for allowances and related adjustments) and to raise necessary capital to fund our acquisition strategy and operations or to meet increased minimum regulatory capital levels;
- potential fluctuations in the market value and liquidity of our investment securities;
- the effects of competition from a wide variety of local, regional, national and other providers of financial, investment and insurance services;
- our ability to maintain an effective system of disclosure controls and procedures and internal controls over financial reporting;

- risks associated with fraudulent and negligent acts by our customers, employees or vendors;
- our ability to keep pace with technological change or difficulties when implementing new technologies;
- risks associated with difficulties and/or terminations with third-party service providers and the services they provide;
- risks associated with unauthorized access, cyber-crime and other threats to data security;
- potential impairment on the goodwill we have recorded or may record in connection with business acquisitions;
- our ability to comply with various governmental and regulatory requirements applicable to financial institutions;
- the impact of recent and future legislative and regulatory changes, including changes in banking, securities and tax laws and regulations and their application by our regulators, and economic stimulus programs;
- uncertainty regarding the future of LIBOR and any replacement alternatives on our business;
- governmental monetary and fiscal policies, including the policies of the Federal Reserve;
- our ability to comply with supervisory actions by federal and state banking agencies;
- changes in the scope and cost of FDIC, insurance and other coverage; and
- systemic risks associated with the soundness of other financial institutions

Other factors not identified above, including those described under the headings “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” in our Annual Report on Form 10-K for the year ended December 31, 2019, as well as the information contained in this Quarterly Report on Form 10-Q, may also cause actual results to differ materially from those described in our forward-looking statements. Most of these factors are difficult to anticipate and are generally beyond our control. You should consider these factors in connection with considering any forward-looking statements that may be made by us. We undertake no obligation to release publicly any revisions to any forward-looking statements, to report events or to report the occurrence of unanticipated events unless we are required to do so by law.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

As a financial institution, our primary component of market risk is interest rate volatility. Our asset, liability and funds management policy provides management with the guidelines for effective funds management, and we have established a measurement system for monitoring our net interest rate sensitivity position. We manage our sensitivity position within our established guidelines.

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

We manage our exposure to interest rates by structuring our balance sheet in the ordinary course of business. We do not enter into instruments such as leveraged derivatives, interest rate swaps, financial options, financial future contracts or forward delivery contracts for the purpose of reducing interest rate risk. Based upon the nature of our operations, we are not subject to foreign exchange or commodity price risk. We do not own any trading assets.

Our exposure to interest rate risk is managed by the Asset-Liability Committee of the Bank in accordance with policies approved by its board of directors. The committee formulates strategies based on appropriate levels of interest rate risk. In determining the appropriate level of interest rate risk, the committee considers the impact on earnings and capital of the current outlook on interest rates, potential changes in interest rates, regional economies, liquidity, business strategies and other factors. The committee meets regularly to review, among other things, the sensitivity of assets and liabilities to interest rate changes, the book and market values of assets and liabilities, unrealized gains and losses, purchase and sale activities, commitments to originate loans and the maturities of investments and borrowings. Additionally, the committee reviews liquidity, cash flow flexibility, maturities of deposits and consumer and commercial deposit activity. Management employs methodologies to manage interest rate risk, which include an analysis of relationships between interest-earning assets and interest-bearing liabilities, and an interest rate shock simulation model.

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

On a quarterly basis, we run two simulation models including a static balance sheet and dynamic growth balance sheet. These models test the impact on net interest income and fair value of equity from changes in market interest rates under various scenarios. Under the static and dynamic growth models, rates are shocked instantaneously and ramped rate changes over a 12-month horizon based upon parallel and non-parallel yield curve shifts. Parallel shock scenarios assume instantaneous parallel movements in the yield curve compared to a flat yield curve scenario. Non-parallel simulation involves analysis of interest income and expense under various changes in the shape of the yield curve. Internal policy regarding internal rate risk simulations currently specifies that for instantaneous parallel shifts of the yield curve, estimated net interest income at risk for the subsequent one-year period should not decline by more than 12.5% for a 100 basis point shift, 15.0% for a 200 basis point shift, and 20.0% for a 300 basis point shift.

The following table summarizes the simulated change in net interest income and fair value of equity over a 12-month horizon as of the dates indicated:

Change in Interest Rates (Basis Points)	As of September 30, 2020		As of December 31, 2019	
	Percent Change in Net Interest Income	Percent Change in Fair Value of Equity	Percent Change in Net Interest Income	Percent Change in Fair Value of Equity
+ 300	16.77 %	16.28 %	14.51 %	12.01 %
+ 200	10.66 %	10.90 %	9.89 %	9.42 %
+ 100	4.83 %	5.11 %	5.17 %	5.76 %
Base	— %	— %	— %	— %
-100	(1.82)%	(4.36)%	(3.99)%	(8.03)%

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

#### Item 4. Controls and Procedures

*Evaluation of disclosure controls and procedures* — As of the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of its management, including its Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of its disclosure controls and procedures. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management was required to apply judgment in evaluating its controls and procedures. Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) were effective as of the end of the period covered by this Report.

There were no changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended September 30, 2020 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II. OTHER INFORMATION

### Item 1. Legal Proceedings

We are from time to time subject to claims and litigation arising in the ordinary course of business. These claims and litigation may include, among other things, allegations of violation of banking and other applicable regulations, competition law, labor laws and consumer protection laws, as well as claims or litigation relating to intellectual property, securities, breach of contract and tort. We intend to defend ourselves vigorously against any pending or future claims and litigation.

At this time, in the opinion of management, the likelihood is remote that the impact of such proceedings, either individually or in the aggregate, would have a material adverse effect on our consolidated results of operations, financial condition or cash flows. However, one or more unfavorable outcomes in any claim or litigation against us could have a material adverse effect for the period in which they are resolved. In addition, regardless of their merits or their ultimate outcomes, such matters are costly, divert management's attention and may materially adversely affect our reputation, even if resolved in our favor.

### Item 1A. Risk Factors

In evaluating an investment in our common stock, investors should consider carefully, among other things, the risk factors previously disclosed in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2019, as well as the information contained in this Quarterly Report on Form 10-Q and our other reports and registration statements filed with the SEC.

There has been no material change in the risk factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2019, with the exception of:

***The novel coronavirus ("COVID-19") and the impact of actions to mitigate it could have a material adverse effect on our business, financial condition and results of operations, and such effects will depend on future developments, which are highly uncertain and are difficult to predict.***

COVID-19 has led to federal, state and local governments enacting various restrictions in an attempt to limit the spread of the virus, including the declaration of a federal National Emergency; multiple cities' and states' declarations of states of emergency; school and business closings; limitations on social or public gatherings and other social distancing measures, such as working remotely, travel restrictions, quarantines and shelter in place orders. Such measures have significantly contributed to rising unemployment and reductions in consumer and business spending. Possible additional waves of COVID-19 and the uncertainty of the timing of a widely available vaccine may adversely affect the re-opening process.

In response to the economic and financial effects of COVID-19, the Federal Reserve has sharply reduced interest rates (which we expect will likely remain low for a considerable period) and instituted quantitative easing measures as well as domestic and global capital market support programs. In addition, the Trump Administration, Congress, various federal agencies and state governments have taken measures to address the economic and social consequences of the pandemic, including the passage of the CARES Act and the creation of the Main Street Lending Program. The CARES Act, among other things, provides certain measures to support individuals and businesses in maintaining solvency through monetary relief, including in the form of financing, loan forgiveness and automatic forbearance. Beginning in early April 2020, we began processing loan applications under the PPP created under the CARES Act. The Federal Reserve's Main Street Lending Program will offer deferred interest on 5-year loans to small and mid-sized businesses. Other banking regulatory agencies have encouraged lenders to extend additional loans, and the federal government is considering additional stimulus and support legislation focused on providing aid to various sectors, including small businesses. The full impact on our business activities as a result of new government and regulatory policies, programs and guidelines, as well as regulators' reactions to such activities, remains uncertain.

The economic effects of the COVID-19 outbreak have had a destabilizing effect on financial markets, key market indices and overall economic activity. The uncertainty regarding the duration of the pandemic and the resulting economic disruption has caused increased market volatility and may lead to an economic recession and/or a significant decrease in consumer confidence and business generally. The continuation of these conditions caused by the outbreak, including whether due to a resurgence or a second wave of COVID-19 infections, particularly as the geographic areas in which we operate open, and the uncertainty of the timing of a widely available vaccine, as well as the impacts of the CARES Act and other federal and

state measures, specifically with respect to loan forbearances, can be expected to adversely impact our businesses and results of operations and the operations of our borrowers, customers and business partners. In particular, these events can be expected to, among other things:

- impair the ability of borrowers to repay outstanding loans or other obligations, resulting in increases in delinquencies;
- impair the value of collateral securing loans (particularly with respect to real estate);
- impair the value of our securities portfolio;
- require an increase in our allowance for credit losses or unfunded commitments;
- adversely affect the stability of our deposit base, or otherwise impair our liquidity;
- result in a triggering event that could, under certain circumstances, cause us to perform a goodwill impairment test and result in an impairment charge being recorded;
- reduce our wealth management revenues and the demand for our products and services;
- result in increased compliance risk as we become subject to new regulatory and other requirements associated with the PPP and other new programs in which we participate;
- impair the ability of loan guarantors to honor commitments;
- negatively impact our regulatory capital ratios;
- negatively impact the productivity and availability of key personnel and other employees necessary to conduct our business, and of third-party service providers who perform critical services for us, or otherwise cause operational failures due to changes in our normal business practices necessitated by the outbreak and related governmental actions;
- increase cyber and payment fraud risk, given increased online and remote activity; and
- broadly result in lost revenue and income.

Prolonged measures by health or other governmental authorities encouraging or requiring significant restrictions on travel, assembly or other core business practices could further harm our business and those of our customers, in particular our small to medium-sized business customers. Although we have business continuity plans and other safeguards in place, there is no assurance that they will be effective.

Our results of operations have been adversely affected by the factors described above. For example, for the nine months ended September 30, 2020, these factors caused a substantial increase in our allowance for credit losses and related provision for credit losses. While the ultimate impact of these factors over the longer term is uncertain at this time and we do not yet know the full extent of the impacts on our business, our operations or the global economy as a whole, nor the pace of the economic recovery when the COVID-19 pandemic subsides. However, the decline in economic conditions generally and a prolonged negative impact on small to medium-sized businesses, in particular, due to COVID-19 is likely to result in a material adverse effect on our business, financial condition and results of operations and may heighten many of our known risks described in the “Risk Factors” section of our Annual Report on Form 10-K for the year ended December 31, 2019.

## **Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

On January 28, 2019, the Company's Board originally authorized the Stock Buyback Program pursuant to which the Company could, from time to time, purchase up to \$50 million of its outstanding common stock in the aggregate. The Board authorized increases of \$50 million on September 3, 2019 and \$75 million on December 12, 2019, resulting in an aggregate authorization to purchase up to \$175 million under the Stock Buyback Program. The Board also authorized an extension of the original expiration date of the Stock Buyback Program from December 31, 2019 to December 31, 2020. On October 27, 2020, the Board authorized an extension of the expiration date of the Stock Buyback Program from December 31, 2020, and recently authorized a further extension to March 31, 2021. The shares may be repurchased in the open market or in privately negotiated transactions from time to time, depending upon market conditions and other factors, and in accordance with applicable regulations of the SEC. The Stock Buyback Program does not obligate the Company to purchase any shares and may be terminated or amended by the Board at any time prior to its expiration date. The following repurchases were made under the Stock Buyback Program during the nine months ended September 30, 2020:

	(a)	(b)	(c)	(d)
Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs	Maximum number (or approximate dollar value) of shares that may yet be purchased under the plans or programs
January 1, 2020 - January 31, 2020	77,800	\$ 28.22	77,800	\$ 78,272,000
February 1, 2020 - February 28, 2020	1,052,506	27.89	1,052,506	48,912,000
March 1, 2020 - March 31, 2020	871,905	20.72	871,905	30,850,000
April 1, 2020 - April 30, 2020	—	—	—	30,850,000
May 1, 2020 - May 31, 2020	—	—	—	30,850,000
June 1, 2020 - June 30, 2020	—	—	—	30,850,000
July 1, 2020 - July 31, 2020	—	—	—	30,850,000
August 1, 2020 - August 31, 2020	—	—	—	30,850,000
September 1, 2020 - September 30, 2020	—	—	—	30,850,000
	2,002,211	\$ 24.78	2,002,211	\$ 30,850,000

**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Mine Safety Disclosures**

Not Applicable.

**Item 5. Other Information**

None.

**Item 6. Exhibits**



Exhibit Number	Description of Exhibit
<a href="#"><u>2.3</u></a>	<a href="#"><u>Agreement and Plan of Reorganization dated July 23, 2018, by and among Veritex Holdings, Inc., MustMS, Inc. and Green Bancorp, Inc. (incorporated by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K filed July 24, 2018).</u></a>
<a href="#"><u>3.1</u></a>	<a href="#"><u>Second Amended and Restated Certificate of Formation of Veritex Holdings, Inc. (incorporated by reference to Exhibit 3.1 to Amendment No. 1 to the Company's Registration Statement on Form S-1 filed September 22, 2014 (File No. 333-198484)).</u></a>
<a href="#"><u>3.2</u></a>	<a href="#"><u>Third Amended and Restated Bylaws of Veritex Holdings, Inc. (incorporated by reference to Exhibit 3.2 to the Company's Quarterly Report on Form 10-Q filed July 25, 2017).</u></a>
<a href="#"><u>3.3</u></a>	<a href="#"><u>Third Amended and Restated Bylaws of Veritex Holdings, Inc., marked to show amendments effective as of May 18, 2017 (incorporated by reference to Exhibit 3.3 to the Company's Quarterly Report on Form 10-Q filed July 25, 2017).</u></a>
<a href="#"><u>21.1*</u></a>	<a href="#"><u>Subsidiaries of Veritex Holdings, Inc.</u></a>
<a href="#"><u>31.1*</u></a>	<a href="#"><u>Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u></a>
<a href="#"><u>31.2*</u></a>	<a href="#"><u>Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u></a>
<a href="#"><u>32.1**</u></a>	<a href="#"><u>Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u></a>
<a href="#"><u>32.2**</u></a>	<a href="#"><u>Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u></a>
101*	The following materials from Veritex Holdings, Inc.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 2020, formatted in Inline XBRL (Inline eXtensible Business Reporting Language): (i) Cover Page, (ii) Condensed Consolidated Balance Sheets, (iii) Condensed Consolidated Statements of Income, (iv) Condensed Consolidated Statements of Comprehensive Income, (v) Condensed Consolidated Statements of Changes in Stockholders' Equity, (vi) Condensed Consolidated Statements of Cash Flows, and (vii) Notes to Condensed Consolidated Financial Statements.
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)

\* Filed with this Quarterly Report on Form 10-Q

\*\* Furnished with this Quarterly Report on Form 10-Q

## SIGNATURES

Pursuant to the requirements 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.

**VERITEX HOLDINGS, INC.**

(Registrant)

Date: November 4, 2020

/s/ C. Malcolm Holland, III

---

C. Malcolm Holland, III

Chairman and Chief Executive Officer

(Principal Executive Officer)

Date: November 4, 2020

/s/ Terry S. Earley

---

Terry S. Earley

Chief Financial Officer

(Principal Financial and Accounting Officer)

## CERTIFICATION

I, C. Malcolm Holland, III, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Veritex Holdings, Inc. for the quarter ended September 30, 2020;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 4, 2020

/S/ C. Malcolm Holland, III

C. Malcolm Holland, III

Chairman of the Board & Chief Executive Officer

## CERTIFICATION

I, Terry S. Earley, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Veritex Holdings, Inc. for the quarter ended September 30, 2020;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 4, 2020

/S/ Terry S. Earley

Terry S. Earley  
Chief Financial Officer

**CERTIFICATION**

In connection with the Quarterly Report on Form 10-Q of Veritex Holdings, Inc. (the “Company”) for the quarter ended September 30, 2020 (the “Report”), as filed with the Securities and Exchange Commission on the date hereof, I, C. Malcolm Holland, III, Chairman and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ C. Malcolm Holland, III

C. Malcolm Holland, III

Chairman of the Board & Chief Executive Officer

Date: November 4, 2020

**CERTIFICATION**

In connection with the Quarterly Report on Form 10-Q of Veritex Holdings, Inc. (the "Company") for the quarter ended September 30, 2020 (the "Report"), as filed with the Securities and Exchange Commission on the date hereof, I, Terry S. Earley, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/S/ Terry S. Earley

Terry S. Earley

Chief Financial Officer

Date: November 4, 2020

### Subsidiaries of the Registrant

The following is a list of the consolidated subsidiaries of Veritex Holdings, Inc., the names under which such subsidiaries do business and the state in which each was organized, as of September 30, 2020.

Name	Jurisdiction of Organization
Veritex Community Bank	Texas
Parkway National Trust I	Texas
SovDallas Capital Trust	Texas
Patriot Bancshares Capital Trust I	Texas
Patriot Bancshares Capital Trust II	Texas
8214 Westchester, LLC <sup>1</sup>	Texas
Patriot Bank Mortgage, Inc. <sup>1</sup>	Texas
PB Commercial, LLC <sup>1</sup>	Texas
Potomac River Holdings, LLC <sup>1</sup>	Texas
PKDAH, LLC <sup>1</sup>	Texas
VB Acquisition Sub No. 1, LLC <sup>1</sup>	Texas
VB Acquisition Sub No. 2, LLC <sup>1</sup>	Texas
VB Acquisition Sub No. 3, LLC <sup>1</sup>	Texas
VB Sub 5, LLC <sup>1</sup>	Texas

<sup>1</sup> Subsidiary of Veritex Community Bank.